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Focus

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FEATURE COMMENT: Supreme Interest: Cases Pending At The Supreme Court Could Change The Scope Of FCA Litigation

The ongoing rise of False Claims Act cases and news stories regarding massive settlements resulting from them continue to earn the attention of those who do business with the Government, including health care providers and Government contractors. In part, the FCA's increased utilization stems from a lack of uniform framework for courts to use when interpreting and applying the Act. The results are startling. The Justice Department has collected over $3.5 billion from FCA cases in each of the last four years, and 638 qui tam actions were filed by relators in fiscal year 2015, compared to just 30 actions filed in FY 1987.

Yet while FCA cases are becoming more prevalent, the law has become less, not more, clear. Issues regarding implied certification, the applicable scienter standard, the consequences of breaching the FCA's seal requirement, and the application of Rule 9(b) at the pleading stage have all split lower courts. And the U.S. Supreme Court has started to take notice. In the upcoming term, the Court has the opportunity to bring clarity to the FCA in three different cases that address these issues, and each will be closely watched. *U.S. ex rel. Escobar v Universal Health Servs., Inc.*, 780 F.3d 504 (1st Cir.), cert. granted in part, 136 S. Ct. 582 (2015); *U.S. ex rel. Rigsby v. State Farm Fire & Cas. Co.*, 794 F.3d 457 (5th Cir. 2015); *U.S. ex rel. Heath v. AT&T, Inc.*, 791 F.3d 112 (D.C. Cir. 2015).

***Escobar* and the Viability of the Implied Certification Doctrine**—For years, courts have struggled to apply a consistent framework in FCA cases that allege legally false, as opposed to factually false, claims. Often a complaint asserts factually false claims by alleging that a provider supplied an incorrect description of goods or services provided, or requested reimbursement for goods or services never provided. A complaint asserting legally false claims, on the other hand, often alleges that a claim for payment was submitted and a provider falsely certified compliance with some statute, regulation or contractual provision. Such theories of legal falsity under the FCA have become the focus of private relators and Government plaintiffs.

When alleging an FCA claim based on legal falsity, the key requirement is the provider's certification of compliance with an applicable statute or regulation. *U.S. ex rel. Spicer v. Westbrook*, 751 F.3d 354, 365 (5th Cir. 2014). Some courts, however, have not limited the requirement to express certifications of compliance. Instead, many relators have argued, and several lower courts have adopted the position, that even if a provider made no express statement of compliance with a particular statute, regulation or contractual provision, the provider may have impliedly certified compliance with the provision when it submitted claims for payment.

Courts have justified this "implied certification" theory by citing "Congress' expressly stated purpose that the Act include at least some kinds of legally false claims, and [] the Supreme Court's admonition that the Act intends to reach all forms of fraud that might cause financial loss to the government." *Mikes v. Straus*, 274 F.3d 687, 699 (2d Cir. 2001) (internal citations omitted). This implied certification doctrine has created both huge potential liability for defendants, and significant questions for courts. Fortunately, the Supreme Court recently agreed to decide a case that could help resolve the debate.

Various Circuit Views and the Opportunity to Clarify Implied Certification: Lower courts' treatment of the implied certification doctrine has varied by circuit. For instance, some circuits have accepted the implied certification theory and held that a re-

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quirement need not expressly be identified as a condition of payment. *U.S. ex rel. Hutcheson v. Blackstone Med., Inc.*, 647 F.3d 377, 387–88 (1st Cir. 2011); *U. S. v. Triple Canopy, Inc*., 775 F.3d 628, 636 (4th Cir. 2015); *U.S. v. Sci. Applications Int'l Corp*., 626 F.3d 1257, 1269 (D.C. Cir. 2010) (SAIC). These courts have found that a statute, regulation, or contractual requirement may constitute a condition of payment, and thus can lead to FCA liability, even if the requirement's text does not explicitly state it is a condition of payment.

For example, in *Escobar*, the relator argued to the First Circuit that a Massachusetts counseling services center presented false claims to Medicaid by failing to comply with state regulations requiring, among other things, that mental health centers employ individuals who are licensed in psychiatry, psychology, social work and psychiatric nursing, or are supervised by "a fully qualified professional staff member trained in one of [those] disciplines." 780 F.3d at 507 (citation omitted) (internal quotations omitted).

Although the district court dismissed the FCA claim because the state regulations, according to the district court, were mere "conditions of participation" in the Medicaid program and not conditions of payment, the First Circuit reversed. It held that although the particular state regulations did not expressly state they were conditions of payment, other state regulations made clear that compliance was a condition of payment, and FCA liability could flow from submitting claims for payment to the Medicaid program when the defendant was not in compliance with the state regulations.

"Preconditions of payment," the First Circuit held, "may be found in sources such as statutes, regulations, and contracts," and "need not be expressly designated. Rather, the question whether a given requirement constitutes a precondition to payment is a fact-intensive and context-specific inquiry involving a close reading of the foundational documents, or statutes and regulations, at issue." Id. at. 512 (internal citations and quotations omitted). See also *U.S. ex rel. Badr v. Triple Canopy, Inc.*, 775 F.3d 628, 636–38, n.5 (4th Cir. 2015) (recognizing implied certification doctrine and rejecting argument "that implied representations can give rise to liability only when the condition is expressly designated as a condition of payment").

Other circuits, including the Second and Sixth, have taken a "middle-ground" approach. While those courts recognize that a defendant might, in an appropriate case, impliedly certify compliance with a statute or regulation, FCA liability is possible only if the Government *expressly* conditions payment on compliance. *Mikes*, 274 F.3d at 701 (holding plaintiff's allegations cannot establish liability under the FCA because "the Medicare statute does not explicitly condition payment upon compliance"); *Chesbrough v. VPA, P.C*., 655 F.3d 461, 468 (6th Cir. 2011) (rejected implied certification claim because plaintiff did not allege that there was an "express[] require[ment] to comply with those standards as a prerequisite to payment of claims"). The Fifth Circuit has likewise recognized that if implied certification claims did exist, such claims would require that the Government expressly condition payment on compliance. *U.S. ex rel. Steury v. Cardinal Health, Inc.*, 625 F.3d 262 (5th Cir. 2010). For example, a regulation would have to state explicitly that the Government would not pay a provider who fails to comply in order to trigger FCA liability. A provider's mere noncompliance would not suffice. This middle-ground view provides greater protection to FCA defendants than those views that require no statement to find a condition of payment, but it still creates risk even if a provider has not expressly told the Government that it is complying with the particular requirement at issue.

In contrast, the Seventh Circuit seemingly rejected the implied certification doctrine in a recent case, stating that the concept lacked a "discerning limiting principle." *U.S. v. Sanford-Brown, Ltd.*, 788 F.3d 696, 711 (7th Cir. 2015). In *Sanford-Brown*, the relator worked at a for-profit university. He contended that the defendant violated, among others, participation agreement provisions that (a) prohibit paying incentive compensation to certain types of employees involved in admissions and recruiting, and (b) require universities to repay the Department of Education portions of payments for certain students who failed to complete at least 60 percent of a term.

When the U.S. declined to intervene, the relator proceeded with the suit and asserted an implied certification theory, contending that Sanford-Brown presented false claims for payment by breaching provisions of the agreement while simultaneously submitting claims for payment. Although the participation agreement does not state that compliance with the provisions is a condition of payment, the relator relied on the implied certification doctrine to allege that the defendant knowingly defrauded the Government. The defendant contended that the suit

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is more properly termed a breach of contract case, not one based in fraud.

The Seventh Circuit held that because compliance with all of the Title IV regulations in the participation agreement was merely a condition of continued participation in the program, rather than a condition of payment necessary to be eligible for subsidies, the defendant had not violated the FCA. The court examined other circuits' treatment of implied certification claims, including those where courts found certain legal requirements conditions of payment even when not expressly identified as conditions of payment, and explained, "[a]lthough a number of other circuits have adopted this so-called doctrine of implied false certification, we decline to join them ...." Id. at 711–12 (internal citation omitted). The Seventh Circuit cautioned against a situation where "any of the conditions in the [agreement] that are not met by the institution would have the potential to impose strict liability on it under the FCA." Id. at 711. Indeed, the court expressed particular concern that "thousands of pages of federal statutes and regulations" could be incorporated by reference into the participation agreement and thus create liability under the FCA. Id. The FCA, the court made clear, "is simply not the proper mechanism for government to enforce" compliance with any and every Government statute, regulation, and contract. Id. at 712.

However, the Seventh Circuit's opinion did provide possible fodder for some relators to argue that the court did not fully reject the implied certification theory. Although the court stated that it "decline[d] to join" other circuits who had adopted the implied certification theory, it also stated it was "join[ing] the Fifth Circuit." Id. at 711–12. But the Fifth Circuit has not yet ruled regarding whether it accepts the implied certification theory, as the complaints it has examined did not suffice even if it did allow implied certification claims. See, e.g., *U.S. ex rel. Steury v. Cardinal Health, Inc*., 735 F.3d 202 (5th Cir. 2013); *Steury*, 625 F.3d 262. In any event, the Seventh Circuit's approach avoids allowing aggressive relators to turn run-of-the-mill regulatory violations into FCA claims absent an express statement of compliance by the defendant.

The inconsistency of the circuits' treatment of implied certification claims has created an opportunity for the Supreme Court to provide clarification. The Court took advantage of this opportunity by granting certiorari in the *Escobar* case on two issues: (1) whether the "implied" certification theory of legal falsity under the FCA is viable; and (2) if an "implied certification" theory is viable, whether an FCA plaintiff must show that the defendant violated a statute, regulation or contractual provision that *expressly* states that it is a condition of payment.

Following the grant of certiorari, the U.S. recently filed its merits brief as amicus curiae, advocating for a broad reading of the FCA. The Government argues that "[j]udicial references to the 'implied certification' theory of FCA liability are best understood as shorthand for the established principle that a communication can be materially misleading, and can give rise to liability for fraudulent misrepresentation, if the requisite scienter is established, even though it contains no explicit false statement." Brief for the U.S. as Amicus Curiae Supporting Respondents, *Universal Health Servs., Inc. v. U.S. ex rel. Escobar* (No. 15-7).

The Government thus rejects numerous courts of appeals' holdings and contends that no condition of payment requirement exists for legally false claims. Instead, the Government argues that FCA liability can stand for a defendant who submits a claim for payment while in violation of *any* statute, regulation or contractual provision, so long as the provision is deemed "material" under the FCA's diluted definition of "material" and the defendant is acting "knowingly" (which includes reckless disregard). Id. Needless to say, if the Supreme Court were to adopt such an approach, potential liability could increase for many providers, Government contractors and others who conduct business with the Government.

***Rigsby* Provides Two Key FCA Questions—** Beyond *Escobar* and implied certification, the Supreme Court also recently requested the views of the solicitor general regarding a petition for certiorari pending in another FCA case before the Court, *State Farm v. U.S. ex rel. Rigsby*. Petition for Writ of Certiorari, *State Farm Fire & Casualty Co. v. U.S. ex rel. Rigsby* (No. 15-513). The case presents two key issues for the Court's consideration: (1) what standard determines dismissal for a relator's violation of the FCA's seal requirement, 31 USCA § 3730(b)(2); and (2) under what standard an organization can be deemed to have "knowingly" submitted a false claim "based on the purported collective knowledge or imputed ill intent of employees other than" the employee who chose to present the claim. Id. The request reflects the Court's interest in the topics, which may signal that the case could be taken.

Rigsby*'s Background*: The relators in *Rigsby* alleged that State Farm Fire and Casualty Co. submitted false

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claims to the U.S. Government for payment on flood insurance policies. Relators contended that following the massive damage to homes by Hurricane Katrina, State Farm fraudulently submitted to the U.S. a flood claim for payment, although the damage was caused by wind. In response, State Farm has argued that all three claims adjusters assigned to the particular claim shared a good faith belief that the home suffered flood damage, meaning they did not have the requisite intent for an FCA claim.

The relators' initial complaint was filed under seal on April 26, 2006, which was not lifted until Aug. 1, 2007. During that time, relators' counsel violated the FCA seal requirement by disclosing the complaint to several news outlets through e-mails and interviews, including e-mailing sealed evidence to ABC News to use for a 20/20 story. The district court found that these actions did not require dismissal of the case, and proceeded to trial.

At trial, the jury found for relators. On appeal, State Farm argued, among other things, that it could not have acted "knowingly" because the claims adjusters believed in good faith that the claim was based on flood damage, not wind damage, and any evidence of wind damage was developed only after the claims were submitted. The Fifth Circuit affirmed, and State Farm has sought certiorari from the Supreme Court.

The Seal Requirement: Under the FCA, a relator's complaint "shall be filed in camera, shall remain under seal for at least 60 days, and shall not be served on the defendant until the court so orders." 31 USCA § 3730(b)(2). This seal requirement allows the Government to investigate and determine whether to intervene, and it protects the defendant's reputation until further investigation is done. Despite uniform recognition of the important role this requirement plays in FCA claims, courts of appeals have differed regarding the consequence of violating the requirement.

Consequences for Violation of the Seal Requirement: The strictest view is that a violation of the FCA's seal requirement mandates dismissal. *U.S. ex rel. Summers v. LHC Grp., Inc.*, 623 F.3d 287, 298 (6th Cir. 2010). The Sixth Circuit explained that, "[g]iven that the very existence of the *qui tam* right to bring suit in the name of the Government is created by statute, it is particularly appropriate to have the right exist in a given case only with the preconditions that Congress deemed necessary for the purpose of safeguarding the Government's interests." Id. This rule provides a strong deterrent for potential violators, and offers the best protection to Government investigations and FCA defendants.

Other circuits, however, have held that dismissal is not automatic; instead, they have held that multiple factors must be evaluated. See *U.S. ex rel. Pilon v. Martin Marietta Corp.*, 60 F.3d 995 (2d Cir. 1995); *Smith v. Clark/Smoot/Russell*, 796 F.3d 424, 430 (4th Cir. 2015); *U.S. ex rel. Lujan v. Hughes Aircraft Co.*, 67 F.3d 242 (9th Cir. 1995). For example, the Second Circuit calls for a more general inquiry into whether the relator's actions "incurably frustrated" the interests served by the under-seal rule, which include shielding defendants from meritless lawsuits. *Pilon*, 60 F.3d at 996 (holding "[b]ecause this failure incurably frustrated the statutory purpose underlying these requirements, we agree that the complaint should have been dismissed"). The Ninth Circuit offers even less protection to defendants, as it uses a three-factor balancing test to evaluate whether dismissal is proper: (1) whether the disclosure actually harmed the Government; (2) the nature and severity of the violation (for example, disclosing underlying facts in general terms in a newspaper, a minor violation, versus completely failing to file the complaint under seal, a major violation); and (3) the presence or absence of bad faith or willfulness. *Lujan*, 67 F.3d at 245–46.

The Fifth Circuit's Approach: In *Rigsby*, the Fifth Circuit analyzed other circuits' approaches and adopted the view that "a seal violation does not automatically mandate dismissal." *Rigsby*, 794 F.3d at 471. The court embraced the Ninth Circuit's test and explained that "the 1986 amendments to the FCA were intended to encourage more, not fewer, private FCA actions. Holding that any violation of the seal requirement mandates dismissal would frustrate that purpose, particularly when the government suffers minimal or no harm from the violation." Id. After finding that the Government was not likely harmed by the disclosures to news organizations, the court held that the seal violation did not merit dismissal.

The balancing test adopted by the Fifth and Ninth circuits appears to treat the seal requirement as a mere suggestion, rather than as a text-based requirement of FCA litigation. As a practical matter, it often is difficult for FCA defendants to prove harm to the Government, particularly if the Government has a financial incentive not to weigh in on the issue.

What Does It Mean for an Organization to Act "Knowingly"?: The second question the Supreme

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Court may address in the *Rigsby* case is a key issue for FCA defendants: Can an organization be held liable for "knowingly" acting if the person who submits the claim for payment does so in good faith? Again, courts of appeals have taken various stances on the FCA's scienter requirement.

For instance, the D.C. Circuit and the Fourth Circuit have rejected a "collective knowledge" approach that would allow "a plaintiff to prove scienter by piecing together scraps of 'innocent' knowledge held by various corporate officials, even if those officials never had contact with each other or knew what others were doing in connection with a claim seeking government funds." *U.S. ex rel. Harrison v. Westinghouse Savannah River Co.*, 352 F.3d 908, 918, n.9 (4th Cir. 2003); *SAIC*, 626 F.3d at 1275. The *Rigsby* petitioner argues that the Fifth Circuit's approach stands in contrast, as the Fifth Circuit held that scienter was satisfied based on an alleged generalized intent of a group of employees.

Such a "collective knowledge" approach would ignore the fact that the FCA is a unique statute designed to target only those who knowingly defraud the Government, not any organization who submits a claim for payment later found to be errant—or worse, merely inadequate. Needless to say, in organizations with thousands of employees, monitoring the knowledge of every employee and predicting how such knowledge could be pieced together would be impossible. On the other hand, defending an FCA case by relying on the good faith of the employee submitting the claims could become more viable if the Supreme Court adopts a more exacting standard.

Rule 9(b) and the Challenge to Courts Addressing FCA Complaints—The third FCA case pending before the Supreme Court is currently at the certiorari stage, and if certiorari is granted, the case could solidify a key defense in FCA cases: the application of Federal Rule of Civil Procedure 9(b). *Heath*, 791 F.3d 112. Rule 9(b) provides a fundamental safeguard for defendants of fraud claims, as it requires that a party pleading fraud must "state with particularity the circumstances constituting fraud." It serves to weed out some unsupported FCA claims and protect against improper settlement pressure. Ultimately, it can save millions of dollars in discovery costs by mandating dismissal of claims brought by relators who have not done their homework.

Yet courts have been inconsistent in judging FCA complaints under Rule 9(b). In particular, courts have differed regarding whether a relator must plead "with particularity" the details of a *claim for payment*, or merely the details of a broader *fraudulent scheme*. On one hand, the FCA's text requires false claims for payment to sustain liability, so many courts have recognized the need to link broad alleged schemes to actual claims for payment in order to proceed in an FCA case. See, e.g., *U.S. ex rel. Nathan v. Takeda Pharms. N. Am., Inc.*, 707 F.3d 451, 457–458 (4th Cir. 2013); *U.S. ex rel. Ge v. Takeda Pharm. Co.*, 737 F.3d 116 (1st Cir. 2013); *U.S. ex rel. Bledsoe v. Cmty. Health Sys., Inc.*, 501 F.3d 493, 504 (6th Cir. 2007); *U.S. ex rel. Dunn v. N. Mem'l Health Care*, 739 F.3d 417, 420 (8th Cir. 2014); *U.S. ex rel. Clausen v. Lab. Corp. of Am.*, 290 F.3d 1301, 1308 (11th Cir. 2002).

On the other hand, some courts have cautioned that Rule 9(b) should not be a "straitjacket," so if a court can infer that claims for payment were likely submitted to the Government, even if the complaint does not plead details of those claims with particularity, an appropriate FCA case may still proceed. *U.S. ex rel. Grubbs v. Kanneganti*, 565 F.3d 180, 190 (5th Cir. 2009) (holding that even if a relator "cannot allege the details of an actually submitted false claim, [the case] may nevertheless survive"). See also *Foglia v. Renal Ventures Mgmt., LLC*, 754 F.3d 153, 156 (3d Cir. 2014) (stating "it is hard to reconcile the text of the FCA, which does not require that the exact content of the false claims in question be shown, with the "representative samples" standard); *U.S. ex rel. Lusby v. Rolls-Royce Corp.*, 570 F.3d 849, 854–55 (7th Cir. 2009); *Ebeid ex rel. U.S. v. Lungwitz*, 616 F.3d 993, 998–99 (9th Cir. 2010); *U.S. ex rel. Lemmon v. Envirocare of Utah, Inc.*, 614 F.3d 1163, 1172 (10th Cir. 2010). The *Heath* case would allow the Supreme Court to provide clarity on this key issue. Petition for Writ of Certiorari, *AT&T, Inc. v. U.S. ex rel. Heath* (No. 15-363).

In *Heath*, the relator alleged that the defendant fraudulently overbilled a Government fund administered by the Federal Communications Commission from 1997 to 2009 by failing to offer schools mandatory discounts on services. The relator did not allege specific instances of fraud, but rather more generally asserted that the defendant did not train its employees on the applicable price requirement, and as a result, the fund was fraudulently overbilled.

AT&T moved to dismiss and argued that the FCA complaint was not pled with sufficient particularity. The district court dismissed the case

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on unrelated grounds. On appeal, the D.C. Circuit reversed. While the relator's complaint failed to provide details regarding even one particular claim for payment, the D.C. Circuit held that the complaint satisfied Rule 9(b) because it sufficiently alleged "particular details of a scheme to submit false claims paired with reliable indicia that lead to a strong inference that claims were actually submitted." *Heath*, 791 F.3d at 126 (citation omitted) (internal quotations omitted). The Court explained that it "join[ed] [it's] sister circuits in holding that the precise details of individual claims are not, as a categorical rule, an indispensable requirement of a viable False Claims Act complaint." Id.

An understanding of the specificity needed in a complaint under Rule 9(b) is even more important in the FCA context than in other types of litigation. As the *Heath* court noted, the incentive structure of qui tam actions under the FCA "can give rise to opportunistic and abusive behavior" because of the possibility that the relator could share in any settlement or judgment amount. Id. at 116. The problem is further exacerbated by both the drastic penalties defendants face in FCA litigation, and the significant costs involved to defend an FCA suit through discovery.

Rule 9(b) thus serves as an essential procedural check on plaintiffs' ability to pursue meritless and expensive fishing expeditions. It "serves to discourage the initiation of suits brought solely for their nuisance value, and safeguards potential defendants from frivolous accusations of moral turpitude." Id. at 123. Without that check, FCA plaintiffs know that they can assert broad vague allegations, and then attempt to justify broad, and costly, discovery. In addition, relators would face a lower burden in turning allegations of regulatory or contract breaches into an FCA claim that could survive a motion to dismiss.

Given that landscape, the Supreme Court in *Heath* has an important opportunity to refocus courts on the text of the FCA and, in particular, require the pleading of actual claims for payment (which are "sine qua non" of an FCA violation) before allowing cases to proceed into discovery. See *Sanderson v. HCA-The Healthcare Co*., 447 F.3d 873, 878 (6th Cir. 2006). The Supreme Court in other contexts has already recognized that, without proper enforcement of pleading standards, "the threat of discovery expense" in large-scale litigation "will push cost-conscious defendants to settle even anemic cases." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 559 (2007). In *Heath*, it may recognize those same risks for FCA defendants.

Conclusion—The current landscape at the Supreme Court could allow for new clarity and uniformity in FCA litigation. The Court has already agreed to decide the implied certification question in *Escobar*, and that case will be closely watched given its potentially huge ramifications for all who do business with the Government. The Court has the opportunity to craft a rule that avoids confusion and excessive application of the FCA to commonplace regulatory disputes.

Moreover, the Court has called for the views of the solicitor general on the seal and scienter issues in *Rigsby*, which signals its interest in additional questions that often arise in FCA litigation and investigations. And in *Heath*, the Supreme Court also has the chance to set the Rule 9(b) standard which governs every FCA complaint. While in theory Congress could amend the FCA's terms to correct certain misinterpretations, such action remains unlikely given the current legislative environment. Health care providers and others who do business with the Government should keep abreast, as the scope of FCA litigation may take a significant turn.

This Feature Comment was written for The Government Contractor by* B. Kurt Copper, J. Andrew Jackson, Heather M. O'Shea *and* Danielle L. Scoliere, *Jones Day. The authors are attorneys from the Columbus, Chicago and Washington offices of Jones Day who defend investigations and litigation brought under the FCA. ***Disclaimer: The views set forth herein are the personal views of the authors and do not necessarily reflect those of Jones Day. Any publication by a Jones Day lawyer or employee should not be considered or construed as legal advice on any individual matter or circumstance. The contents of this document are intended for general information purposes only. The distribution of this publication or its content is not intended to create, and receipt of it does not constitute, an attorney-client relationship.***

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