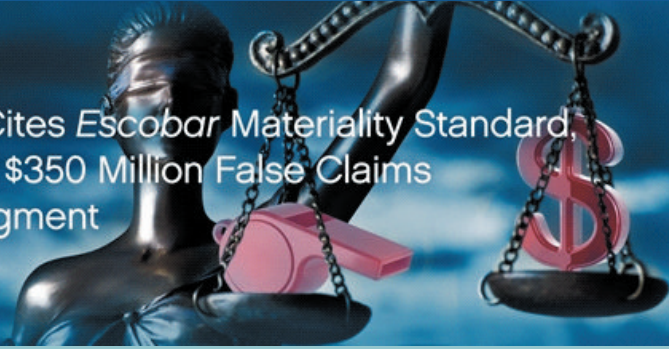


## Judge Cites *Escobar* Materiality Standard, Vacates \$350 Million False Claims Act Judgment



### IN SHORT

**The Situation:** The False Claims Act imposes civil liability on any person or entity that "knowingly presents, or causes to be presented" to the U.S. government "a false or fraudulent claim for payment or approval."

**The Development:** A U.S. district court has vacated a \$350 million False Claims Act verdict against a group of nursing home operators, based on the "materiality standard" established by the U.S. Supreme Court's *Escobar* decision.

**Looking Ahead:** The court noted that it was the relator's obligation to show that the government did not know of the recordkeeping irregularities in the case, and that it would have refused to pay had it known.

Relying upon the U.S. Supreme Court's *Universal Health Services v. United States ex rel. Escobar* decision, the U.S. District Court for the Middle District of Florida vacated a nearly \$350 million False Claims Act ("FCA") verdict against a group of nursing home operators. Guided by *Escobar*'s emphasis on the "rigorous" and "demanding" materiality and scienter hurdles, *U.S. ex rel. Ruckh v. CMC II LLC et al.* ("*Ruckh*") demonstrates that the government's own actions, such as continuing payment or demanding compliance, may create a practical impediment to establishing materiality.

The FCA imposes civil liability on any person or entity that "knowingly presents, or causes to be presented" to the U.S. government "a false or fraudulent claim for payment or approval." 31 U.S.C. § 3729(a)(1). Under the implied certification theory, a person or entity submitting a request for payment impliedly certifies compliance with all applicable laws, regulations, and contract requirements. A violation of any of those laws, regulations, or contract requirements may lead to FCA liability based upon the false certification, even when the government payment decision does not specifically rely on the certification.

While the unanimous decision in *Escobar* upheld the heavily debated theory of "implied certification," the Supreme Court stressed that the government and relators must continue to satisfy the FCA's materiality and scienter elements. The unanimous *Escobar* decision found that implied certification claims could succeed "at least" where the defendant has made "specific representations about the goods or services provided," and "the defendant's failure to disclose its noncompliance with material statutory, regulatory, or contractual requirements makes those representations misleading half-truths." The Supreme Court also held that designation of a term as a condition of payment is relevant to, but not dispositive of, materiality. But, the *Escobar* decision left it to lower courts to decide whether the two-part test for establishing falsity under an implied certification theory is mandatory and how to apply the materiality standard.

In *Ruckh*, the relator alleged that a group of nursing home operators engaged in a scheme to defraud Medicare and Medicaid by (i) failing to maintain a "comprehensive care plan" ostensibly required by a Medicaid regulation, and (ii) submitting defective paperwork, which the relator claimed showed that defendants never provided the therapy evidenced by the paperwork and billed to Medicare. After originally confirming the jury verdict and trebling damages, the court granted the defendants' motion for judgment as a matter of law under Federal Rule of Civil Procedure 50 and vacated the judgment. Noting that materiality was "defined unambiguously and required emphatically by" *Escobar*, the court based its ruling on the relator's failure to offer evidence of materiality.

The *Ruckh* court described *Escobar* as "reject[ing] a system of government traps, zaps, and zingers that permits the government to retain the benefit of a substantially conforming good or service but to recover the price entirely—multiplied by three—because of some immaterial contractual or regulatory non-compliance." The court noted that the FCA instead "requires proof that a vendor committed some non-compliance that resulted in a material deviation in the value received and requires proof that the deviation would materially and adversely affect the buyer's willingness to pay."



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The court found that "[n]ot only did the relator fail to prove that the government regarded the disputed practices as material and would have refused to pay, but the relator failed to prove that the defendants submitted claims for payment despite the defendants' knowing that the governments would refuse to pay the claims if either or both governments had known about the disputed practices." The court concluded that, having failed to prove that the governments considered the defendants' alleged noncompliance material, the relator could not establish the defendants' knowledge of materiality.

The court held that it was the relator's burden to show that the government did not know about the recordkeeping deficiency and that, had it known, it would have refused to pay for the goods and services provided. However, the relator did not satisfy that burden. The court explained that "[t]he governments paid and continue to pay to this day despite the disputed practices, long ago known to all who cared to know."

The court also suggested that the government's lack of enforcement, whether knowing or unknowing, presents a barrier to establishing materiality. "Every day that the government continues to pay for a good or service, notwithstanding some known or unknown non-compliance and, consequently, the greater the proposed repayment times three in the event of a successful False Claims Act action, the greater the practical impediment to proof of materiality." The court explained that the required proof for materiality "likely would need to exclude the governments' choosing to resort to a more moderate, more proportional, more efficacious remedy, such as delivery of a 'notice of noncompliance,' accompanied by a stern demand for, and a fair deadline for, compliance. Or to exclude the governments' choosing to resort to some mediated solution or to an administrative hearing or to an order to show cause. Or perhaps the governments' offering a price adjustment."

### THREE KEY TAKEAWAYS

1. Although implied certification remains a valid theory for establishing FCA liability, the government and relators bear the burden of satisfying the "rigorous and demanding" materiality requirement under *Escobar*.
2. The government's continued payment for a good or service, notwithstanding a known or even unknown issue of noncompliance, may make it more difficult to prove materiality
3. FCA defendants may be able to rely on certain government remedial measures, such as demanding compliance or offering a price adjustment, to prove the absence of materiality.

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