2011 MID-YEAR FALSE CLAIMS ACT UPDATE

To Our Clients and Friends:

$7,300,000,000! That's 7.3 billion dollars. If that figure grabbed your attention, imagine the reaction of federal and state prosecutors and qui tam plaintiffs' lawyers across the country when they heard that between January 2009 and June 2011, the Department of Justice ("DOJ") recovered more than $7.3 billion in civil settlements and judgments alone under the False Claims Act, 31 U.S.C. §§ 3729-33 (the "FCA" or the "Act").[1] And far more may be in the pipeline: As of January 4, 2011, there were 1,341 qui tam cases under seal for which the government has yet to reach a decision on intervention.[2] During the fourth quarter of 2010 alone, DOJ attorneys "requested authority to issue over 500 CIDs [civil investigative demands], which is more than six times the number of CIDs requested during the two preceding years combined."[3] At least thirty-nine new FCA cases were filed during the first quarter of 2011, and the actual number of new cases may be significantly higher, as qui tam actions must be filed under seal.[4] In June 2011, the Congressional Budget Office estimated that DOJ will recover between $3 and $4 billion annually in civil fraud judgments over the next ten years.[5] Indeed, sources suggest that at present, "[t]here are at least ten False Claims Act settlements in the works that are likely to top a billion dollars each."[6]

Never before have we witnessed such an aggressive focus on fighting fraud in government programs. In January 2011, Assistant Attorney General for the Civil Division Tony West testified before the Senate Committee on the Judiciary about the DOJ's "aggressive civil enforcement actions aimed at rooting out waste, fraud, and abuse,"[7] attributing most of 2010's record-setting recoveries to whistleblower lawsuits and recent FCA amendments. According to West, DOJ "has never been more aggressive--or more successful--in the anti-fraud battle as it has in the last two years."[8] The Administration has shown no signs of letting up.

As further described below, in May 2011, legislation was introduced in Congress to provide greater funding to the DOJ to be spent on investigation and prosecution of FCA actions. Further, by way of an executive order signed June 13, 2011 and a video message released to the American public on YouTube the day before, President Obama launched a "Campaign to Cut Waste," to "hunt down and eliminate misspent tax dollars in every agency and department across the federal government."[9] As part of this campaign, Vice President Biden will lead an 11-member "Government Accountability and Transparency Board," that will "advance efforts to detect and remediate fraud, waste, and abuse in Federal programs."[10] In the June 12, 2011 video, Vice President Biden spoke of the need for transparency and accountability in government spending and a "relentless focus" on eliminating fraud and waste in government programs.[11] Within one week of that announcement, the Centers for Medicare & Medicaid Services ("CMS") announced that starting July 1, 2011, CMS will begin using predictive modeling technology to help identify potentially fraudulent Medicare claims.[12]

In this time of budget deficits, state governments, too, are actively pushing civil fraud legislation and pursuing false claims actions as well. As discussed further below, states are looking to pass or amend
aggressive false claims statutes patterned after the FCA, and state recoveries are reaching record-highs. In May 2011, for example, the California Attorney General announced a $241 million settlement, reportedly "the largest recovery in the history of California's False Claims Act."[13]

In this mid-year update, we first summarize federal and state legislative action during the first six months of 2011. Next, we briefly summarize significant settlements and judgments announced during the first half of 2011. Finally, we discuss important judicial decisions and continuing trends during the first half of this year. A collection of Gibson Dunn's recent publications on the FCA, including more in-depth discussions of the FCA's framework and operation along with practical guidance to help companies avoid or limit liability under the FCA, may be found on our FCA Website.

I. Legislative Action in the First Six Months of 2011

A. Federal Legislation

1. Fighting Fraud to Protect Taxpayers Act of 2011, S. 890.

On May 5, 2011, Senators Patrick Leahy (D-VT) and Charles Grassley (R-IA) introduced the Fighting Fraud to Protect Taxpayers Act of 2011.[14] On May 19, 2011, the bill was reported out of the Judiciary Committee and placed on the Senate Legislative Calendar. Upon introduction of the bill, Senator Leahy explained that in 2010 the DOJ recovered "far more than it costs to investigate and prosecute" fraud actions.[15] One goal of the proposed legislation is to capitalize "on this rate of return by ensuring that a percentage of money recovered by the Government through fines and penalties in fraud cases . . . is reinvested in the investigation and prosecution of fraud cases."[16]

Section 2 of the proposed bill would provide greater funding to the DOJ for the investigation and prosecution of fraud, including FCA violations.[17] The DOJ currently retains 3% of the funds recovered from civil fraud actions in its Working Capital Fund. The bill would increase this amount to 3.5%, giving the DOJ approximately $15 million more per year to dedicate to FCA enforcement.[18]

Section 3 of the proposed legislation would permit the DOJ to recover the investigation and prosecution costs relating to FCA actions (to be accomplished by way of an additional deduction from FCA recoveries paid to victim agencies).[19]

Section 9 of the bill would require the Attorney General to submit an annual report to Congress detailing every FCA settlement involving claims for damages of more than $100,000, including information regarding the amount of the settlement that constitutes the government's single damages, as well as the amount of penalties and multipliers of damages.[20] The CBO "estimates that it would cost about $1 million annually, subject to the availability of appropriated funds, for DOJ to prepare the reports required by the bill."[21] Although this reporting provision may increase transparency and lead to more consistent results, as a practical matter, these reporting requirements also may discourage settlements.
2. Proposed Amendments to FAR OCI Rules

On April 26, 2011, the Department of Defense, General Services Administration, and the National Aeronautics and Space Administration published a proposed rule to substantially amend the provisions of the Federal Acquisition Regulation ("FAR") concerning organizational conflicts of interest ("OCI") and contractor access to nonpublic information. FAR OCI rules are designed to identify and address circumstances in which a government contractor may be unable to render impartial assistance or advice to the government or might have an unfair competitive advantage based on unequal access to information or prior involvement. The proposed rule describes two types of harm that a potential OCI may present: (1) harm to the integrity of the competitive acquisition process; and (2) harm to the government's business interests. The rule describes the responsibilities of a contracting officer ("CO") to address potential OCIs, and requires COs to address OCI issues throughout the procurement process.

In many cases, the proposed rule would require potential contractors to make broader OCI disclosures than previously necessary. Proposed FAR 52.203-XX would require potential contractors on covered contracts to disclose all relevant information regarding any OCIs. By signing an offer, a contractor would be making a representation that it has complied with the disclosure requirements. This disclosure requirement arguably implicates the FCA because a knowing failure to disclose OCIs in contract proposals could result in false representations or alleged fraudulent inducement. Additionally, proposed FAR 52.203-ZZ would obligate covered contractors to continually monitor potential OCIs and disclose any newly occurring OCIs to the government. Should a contractor fail to alert the government to potential OCIs, the contractor arguably would risk FCA liability for making a false statement or certification.

B. State Legislative Action

Currently, more than 30 states have enacted some version of a false claims act.[22] Section 1909 of the Social Security Act, as enacted by section 6031 of the Deficit Reduction Act of 2005 (the "DRA"),[23] provides a financial incentive for states to adopt false claims legislation by offering states an additional 10% of any funds recovered through a state Medicaid false claims action.[24] To determine whether states qualify for this enhancement, the U.S. Department of Health and Human Services ("HHS"), Office of the Inspector General ("OIG") reviews the state false claims acts for compliance with the DRA. The OIG previously carried out such reviews and determined that 14 states were eligible to receive the additional 10% recovery. Following recent amendments to the FCA (discussed in our prior alerts), however, the OIG again reviewed several states' false claims acts and found that none satisfied the requirements.

On March 21, 2011, OIG sent several letters to states' attorneys general informing them that their state laws do not, or no longer, meet the requirements of section 1909 of the DRA. For the 14 states previously determined eligible, OIG granted a two-year grace period, until March 13, 2013, during which time those states must amend their false claims legislation (while continuing to receive the additional 10% recovery). For the other 10 states reviewed and found ineligible, no grace period was given because OIG had not previously approved those states' false claims acts.
With 10% of significant recoveries on the line, we expect to see increased state legislative action over the next several months. Indeed, as shown below, there already has been a flurry of state legislative activity during the first half of 2011. Despite the flurry, however, only a few states actually have successfully passed proposed legislation, with the most significant changes occurring in Virginia.

1. States with Relevant Legislative Activity in 2011

The following list of state legislative activity is intended to be illustrative, not exhaustive.

- **Arizona**: Legislators in Arizona introduced two bills in 2011 with the purpose of creating a state false claims act. H.B. 2629 proposed a false claims act that tracked the provisions of the Federal FCA and included a *qui tam* provision and protection for whistleblowers.[25] H.B. 2674 was similar to H.B. 2629 except that it would have applied only to health care fraud.[26] Neither bill came up for a vote before the First Regular Session of the 50th Arizona Legislature ended in April 2011.

- **Arkansas**: The Arkansas Medicaid Fraud False Claims Act permits the state to reward individuals who provide information about Medicaid fraud, but it does not authorize individuals to bring suit themselves as relators.[27] In April 2011, Arkansas enacted an amendment to its act to provide a larger reward to individuals who provide information that aids the state in prosecuting fraud.[28] While the previous statute had capped the monetary award at $100,000, the 2011 amendment provides that Arkansas may award up to 10% of the penalty recovered to an individual informer.[29]

- **Illinois**: In 2011, Illinois state legislators proposed H.B. 3363, which would have amended the public disclosure bar of the Illinois False Claims Act to more closely track the current language in the federal statute.[30] The bill was stuck in the Rules Committee, however, and was not passed by the end of the legislative session on May 31, 2011.

- **Kentucky**: In Kentucky, two false claims bills were proposed in 2011. H.B. 4 provided for implementation of a false claims act in the state, and included a *qui tam* provision.[31] S.B. 11 was similar to H.B. 4, but pertained only to the Commonwealth's Medical Assistance Program.[32] Despite an initial appearance of support, neither bill managed to pass both the House and Senate. H.B. 4 passed the House but died in the Senate, and S.B. 11 passed in the Senate but was never heard in House committee.

- **Mississippi**: In 2011, three bills relating to false claims were introduced in Mississippi. H.B. 208 and S.B. 2063 both proposed the creation of the Mississippi False Claims Act, which would have been substantially similar to the FCA.[33] H.B. 565 proposed an amendment to the Mississippi Medicaid Fraud Control Act that, among other things, would provide greater specificity about what constitutes a fraudulent claim, would allow relators to bring *qui tam* suits, and would define the statute of limitations for suits under the state act.[34] None of the three bills passed during the 2011 regular session.

- **Missouri**: Missouri also attempted to enact a false claims act in 2011. H.B. 374 was similar to the state false claims bills proposed in other states this year: it included a *qui tam* provision and
an anti-retaliation provision, and mirrored the language of the FCA.[35] The bill did not pass before the legislature adjourned.

- **New Hampshire**: On June 14, 2011, the Governor of New Hampshire signed S.B. 139 into law.[36] S.B. 139 amends the New Hampshire False Claims Act[37] to clarify the criteria for bringing an action as a relator. Specifically, the amendment provides that a relator can bring an action against a defendant who either has its principal place of business in New Hampshire or has received Medicaid reimbursement during the 12-month period immediately preceding the date the action is filed.[38]

- **New Mexico**: H.B. 314, introduced in 2011, proposed changes to the New Mexico Fraud Against Taxpayers Act.[39] The proposed amendment included provisions specifying the type of information required from a *qui tam* plaintiff, providing for civil investigative demands, and allowing the state to bring a separate action if it decides not to intervene in an action under the state act. The proposed amendments did not pass.

- **Ohio**: On April 7, 2011, S.B. 143 was proposed in the Ohio Senate, providing for the creation of an Ohio False Claims Act.[40] The proposed bill mirrored the federal FCA, included *qui tam* provisions, and was otherwise intended to be fully compliant with the DRA and the amended FCA. Ohio's Attorney General has promoted the legislation. In February 2011, Ohio-based managed care contractor CareSource agreed to pay $26 million to resolve FCA allegations relating to Medicaid fraud.[41] State Attorney General Mike DeWine announced that if Ohio had a state version of the FCA in place at that time, Ohio's "percentage of the (CareSource) settlement would have gone up 10 percent."[42]

- **Pennsylvania**: In January 2011, a bill was introduced in the Pennsylvania Legislature that would have enacted a state false claims act.[43] The bill is similar to the FCA and provides for, among other things, "adoption of Congressional intent of the Federal False Claims Act."[44] The bill was referred to the Judiciary Committee on January 12, 2011, but no further action has been taken.

- **Texas**: Texas has had a Medicaid false claims act since 1995.[45] In 2011, S.B. 1115 was introduced to create a cause of action that mirrors the current version of the FCA.[46] S.B. 1115 would not have altered the existing Medicaid false claims act.[47] However, S.B. 1115 did not pass during the regular legislative session, and it was not reintroduced in the special legislative session.

- **Utah**: Utah has had a state false claims act for many years, but it does not include a *qui tam* provision.[48] S.B. 103, proposed in the 2011 Utah legislative session, would have amended the Utah False Claims Act to meet the DRA requirements, including the addition of a *qui tam* provision and the creation of specific protections for whistleblowers.[49] S.B. 103 did not make it out of the Senate Rules Committee in 2011.

- **Vermont**: The Vermont House of Representatives introduced a bill in 2011 to create a health care false claims act. The purpose of H. 132 was to create a false claims act that met federal criteria in order to allow Vermont to "retain an additional ten percentage points of the federal
share of Medicaid funds recovered from fraud."[50] H. 132 would have authorized *qui tam* actions and would have included a provision prohibiting retaliation against whistleblowers. The Vermont legislature adjourned without passing H. 132.

- **Virginia:** In March 2011, Virginia passed an amendment to the Virginia Fraud Against Taxpayers Act.[51] The amendment, S.B. 1262, makes three important changes to Virginia's false claims act: first, it provides that a designee of the Attorney General may issue civil investigative demands; second, it allows the Attorney General to share information with *qui tam* relators under certain circumstances; third, it amends the elements of the offenses for which individuals are liable under Virginia's false claims act.[52]

- **Washington:** Three false claims bills were proposed during the 2011 legislative session in the State of Washington. S.B. 5310 proposed the creation of a Washington False Claims Act and included a *qui tam* provision.[53] Two narrower bills, S.B. 5458 and S.B. 5960, only applied to Medicaid claims.[54] S.B. 5310 died in the regular session, and, though S.B. 5458 and S.B. 5960 continued into the special session, neither passed.

- **West Virginia:** On January 12, 2011, H.B. 2072 was introduced to amend portions of the West Virginia Code that create liability for presenting false claims to the state medical reimbursement programs. The purpose of HB 2027 was to "adopt the congressional intent behind the federal False Claims Act," and it included a *qui tam* provision, as well as protections for whistleblowers, but the bill only applied to claims made to the West Virginia Department of Health and Human Resources.[55] H.B. 2072 died in the House Committee on the Judiciary.

- **Wyoming:** In the 2011 Wyoming legislative session, a bill was introduced that proposed a state Medicaid false claims act.[56] The bill was similar to the FCA, but limited to Medicaid fraud.[57] The Wyoming Legislature adjourned without passing the bill.

### 2. **State Attorneys General Vow to Aggressively Enforce State Acts**

Along with state action to enact enabling laws, state attorneys general have vowed to aggressively enforce those laws. As we discussed in our 2010 Year-End False Claims Act Update, New York recently amended its false claims act to encourage *qui tam* suits and to increase the protections and incentives available to whistleblowers. In January 2011, New York Attorney General Eric T. Schneiderman pledged that he would use the New York false claims act to aggressively pursue fraud in the state.[58] To that end, Schneiderman announced further that he would establish a new Taxpayer Protection Unit to investigate and prosecute tax violations and fraud relating to government pensions and contractors.[59] He also promised to strengthen the Medicaid Fraud Control Unit at the Office of the Attorney General through the "addition of dozens of new prosecutors, investigators, and auditors, devoted to cracking down on Medicaid fraud."[60] Shortly thereafter, in February 2011, AG Schneiderman announced "three settlement agreements in Medicaid fraud investigations" that came "on the heels" of these initiatives and emphasized the AG's commitment to "work every day to ensure those who cheat the taxpayers are caught and forced to pay for their crimes."[61]

Additionally, both Schneiderman and California Attorney General Kamala Harris have both indicated that they intend to use their respective state false claims acts to crack down on mortgage fraud.
Discussing the newly implemented Mortgage Fraud Strike Force in California, Harris declared that the Attorney General's Office is prepared to use the California false claims act "in a way that will look at all those who have made false statements or misled investors of any nature – be they individuals, institutions or municipalities."[62] In New York, Schneiderman requested information from three major financial institutions regarding their mortgage securities operations, indicating a possible FCA investigation.[63]

Similarly, in January 2011, Virginia Attorney General Kenneth T. Cuccinelli, II intervened in a qui tam lawsuit filed under the Virginia Fraud Against Taxpayers Act seeking $150 million in damages from a financial institution for allegedly defrauding the state's public pension fund by overcharging for foreign currency trades.[64] The Virginia suit is similar to one filed in California against a different bank, seeking $200 million in damages based on foreign currency exchange practices.[65] In fact, as a result of at least three qui tam actions filed by FX Analytics in Virginia, California and Florida, a number of federal and state regulators and prosecutors are investigating companies' foreign currency exchange practices.[66]

II. FCA Settlements and Judgments During the First Six Months of 2011

The federal government did not announce any record-breaking FCA settlements during the first half of 2011, but we witnessed a steady stream of substantial FCA settlements and judgments. Although like prior years, most recoveries were in the health care sector, there have been recoveries in nearly every industry supported in whole or in part by government spending. For the first half of 2011, the following settlements and judgments are noteworthy:

- In January 2011, a technology company agreed to pay $46 million to settle claims that a company it acquired in 2010 submitted false claims and caused others to submit false claims to the GSA and other federal agencies. The settlement resolved allegations under the FCA and Anti-Kickback Act that the acquired company paid kickbacks to systems integrator companies in return for recommendations that federal agencies purchase its products.[67]

- In January 2011, the government settled FCA claims against a Japanese company and its U.S. subsidiary in connection with the importation and sale of defective Zylon fiber used in bulletproof vests. The settlement was part of a larger investigation of the Zylon body armor industry; the government previously settled with eight other industry participants for more than $59 million.[68]

- In February 2011, a pharmaceutical company pleaded guilty to a misdemeanor violation and settled FCA claims stemming from the alleged illegal promotion of an epilepsy drug.[69] Of the total global resolution of $203.5 million, the company agreed to pay $102 million to resolve the civil FCA allegations ($59 million of which will go to the federal government).

- In March 2011, an Illinois medical products company agreed to pay $85 million to settle a whistleblower lawsuit accusing the company of paying kickbacks to hospitals and companies that bought supplies paid for by federal health care programs.[70]
In April 2011, a telecommunications company agreed to pay $93.5 million to resolve allegations that the company and its subsidiary overcharged the GSA on voice and data telecommunications services contracts.[71]

In April 2011, a German company agreed to pay the U.S. approximately $9.1 million (€6.5 million) to settle allegations that the company fraudulently billed the Army for guard hours not actually worked at U.S. Army installations in Germany.[72] In addition to paying $9.1 million, the company agreed to dismiss its own claims against the Army, seeking approximately $5.7 million. Significantly, during the investigation, the German police helped the United States government collect information. In addition, the U.S. asserted the FCA claims as counterclaims in an action that the company brought against the U.S. in the Court of Federal Claims. This highlights a significant risk that contractors face when bringing actions against the government, which often are met with FCA counterclaims.

In April 2011, a pharmaceutical company announced that it had reached a settlement in principle to resolve a qui tam action filed against it by the pharmacy Ven-A-Care of the Florida Keys, Inc. for $154 million.[73] Ven-a-Care has initiated qui tam claims against several drug manufacturers, generally alleging that the companies caused government health care programs to pay inflated prices for prescription drugs. Notably, in February 2011, a Texas court ordered two companies to pay $170 million for overcharging the Texas Medicaid program in a qui tam action initiated by Ven-A-Care.[74] The L.A. Times reported in January 2011 that Ven-a-Care "has won settlements in at least 18 [qui tam] suits. . . . [And] the fees awarded the company and its attorneys since 2000 [total] more than $380 million."[75]

In May 2011, certain pharmaceutical companies agreed to pay $44.3 million to settle FCA claims stemming from alleged illegal promotion and kickbacks in connection with sales of a prescription drug.[76]

In June 2011, two oil and gas companies and their affiliates agreed to pay more than $17 million to settle allegations that the companies underpaid royalties owed on natural gas produced from federal and Indian leases. This settlement arose from a qui tam lawsuit filed by Harrold Wright. To date, settlements with defendants in the Wright action have exceeded $249 million.[77]

In June 2011, two health care companies settled FCA claims stemming from alleged off-label promotion of prescription drugs. On June 9, 2011, DOJ announced that the U.S. subsidiary of a Belgian pharmaceutical manufacturer pleaded guilty and agreed to pay more than $34 million to resolve criminal and civil liability arising out of off-label promotion of an epilepsy drug.[78] The company agreed to pay $25.7 million to resolve the civil FCA allegations. The next day, DOJ announced yet another settlement of off-label promotion based FCA claims for $25 million.[79]

Finally, as noted above, in May 2011, the California Attorney General announced a $241 million settlement with "the state's biggest provider of medical laboratory testing."[80] The settlement reportedly is "the largest recovery in the history of California's False Claims
The settlement stems from a lawsuit filed by a competitor against seven medical laboratories under the *qui tam* provisions of the California FCA. The relator alleged that the labs overcharged the state's Medi-Cal program and provided illegal kickbacks for referral of Medi-Cal patients. Cases remain pending against the non-settling laboratories.

### III. Case Law Developments in the First Half of 2011

In our 2010 Year-End False Claims Act Update, we discussed several important FCA-related, judicial decisions issued during 2010. In the first half of 2011, courts have continued to be active in deciding FCA-related cases. Since the last update, the Supreme Court has issued another opinion interpreting the FCA's public disclosure bar (and denied certiorari in another) and many lower courts also have examined issues including the relevance of industry-wide allegations to the public disclosure bar, indirect reverse false claims, and the constitutionality of the FCA's mandatory seal requirement.

#### A. Supreme Court Developments

First, in *Schindler Elevator Corp. v. United States ex rel. Kirk*, 131 S. Ct. 1885 (2011), the Supreme Court held that a federal agency's response to a Freedom of Information Act ("FOIA") request is a "report . . . or investigation" within the meaning of the public disclosure bar. The FCA's public disclosure bar prohibits a relator who is not an "original source" from bringing a *qui tam* action if the suit is based on information publicly disclosed in government hearings and reports, or in the news media. 31 U.S.C. § 3730(e)(4). At issue in *Schindler Elevator* was whether government records obtained through FOIA requests are government reports within the meaning of the public disclosure bar. By a 5-3 vote (Justice Kagan did not participate), the Supreme Court adopted a broad definition of "report" and held that FOIA requests qualify as government reports triggering the bar. 131 S. Ct. at 1891-93. *Schindler Elevator* strengthens the public disclosure bar by preventing relators from filing *qui tam* actions based on allegations disclosed in FOIA requests, unless they are an "original source."

*Schindler* follows the Supreme Court's broad interpretation of the public disclosure bar last year in *Graham County Soil & Water Conservation District v. United States ex rel. Wilson*, 125 S. Ct. 2444 (2010), in which the 7-2 majority held that whistleblowers cannot file lawsuits based upon information that is publicly available in state and local administrative reports, audits, and investigations. And both cases follow on the heels of *Rockwell International Corp. v. United States*, 549 U.S. 457 (2007), in which the Supreme Court narrowly construed the "original source" requirement and clarified that the public disclosure bar was a jurisdictional issue.

These cases, which otherwise represent important victories for FCA defendants in the Supreme Court, may in fact have little impact going forward. On March 23, 2010, President Obama signed into law the Patient Protection and Affordable Care Act ("PPACA"), Pub. L. 111-148, 124 Stat. 119 (2010). Among other things, the PPACA eliminates what was an absolute jurisdictional bar in favor of providing the DOJ with discretion over public disclosure dismissals. In addition, the PPACA legislatively overruled *Graham* by specifically amending the FCA to bar only those actions based on disclosures from federal sources or the news media. The PPACA also attempted to dilute the public disclosure bar, by eliminating the "direct and independent knowledge" requirement in favor of
"knowledge that is independent of and materially adds to the publicly disclosed allegations or transactions." 31 U.S.C. § 3730(e)(4)(B).

Second, as we noted in our 2010 Year-End False Claims Act Update, the Sixth Circuit's decision in United States ex rel. Summers v. LHC Group, Inc., 623 F.3d 287 (6th Cir. 2010), cert. denied, 79 U.S.L.W. 3403 (U.S. June 27, 2011), created a new circuit split involving the FCA's under seal filing requirement for qui tam cases. In contrast to the case-by-case approach used in the Ninth and Second Circuits, the Sixth Circuit in Summers endorsed a per se rule requiring dismissal if a relator fails to follow the under seal filing procedure. After calling for the views of the Solicitor General, who expressed disagreement with the per se rule adopted in Summers but recommended denial of the petition because the suit was subject to dismissal on an alternative ground, the Supreme Court declined to resolve the split and denied certiorari.[82]

B. When Do Reports Documenting Fraud in an Industry as a Whole Trigger the Public Disclosure Bar?

The Seventh Circuit in United States ex rel. Baltazar v. Warden, 635 F.3d 866 (7th Cir. 2011), addressed the issue whether industry-wide allegations of fraud trigger the public disclosure bar. Baltazar involved allegations that the defendants had submitted false claims to Medicare and Medicaid for chiropractic services. Id. at 866-67. The defendants moved for dismissal under the public disclosure bar, relying on the Seventh Circuit's earlier decision in United States ex rel. Gear v. Emergency Medical Associates of Illinois, Inc., 436 F.3d 726 (7th Cir. 2006), and arguing that the relator's allegations were based on public reports about fraud in the industry as a whole. Baltazar, 635 F.3d at 867-69. The Seventh Circuit reversed the district court's dismissal, distinguishing Gear as involving reports of a uniform practice in an industry, unlike the reports found persuasive by the district court that only revealed a high rate (57%) of erroneous claims submitted to Medicare by chiropractors. Id. at 867-69. Nothing in Baltazar, however, suggests that Gear was wrongly decided or that industry-wide disclosures cannot trigger the public disclosure bar in appropriate circumstances, such as where a uniform industry-wide practice has been revealed and a relator adds nothing to the industry-wide allegations. See id. at 869.

C. Kickback Statutes and the FCA

Recently, courts have decided a number of FCA cases involving the Anti-Kickback Statute, 42 U.S.C. § 1320a-7b ("AKS") and the Anti-Kickback Act, 41 U.S.C. §§ 8701-07 (formerly 41 U.S.C. § 51 et seq.) ("AKA").

In United States ex rel. Wilkins v. United Health Group, Inc., --- F.3d ----, No. 10-2747, 2011 U.S. App. LEXIS 13322 (3d Cir. June 30, 2011), the Third Circuit held that a false certification (express or implied) of compliance with the AKS could give rise to an FCA action because "[c]ompliance with the AKS is clearly a condition of payment under” Medicare. Id. at *48. Similarly, in United States ex rel. Hutcheson v. Blackstone Medical, Inc., --- F.3d ----, No. 10-1505, 2011 U.S. App. LEXIS 10972 (1st Cir. June 1, 2011), the First Circuit held that it is "abundantly clear that AKS compliance is a precondition of Medicare payment," meaning that an FCA action may lie for a violation of the AKS, and that there is no exception for violations caused by third parties. Id. at *45-46.
The relator in *Hutcheson* alleged that defendant paid kickbacks to induce doctors to use its products in certain spinal surgeries, causing the hospitals to submit fraudulent claims to Medicare by certifying that they had complied with the AKS. *Id.* at *8-9. Defendant argued that the hospitals' certifications could not be rendered false by its actions as a third party. *Id.* at *34. The First Circuit rejected the idea of a categorical limitation from FCA liability for third parties who have not submitted claims themselves, *Id.* at *35-41, and further held that, for purposes of the motion to dismiss, the relator's allegations were sufficient to establish that "the kickbacks were capable of influencing Medicare's decision as to whether to pay" the claims, and that Blackstone caused the hospitals to submit false claims, *Id.* at *48-51.

The *Hutcheson* court declined to reach the "broader argument" whether "violations of the AKS inherently render claims to federal health care programs materially false or fraudulent under the FCA." *Id.* at *3 n.1. Of course, the PPACA amended the AKS, 42 U.S.C. § 1320a-7b(g), to provide that any claim submitted for items or services provided in violation of the AKS "constitutes a false or fraudulent claim for purposes of" the FCA.

In two recent cases, district courts have held that the AKA, 41 U.S.C. §§ 8701-07, prohibits downstream kickbacks, and that claims tainted by unlawful kickbacks may constitute FCA violations. In *United States ex rel. Garrison v. Crown Roofing Services, Inc.*, No. H-07-1018, 2011 U.S. Dist. LEXIS 27008 (S.D. Tex. Mar. 16, 2011), the court rejected defendant's argument that "the AKA only forbids payments going up the contractual chain," holding that "[n]othing in the plain language of the [AKA] prohibits kickbacks made from prime contractors to subcontractors." *Id.* at *8-9. Likewise, in *United States ex rel. Compton v. Circle B Enterprises, Inc.*, No. 7:07-cv-32 (HL), 2011 U.S. Dist. LEXIS 10949 (M.D. Ga. Feb. 3, 2011), the court held that "[i]f it is proven that Circle B included in its contract price the cost of the kickbacks paid to the subcontracting companies, then that conduct can give rise to FCA liability. In such a case, the loss the Government sustained was at least the cost of the kickbacks [paid by Circle B]." *Id.* at *20.

In *United States ex rel. Vavra v. Kellogg Brown & Root, Inc.*, 1:04-cv-42-MAC (E.D. Tex. Feb. 8, 2011), Dkt. 71, the court held that an upstream kickback does not, without more, give rise to an FCA violation. In that case, the relator and the government (which intervened) alleged that Kellogg Brown & Root ("KBR") employees accepted kickbacks from employees of certain subcontractors in exchange for awarding subcontracts to transport U.S. military equipment and supplies to Iraq. *Id.* at 2. The government alleged, *inter alia*, that KBR violated the FCA by billing the government for subcontract costs that were tainted by kickbacks. *Id.* at 14. The district court rejected the government's argument that "the acceptance of kickbacks necessarily gives rise to an FCA claim," and granted KBR's motion to dismiss the complaint in relevant part. The court held, the government failed to plead "that compliance with the AKA is a condition of payment" or facts sufficient to "tie KBR's acceptance of kickbacks to its submitted claims for payment." *Id.* at 15-16.

D. Eighth Circuit Rejects Application of False Certification Theory to Lenders of Federally Backed Student Loans

Participants in federal student financial aid programs, in particular for-profit schools, have in recent years become frequent targets of FCA suits based on a false certification theory endorsed by the
Seventh Circuit in *United States ex rel. Main v. Oakland City University*, 426 F.3d 914, 916-17 (7th Cir. 2005), and the Ninth Circuit in *United States ex rel. Hendow v. University of Phoenix*, 461 F.3d 1166, 1176-77 (9th Cir. 2006). In *United States ex rel. Vigil v. Nelnet, Inc.*, 639 F.3d 791 (8th Cir. 2011), the Eighth Circuit rejected an attempt to extend this theory of FCA liability to private lenders offering loans through the Federal Family Education Loan Program ("FFELP"). Under the FFELP program, the government offers incentives, including interest-rate subsidies and insurance against defaults, to private lenders who issue and service certain student loans. *Id.* at 794-95. In *Vigil*, the relator alleged that the lenders had violated a subsection of the FFELP statutes requiring that participating lenders refrain from certain conduct, such as offering improper inducements or engaging in fraudulent advertising. *Id.* at 795. Noting that the FCA was not concerned with regulatory noncompliance, the court affirmed dismissal of the relator's complaint because it lacked sufficient allegations of any false certification of compliance with the FFELP eligibility statutes in connection with a claim for payment. *Id.* at 796-97. The court distinguished *Main* and *Hendow* on the ground that the schools in those cases allegedly submitted a fraudulent initial application to participate in federal student financial aid programs. *Id.* at 797. Additionally, the court found it significant that the FFELP statutes and regulations created a complex monitoring system for eligibility violations, and concluded that imposition of FCA liability would undermine this regulatory scheme. *Id.* at 798.

**E. Fourth Circuit Rejects Constitutional Challenge to FCA Seal Provision**

The FCA requires a *qui tam* relator to file his or her complaint under seal, and provides that the complaint shall remain under seal for 60 days while the government decides whether to intervene. 31 U.S.C. § 3730(b)(2). The government may move to extend the seal period for "good cause." *Id.* As we noted in our 2010 Year-End False Claims Act Update, the American Civil Liberties Union, OMB Watch, and the Government Accountability Project together recently challenged the constitutionality of the FCA's seal provisions. In *American Civil Liberties Union v. Holder*, --- F.3d ----, No. 09-2086, 2011 U.S. App. LEXIS 6216 (4th Cir. Mar. 28, 2011), the Fourth Circuit affirmed a rejection of that challenge, holding that the seal provisions were permissible because the government has "a compelling interest in protecting the integrity of ongoing fraud investigations," and the seal provisions are "narrowly tailored to serve that compelling government interest." *Id.* at *20. Judge Gregory dissented, lamenting the "FCA's lack of transparency" and rejecting the government's justifications for the seal provisions. *Id.* at *45-51. On May 10, 2011, a petition for rehearing and rehearing en banc was filed.

**F. Fifth Circuit Recognizes "Indirect Reverse False Claims" Theory**

In *United States v. Caremark, Inc.*, 634 F.3d 808 (5th Cir. 2011), the Fifth Circuit held that a defendant can violate 31 U.S.C. § 3729(a)(7) under a theory of *indirect* reverse false claims. Under a reverse false claims theory, a person may be liable for making a false statement to conceal, avoid, or decrease an obligation to the government. In this case, Caremark administered pharmacy benefit plans for certain "dual-eligible" individuals, who are eligible for coverage under private health plans and Medicaid. Caremark argued, and the lower court agreed, that it did not impair an obligation to the government within the meaning of the FCA because *Caremark* did not owe a direct obligation to the federal government. *Id.* at 815.
The government argued, however, that Caremark violated the FCA by falsely stating that individuals were not covered by private plans and denying requests for reimbursement from state Medicaid agencies, which in turn caused the state Medicaid agencies to receive and retain federal funds to which they would not otherwise be entitled. States, the government argued, have a legal duty to seek reimbursement from a third party for dual-eligible individuals, as well as a legal duty to return federal funds if they are able to recover from third parties. The Fifth Circuit agreed, holding that Caremark could be liable for violating § 3729(a)(7) because "even if Caremark did not owe an 'obligation' to the Government, its false statements caused the state Medicaid agencies to make false statements to the Government, which is itself a violation" of the FCA. Id. at 817. The Act requires that a false statement impair "an obligation," the court reasoned, not the defendant's obligation. Id.

G. Court Declines to Adopt Public Policy Exception Allowing Relators to Violate Confidentiality Agreements

In United States ex rel. Cafasso v. General Dynamics C4 Systems, Inc., 637 F.3d 1047 (9th Cir. 2011), Cafasso, a former employee of General Dynamics, alleged that General Dynamics fraudulently withheld disclosure of new inventions that the government had the right to use and license. Id. at 1051-52. Anticipating a qui tam action, Cafasso copied a large amount of data from company computers, thereby violating a confidentiality agreement that Cafasso had executed at the start of her employment with General Dynamics. Id. Cafasso admitted that her appropriation of the files violated the confidentiality agreement, but she argued for the adoption of a public policy exception to enforcement of confidentiality agreements where the information is relevant to an FCA action. Id. at 1061-62. The Ninth Circuit acknowledged that such a public policy exception may have some merit but refused to adopt the exception in this case, holding that "it would not cover Cafasso's conduct given her vast and indiscriminate appropriation" of General Dynamics' files. Id. at 1062. The court explained that if it were to adopt a public policy exception to confidentiality agreements to protect relators, the relators must "justify why removal of the documents was reasonably necessary to pursue an FCA claim." Id.

H. A Defendant's Former General Counsel is Prohibited from Bringing Qui Tam Action Based on Confidential Information

A federal judge in the Southern District of New York recently dismissed qui tam claims brought by in-house counsel against his former employer. In United States ex rel. Fair Laboratory Practices Associates v. Quest Diagnostics Inc., No. 05 Civ. 5393 (RPP), 2011 U.S. Dist. LEXIS 37014 (S.D.N.Y. Apr. 5, 2011), the court not only concluded that the former general counsel should be prohibited from pursuing his claim because it relied on information he had received in a privileged context, it also disqualified his co-relators and the relators' counsel from further litigation as protection against disclosure of client confidences. Until now, courts have been relatively silent on the issue of whether an attorney who gains confidential information through his legal role with a company can then leave the company and use that same information to bring a whistleblower action against his former employer. See, e.g., United States ex rel. John Doe v. X Corp., 862 F. Supp. 1502, 1506 (E.D. Va. 1994) (after enjoining former counsel from voluntarily disclosing defendant's confidential documents and information to the government, and after defendant settled with the government, the court held former counsel was "ineligible to serve as a relator," for purposes of determining whether he was
entitled to a relator's-share award); *Bury v. Community Hospitals of Central California*, No. F036667, 2002 Cal. App. Unpub. LEXIS 1035, at *12 (Cal. App. May 8, 2002) (California appellate court affirmed the dismissal of a *qui tam* action under the state false claims act ("patterned after" the FCA) because the action was filed by an in-house counsel against his former employer, and the lawyer's duty of confidentiality prevented him from legally disclosing sufficient information to support his claims).

**IV. Conclusion**

The federal and state governments' relentless focus on fighting fraud, together with increased whistleblower incentives and protections, Congress's recent expansion of the FCA and state legislatures' efforts to mimic that expansion, indicate that the explosion in FCA activity we have reported on for the past few years, and that has continued unabated into the first half of 2011, is sure to continue into the foreseeable future. We will continue to monitor this activity and provide you with updates.


[16] Id.


[18] Id.

[19] Id. § 3.

[20] Id. § 9.


[29] Id.


[44] Id.


[47] Id.


[57] Id.


[59] Id.

[60] Id.


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[81] Id.


Gibson Dunn's lawyers have handled hundreds of FCA investigations and have a long track record of litigation success. Among other significant victories, Gibson Dunn successfully argued the landmark Allison Engine case in the Supreme Court, a unanimous decision that prompted Congressional action. See Allison Engine Co. v. United States ex rel. Sanders, 128 S. Ct. 2123 (2008). Our win rate and
immersion in FCA issues gives us the ability to frame strategies to quickly dispose of FCA cases. The firm has more than 30 attorneys with substantive FCA expertise and more than 20 former Assistant U.S. Attorneys and DOJ attorneys. For more information, please feel free to contact the Gibson Dunn attorney with whom you work or the following attorneys:

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