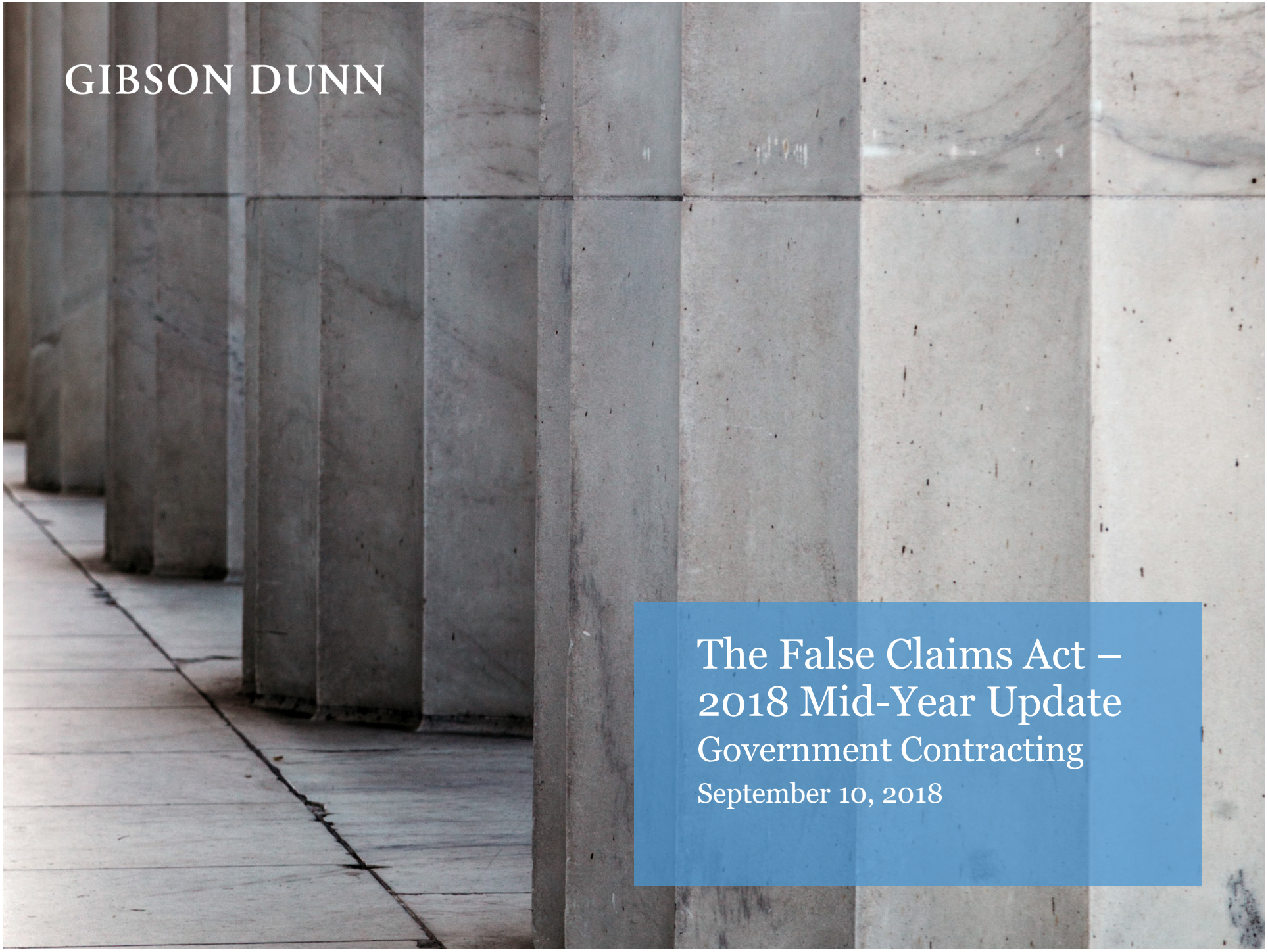


The False Claims Act – 2018 Mid-Year Update

Government Contracting

September 10, 2018

Today's Presenters

John Chesley is a partner in the Washington, D.C. office. He focuses his practice on white collar criminal enforcement and government contracts litigation. He represents corporations, audit committees, and executives in internal investigations and before government agencies in matters involving the Foreign Corrupt Practices Act, procurement fraud, environmental crimes, securities violations, antitrust violations, and whistleblower claims.

James Zelenay is a partner in the Los Angeles office and a member of the firm's Litigation Department. He is experienced in federal and state FCA matters and whistleblower litigation, in which he has represented a breadth of industries and clients.

Jonathan Phillips is a partner in the Washington, D.C. office. He regularly defends government contractors and their affiliates in government investigations under the False Claims Act and in related whistleblower litigation. Previously, he served as a Trial Attorney in DOJ's Civil Division, Fraud Section, where he investigated and prosecuted allegations of fraud under the FCA and related statutes.

Erin Rankin is an associate in the Washington, D.C. office, where she is a member of the firm's Litigation Department. She represents clients on government contracts matters relating to contract claims and terminations, suspension and debarment proceedings, internal investigations, and due diligence.

MCLE Certificate Information

- Most participants should anticipate receiving their certificate of attendance in four weeks following the webcast
- Virginia Bar Association members should anticipate receiving their certificate of attendance in six weeks following the webcast
- All questions regarding MCLE Information should be directed to Jeanine McKeown (National Training Administrator) at 213–229-7140 or jmckeown@gibsondunn.com

Today's Agenda

- False Claims Act Overview
- Intersection of Fraud & Contract Disputes Act Claims
- Department of Justice Enforcement & Policy Updates
- Recent & Notable Jurisprudence
- Recent & Notable Government Contractor FCA Settlements
- Best Practices for FCA Compliance

We encourage your questions throughout this presentation

False Claims Act Overview

The False Claims Act (FCA)

- The FCA, 31 U.S.C. §§ 3729-3733, is the federal government's ***primary weapon to redress fraud*** against government agencies and programs

- The FCA provides for recovery of ***treble damages*** and ***civil penalties*** from any "person" (natural or corporate entity) who knowingly submits or causes the submission of a false or fraudulent claim to the United States for money or property

- DOJ attorneys (Civil Division, as well as U.S. Attorneys' Offices) investigate and pursue FCA cases

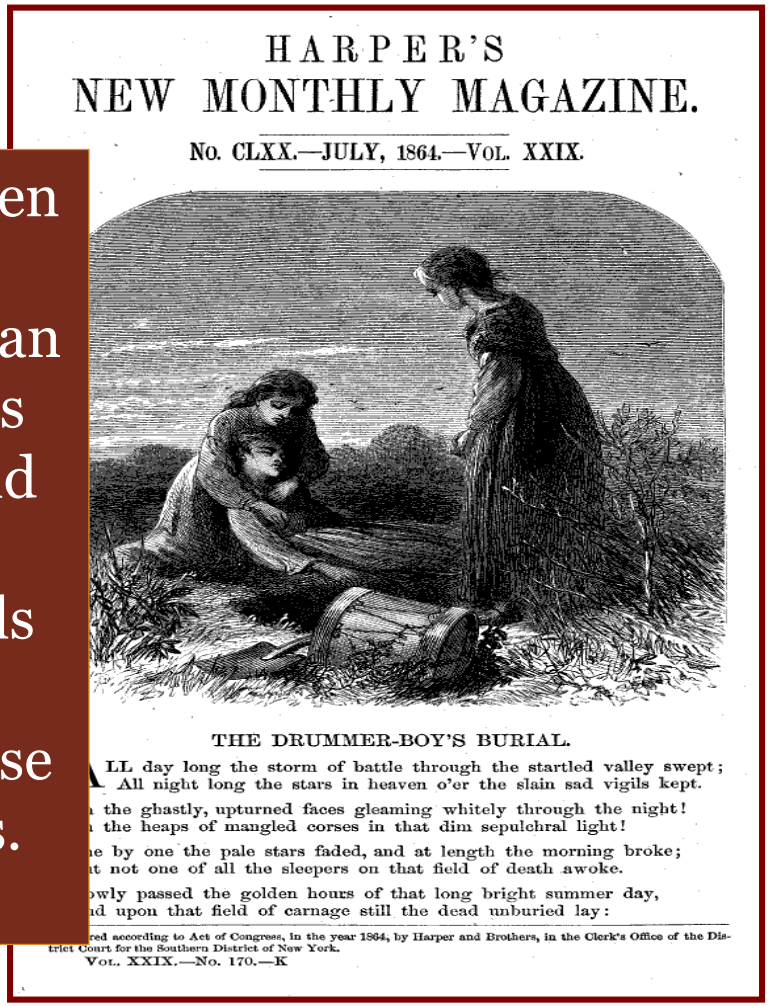
- DOJ is devoting more and more resources to pursuing FCA cases—and increasingly considering whether *qui tam* cases merit parallel criminal investigations

"It seems quite clear that the objective of Congress was broadly ***to protect the funds and property of the Government from fraudulent claims*** …."
Rainwater v. United States, 356 U.S. 590 (1958)

FCA – History

- Civil War profiteering prompted enactment of the "Lincoln Law" in 1863

For sugar [the government] often got sand; for coffee, rye; for leather, something no better than brown paper; for sound horses and mules, spavined beasts and dying donkeys; and for serviceable muskets and pistols the experimental failures of sanguine inventors, or the refuse of shops and foreign armories.



HARPER'S
NEW MONTHLY MAGAZINE.

No. CLXX.—JULY, 1864.—Vol. XXIX.

THE DRUMMER-BOY'S BURIAL.

LL day long the storm of battle through the startled valley swept;
All night long the stars in heaven o'er the slain sad vigils kept.
the ghastly, upturned faces gleaming whitely through the night!
the heaps of mangled corses in that dim sepulchral light!
e by one the pale stars faded, and at length the morning broke;
t not one of all the sleepers on that field of death awoke.
wly passed the golden hours of that long bright summer day,
d upon that field of carnage still the dead unburied lay:

red according to Act of Congress, in the year 1864, by Harper and Brothers, in the Clerk's Office of the District Court for the Southern District of New York.

Vol. XXIX.—No. 170.—K

R. Tomes, *The Fortunes of War*, Harper's New Monthly Magazine 228 (July 1864).

FCA – Key Provisions

31 U.S.C. § 3729(a)(1)	Statutory Prohibition	Summary
(A)	Knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval	False/Fraudulent Claim
(B)	Knowingly makes, uses or causes to be made or used, a false record or statement material to a false or fraudulent claim	False Record/Statement
(G)	Knowingly conceals or knowingly and improperly avoids or decreases an obligation to pay or transmit money or property to the Government	"Reverse" False Claim
(C)	Conspires to violate a liability provision of the FCA	Conspiracy

FCA – Scienter

- "Knowingly" requires scienter and is defined as:
  - Actual knowledge;
  - Deliberate ignorance; or
  - Reckless disregard
- Negligence is not actionable
- Specific intent to defraud is not required

FCA – Overview of Key FCA Theories

Factual Falsity

- False billing (*e.g.*, services not provided)
- Overbilling (*e.g.*, labor misclassification)

Legal Falsity / False Certification

- Express certification of compliance with legal requirements
- Submission of claim with representations rendered misleading as to goods / services provided

Promissory Fraud / Fraud in the Inducement

- Obtaining a contract through false statements or fraudulent conduct
- *U.S. ex rel. Marcus v. Hess*, 317 U.S. 537 (1943) (claims made by contractors who colluded on bids)

Reverse False Claims

- Improper avoidance of obligation to pay money to the government
- Retention of government overpayment

FCA – Damages and Penalties

Simple Damages Calculation

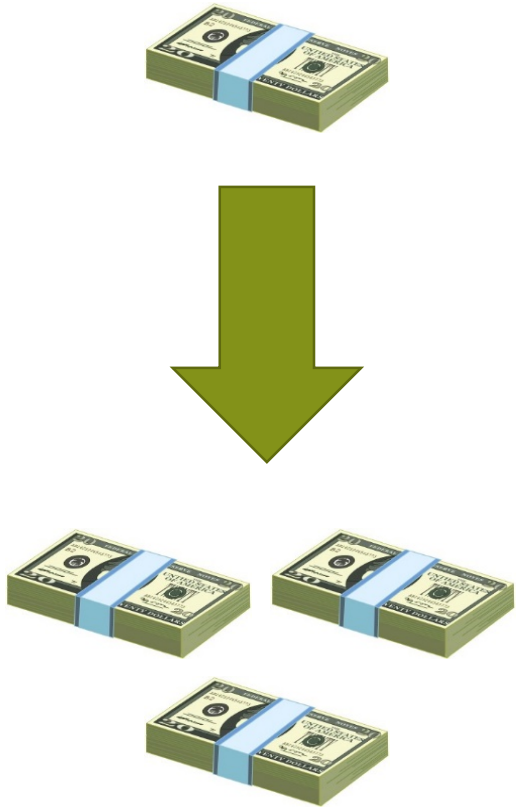
- Treble damages are traditionally calculated by multiplying the government's loss by three (e.g., if defendant charged government $100 for goods not received, damages would be $300)

Complex, Contested Damages Calculation

- Calculations are more complicated (and less certain) when the government receives goods or services it considers deficient or when there is a "false certification" or "promissory fraud"

Civil Penalty Per Claim

- Previously $5,500 to $11,000
- Nearly doubled effective August 1, 2016
- 2018 inflation adjustment increased to range of **$10,957 to $21,563** per violation
- Penalties are ***in addition to*** treble damages



FCA – Statute of Limitations

- For most FCA claims, the statute of limitations is **6 years**
- An extended limitations period of up to 10 years applies in select cases. 31 U.S.C. § 3731(b)(2) (permitting actions for "**3 years** after the date when facts material to the right of action are known or reasonably should have been known by the official of the United States charged with responsibility to act in the circumstances")
  - But not more than **10 years** from the violation
- Circuits are split in determining whether the up to **10-year** period is only available when the government files or intervenes in the FCA suit, as opposed to being pursued only by the relator after the government declines intervention
  - ***U.S. ex rel. Hunt v. Cochise Consultancy Inc.***, 887 F.3d 1081 (11th Cir. 2018)
    - Relators can employ the extended limitations period even in cases where the United States has declined to intervene
  - ***U.S. ex rel. Sanders v. N. Am. Bus Indus., Inc.***, 546 F.3d 288 (4th Cir. 2008)
    - "Section 3731(b)(2) extends the FCA's statute of limitations beyond six years only in cases in which the United States is a party"
  - ***U.S. ex rel. Sikkenga v. Regence Bluecross Blueshield of Utah***, 472 F.3d 702 (10th Cir. 2006)
    - "§ 3731(b)(2) was not intended to apply to private *qui tam* relators at all"

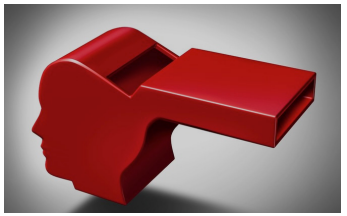
FCA – *Qui Tam* & Whistleblower Provisions

Qui Tam Provisions

- Enable so-called "relators" to bring cases in the government's name and recover **as much as 30%** of favorable judgment or recovery
- Allow government to intervene
  - An increasing number of whistleblower cases are pursued **without government intervention** (but often with government statement of interest)
- DOJ has virtually unlimited dismissal authority
  - Limited use historically, but the January 2018 Granston Memo may result in more frequent use of this power

Whistleblower Protections

- Protect employees and others (e.g., contract workers) from retaliation
- Relief may include double back pay and interest on back pay; reinstatement (at seniority level); and/or costs and attorneys' fees



"In short, sir, I have based the [*qui tam* provision] upon the old-fashioned idea of holding out a temptation and '**setting a rogue to catch a rogue**,' which is the safest and most expeditious way I have ever discovered of bringing rogues to justice."

Statement of Senator Howard, Cong. Globe, 37th Cong. 955-56 (1863)

Retaliation & the "But For" Test

DiFiore v. CSL Behring, LLC, 879 F.3d 71 (3d Cir. 2018)

- While Director of Marketing, plaintiff allegedly became concerned about company's purported efforts to market drugs for off-label use.
  - Plaintiff alleged that as a result she suffered adverse employment actions and resigned shortly thereafter.
  - The district court allowed the FCA retaliation claim to proceed to trial, and instructed the jury that the FCA retaliation provision required that the ***protected activity be the "but for"*** cause of adverse actions.
- On appeal, plaintiff argued that she should have only needed to prove that her ***protected activity was a "motivating factor"*** in the adverse actions
  - The Third Circuit held that an illegal motive must be ***the "but for" cause*** of the employer's adverse action

Whistleblower Protections Extend to Allegations Against Third Parties

O'Hara v. Nika Techs. Inc., 878 F.3d 470 (4th Cir. 2017)

- District court held that, in employee's action alleging that employer fired him for disclosing ***another company's*** alleged fraud on the government, the whistleblower protection provision only protected whistleblowing activity directed at the whistleblower's employer.
- On appeal, the Fourth Circuit held that the district court erroneously read a limitation into the FCA statute that did not appear in its text:
  - FCA statute described protected activity in terms of type of conduct disclosed by the whistleblower, but was silent on the relationship between the whistleblower and the subject of his disclosures.
  - Therefore, protected activity includes disclosures in furtherance of a viable FCA action ***against any person or company***.
- However, summary judgment was upheld because the employee did not disclose any conduct that reasonably could have led to a viable FCA action.

Additional Federal Contractor Whistleblower Protections

- **41 U.S.C. § 4712(a) provides additional protections to employees of government contractors and subcontractors**
  - Employees may not be discharged, demoted, or otherwise discriminated against as a reprisal for disclosing what the employee reasonably believes is evidence of:
    - ***gross mismanagement*** of a Federal contract or grant,
    - a ***gross waste*** of Federal funds,
    - ***an abuse of authority*** relating to a Federal contract or grant,
    - a substantial and specific danger to public health or safety, or
    - ***a violation of law, rule, or regulation*** related to a Federal contract (including the competition for or negotiation of a contract) or grant
  - Agency Inspectors General to investigate complaints and provide report to complainant, contractor / grantee, and Agency head
- **FAR 52.203-17, CONTRACTOR EMPLOYEE WHISTLEBLOWER RIGHTS AND REQUIREMENT TO INFORM EMPLOYEES OF WHISTLEBLOWER RIGHTS**
  - Requires the contractor to inform its employees in writing of employee whistleblower rights and protections under 41 U.S.C. § 4712
  - Flows down to subcontractors

Prohibition on Certain Confidentiality Agreements for Federal Contractors & Subcontractors

- **FAR 52.203-19, Prohibition on Requiring Certain Internal Confidentiality Agreements or Statements**
  - Prohibits requiring ***employees or subcontractors*** to sign or comply with internal confidentiality agreements or statements ***that prohibit or restrict from lawfully reporting*** waste, fraud, or abuse related to the performance of a Government contract to a designated investigative or law enforcement (*e.g.*, agency Office of the Inspector General)
  - Requires notification that any ***preexisting internal confidentiality agreements*** or statements covered by the clause, to the extent that such prohibitions and restrictions are inconsistent with the clause, are ***no longer in effect***

FCA – Public Disclosure and First-to-File Bars

- The **public disclosure bar** provides that relator's *qui tam* complaint cannot be "substantially the same" as allegations publicly disclosed in certain enumerated sources such as public hearings, government audits or reports, or the news media
  - *"Original source" exception*: A relator may proceed on publicly disclosed allegations if he is an "original source" of the allegations, meaning he ***voluntarily disclosed*** them before filing and has knowledge that is "***independent of and materially adds to***" the public disclosures
  - *2010 Amendments*: The public disclosure provisions were amended to the current language in 2010; previously, the bar contained slight differences in the public disclosure and original source provisions
- The **first-to-file bar** provides that, when a *qui tam* action is "***pending***," "***no person*** other than the Government ***may intervene or bring a related action based on the [same] facts***"
  - Generally requires dismissal of the second-filed action

Relators Must Have Direct & Independent Knowledge

***U.S. ex rel. Soloman v. Lockheed Martin*, 878 F.3d 139 (5th Cir. 2017)**

- Relator was the EVMS monitor for a subcontractor on the F-35 program and alleged that the sub- and prime contractor engaged in false cost reporting that led to receipt of higher award fees which they would have otherwise not received
- On the subcontractors' motion for summary judgment, the district court held that prior public disclosure barred relator's claims
- Fifth Circuit affirmed because DCMA and GAO reports had publicly disclosed the alleged issues with the contractors' cost reports, and the relator had no ***direct*** or ***independent*** knowledge ***separate from prior public disclosures***, as required to be original source of allegations:
  - Public disclosures ***need not allege fraud***; the question is "whether the relator *could have* synthesized an inference of fraud from the public disclosures"
  - Relator's knowledge about the connection between cost performance and award fees derived from portions of a contract that were publicly disclosed before the filing of his suit

Recent Jurisprudence – First-to-File Bar

U.S. ex rel. Wood v. Allergan, Inc.,
No. 17-2191 (2d Cir. Aug. 9, 2018)

- Relator, a former Allergan sales representative, alleged that the company provided free products to physicians in violation of the AKS and FCA
- Because two related suits had been filed before relator's suit (but remained under seal at that point), the district court and the circuit court addressed whether a violation of the FCA's first-to-file provision requires dismissal of the action or, rather, can be cured by an amendment to the complaint
- The Second Circuit sided with the D.C. Circuit and the Fourth Circuit, which had held that ***the first-to-file provision requires dismissal of the second-filed action***, and rejected relator's argument that amending the second-filed complaint cures the violation of the first-to-file provision

Mandatory Disclosure of "Credible Evidence" of FCA Violations

FAR 52.203-13 & 3.1003

- A contractor ***must timely disclose*** to the relevant Agency Inspector General and Contracting Officer, in writing, ***credible evidence*** that a principal, employee, agent or subcontractor has committed –
  - a violation of federal criminal law involving fraud, conflict of interest, bribery, or gratuity violations in Title 18 of the United States Code;
  - a ***violation of the civil False Claims Act***; or
  - Significant overpayment(s) on the contract, other than overpayments resulting from contract financing payments

  in connection with the award, performance, or closeout of the contract or a subcontract thereunder
- Applies to contracts for which the value is expected to exceed $5.5 million and the performance period is 120 days or more
- But *all contractors* are subject to this requirement, as knowing failure to disclose may result in suspension or debarment under FAR 3.1003(a)

What is "Credible Evidence"?

- "Credible evidence" is not defined in the FAR
- DFARS 252.246-7003 defines "credible information" in a different context (safety issues) as ***"information that, considering its source and the surrounding circumstances, supports a reasonable belief that an event has occurred or will occur"***
- The "credible evidence" standard should permit contractors reasonably adequate time to investigate the suspected misconduct
- For purposes of mandatory disclosure considerations, credibility determinations are made by the contractor, leaving open the possibility that the determination will be "second guessed" if a decision is made not to disclose and the Government otherwise becomes aware of it

- Internal investigations leading to "no credible evidence" findings should be ***well documented***, including the steps taken, evidence gathered, and remedial actions implemented in response
- Findings of "credible evidence" should be disclosed immediately

Intersection of Fraud & Contract Disputes Act Claims

Government Counterclaims in Fraud at the Court of Federal Claims

- **Anti-Fraud Provision of the Contract Disputes Act**, 41 U.S.C. § 7103(c)(2)
  - Additional liability for a claim if the "contractor is unable to support any part of the contractor's claim and it is determined that the inability is ***attributable to a misrepresentation of fact or fraud*** by the contractor"
  - The liability is for "an amount equal to the unsupported part of the claim plus all of the Federal Government's costs attributable to reviewing the unsupported part of the claim"
  - Government must show falsity and intent by a ***preponderance of the evidence***
- **Special Plea in Fraud** at the Court of Federal Claims, 28 U.S.C. § 2514
  - The contractor forfeits its claim if it "knew that its submitted claims were false" and "intended to defraud the government" by submitting the claims
  - Sometimes called the "Forfeiture Statute"
  - Government must prove by ***clear and convincing evidence***
  - Reckless disregard for the truth may be insufficient; the statute requires actual knowledge of falsity
  - Negligence, ineptitude, carelessness, slothfulness also do not rise to the level of deliberate fraud
- The Government may also assert **False Claims Act** violation as a counterclaim to a contractor CDA claim at the Court of Federal Claims

Government Counterclaims in Fraud at the Court of Federal Claims

MW Builders, Inc. v. United States, 134 Fed.Cl. 469 (2017)

- Contractor had certified a claim for government-caused delays in a construction contract
  - The Government counterclaimed under the anti-fraud provision of the CDA, the Special Plea in Fraud, and the False Claims Act, asserting identical theories of liability for all three
- Judge Susan Braden denied the Government's counterclaims
  - The contractor's use of ***estimated costs*** in its claim, rather than actual costs, was not evidence of specific intent to defraud under the CDA, particularly because the contractor did not expressly characterize the claim as being based on actual costs
    - Even though the contractor overstated its claim, it was based on subjective decisions made in assigning the costs to the project, which does not amount to specific intent to defraud
    - There was no evidence that the contractor had certified its claim "without an honest belief that it reflected what [the contractor] was owed"
  - Government's failure to establish CDA counterclaim for fraud means its special plea in fraud must also fail due to the heightened standard of proof (clear and convincing evidence)
  - Even though the contractor's review of its claim was "not as thorough as it could have been," there was insufficient evidence to establish reckless disregard for the truth under the FCA
    - Such reckless disregard would require failure to make a "minimal examination of the records" that would be "reasonable and prudent" under the circumstances

Boards of Contract Appeals' Jurisdiction over Fraud-Related Claims

- The Boards of Contract Appeals ***generally lack jurisdiction over fraud claims***, but not all appeals involving or relating to fraud must be dismissed
  - ***Laguna Constr. Co. Inc. v. Carter***, 828 F.3d 1364 (Fed. Cir. 2016)
    - Although ASBCA lacks jurisdiction over fraud defense, it does have jurisdiction over the Government's affirmative defense of prior material breach based on fraud provided the ASBCA does not have to make ***factual determinations of fraud***
    - The COO had pleaded guilty to criminal fraud for receiving kickbacks in exchange for awarding subcontracts that were the subject of the contractor's claim, and such admissions were sufficient to impute to the company
    - Government did not have to know about the prior material breach at the time it committed its subsequent breach of non-payment in order to assert defense
  - ***Int'l Oil Trading Co.***, ASBCA Nos. 57491 *et al.*, 18-1 BCA ¶ 36,985; ***ABS Dev. Corp.***, ASBCA No. 60022, 17-1 BCA ¶ 36,842
    - The bar on the ASBCA's jurisdiction over fraud claims does not extend to the Government's affirmative defense that the contract was *void ab initio* because it was obtained through fraud or bribery
    - ASBCA has jurisdiction to decide "whether the contractor can establish that he has a contract with the Government in the first place"

Contracting Officer Final Decisions and Claims "Involving Fraud"

- Pursuant to 41 U.S.C. 7103(c)(2), Contracting Officers do not have authority to issue final decisions for claims "involving fraud"

PROTEC GmbH, ASBCA No. 61161, 18-1 BCA ¶ 37,010

- Contractor submitted claim regarding a negative CPARS evaluation, and a second claim for unpaid invoices
  - The COR had alleged that the contractor had fraudulently submitted invoices for work not performed and misrepresented the qualifications of its personnel
  - The CO denied the contractor's claims in two COFDs, and the contractor appealed to the ASBCA
  - The Government moved to dismiss for lack of jurisdiction arguing that the final decisions were invalid because the CO knew the contractor was under investigation for fraud
- ASBCA denied the motion because ***suspicion of fraud was not the basis for the COFDs***, let alone the only basis. Instead, the COFDs were based on authorized rationales, *e.g.*, failure to provide requisite documentation
- The mere fact of ongoing investigations of fraud which encompasses the events underlying the COFDs does not divest the board of jurisdiction

Enforcement & Policy Updates

Government Players

Department of Justice

DOJ is devoting more and more resources to pursuing FCA cases—and considering whether *qui tam* cases merit criminal investigation

Contracting & Support Agencies

Contracting agencies and support agencies (such as DCAA) increasingly view contract disputes as false claims

Cooperation

Inspectors General

Department of Defense IG

General Services Administration IG

Contracting Agency IG

By the Numbers: 2017

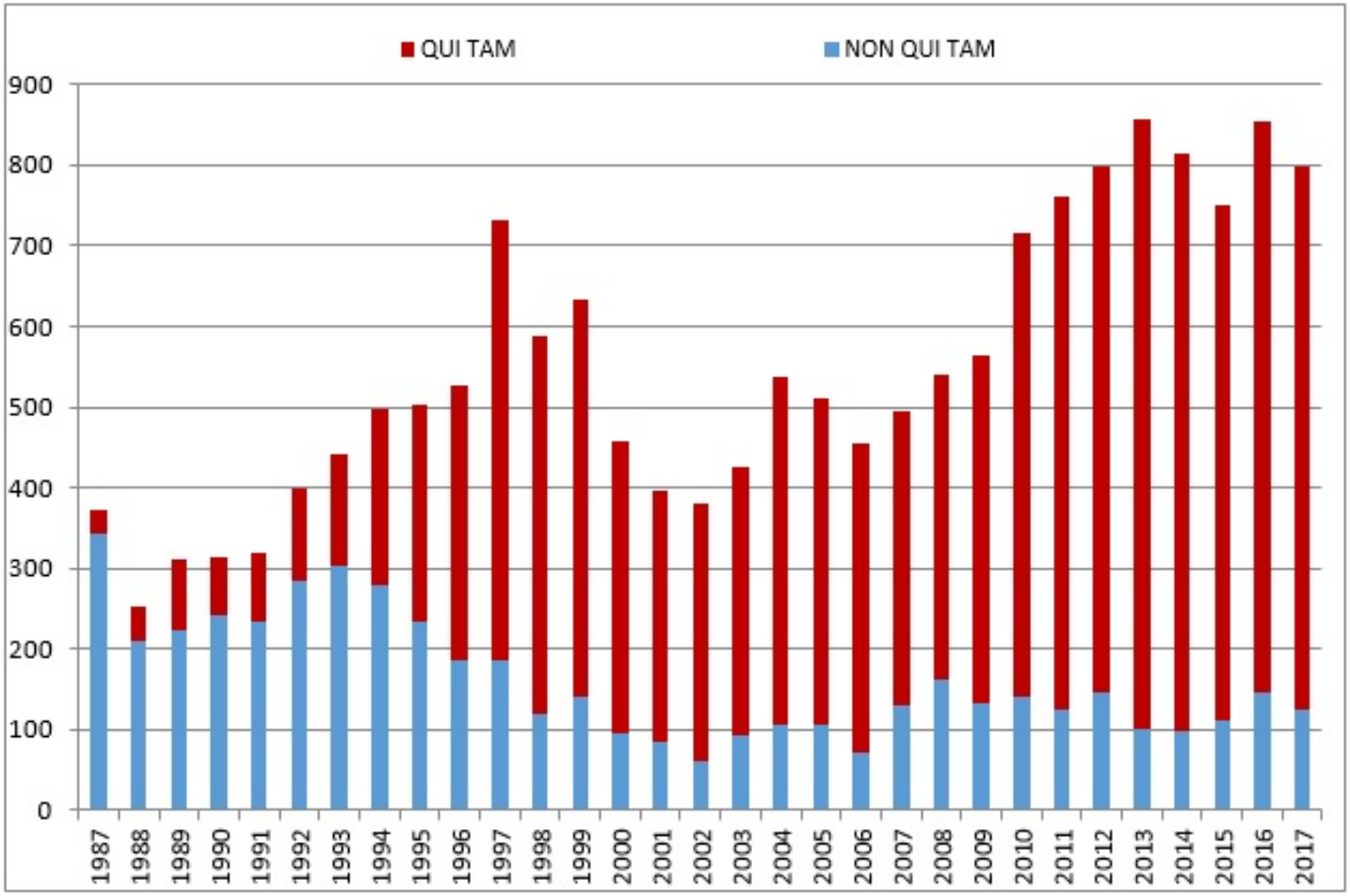
$3.7 billion
Civil Settlements and Judgments Under the FCA

799
New FCA Cases Filed

84 percent
Percentage of New FCA Cases Initiated by a Whistleblower

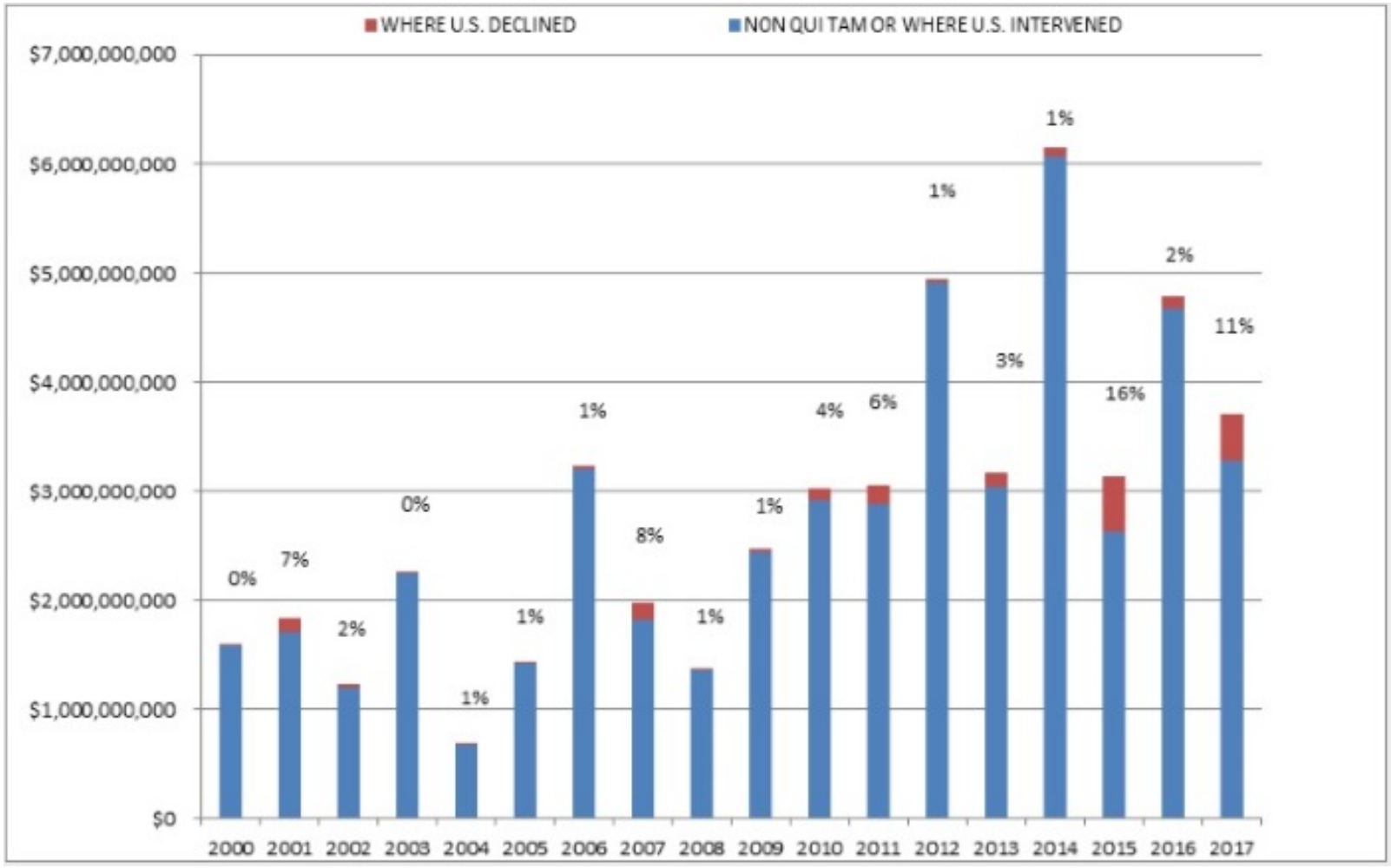
89 percent
Percentage of Overall Federal Recovery from Cases in which the Government Intervened

Number of New FCA Suits (1987-2017)



799 new cases in 2017

Declined Cases in FCA Settlements / Judgments (2000–2017)



Source: DOJ "Fraud Statistics – Overview" (Dec. 21, 2017)

By the Numbers: Mid-Year 2018

>$600 million

FCA recoveries from ***settlements*** in the first half of 2018

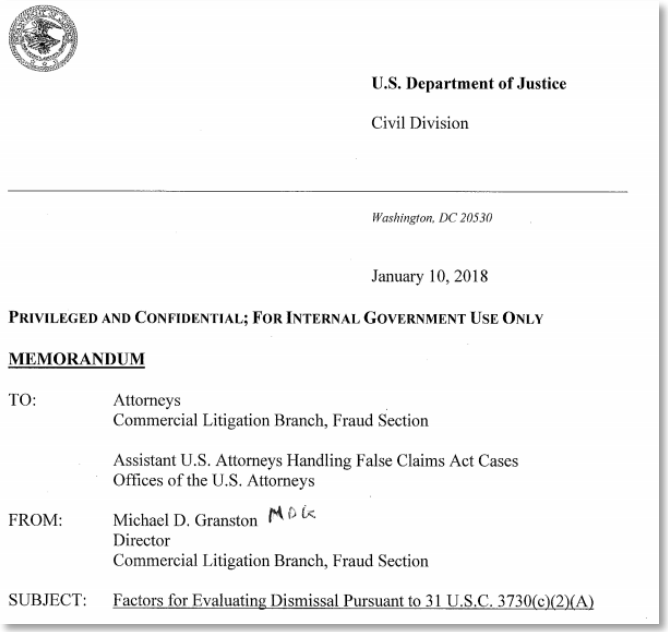
$114 million

Judgments from FCA cases in the first half of 2018

9th?

After ***8 consecutive years exceeding $3 billion*** in FCA recoveries, the streak is in jeopardy this year

The Granston Memo (Jan. 10, 2018)



U.S. Department of Justice

Civil Division

Washington, DC 20530

January 10, 2018

PRIVILEGED AND CONFIDENTIAL; FOR INTERNAL GOVERNMENT USE ONLY

MEMORANDUM

TO: Attorneys
Commercial Litigation Branch, Fraud Section

Assistant U.S. Attorneys Handling False Claims Act Cases
Offices of the U.S. Attorneys

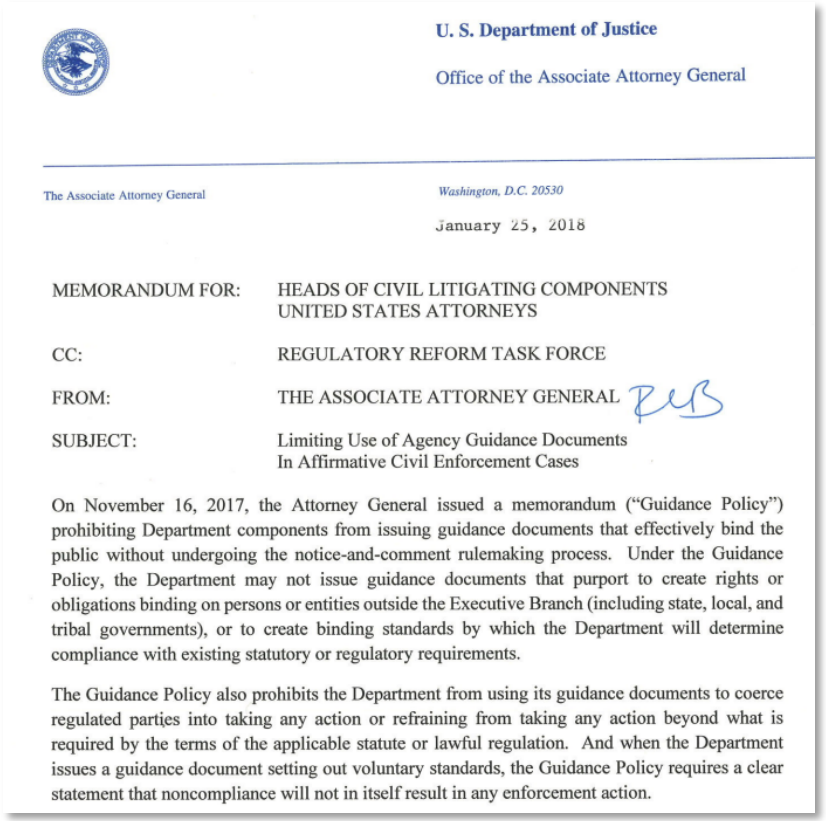
FROM: Michael D. Granston MDG
Director
Commercial Litigation Branch, Fraud Section

SUBJECT: Factors for Evaluating Dismissal Pursuant to 31 U.S.C. 3730(c)(2)(A)

- This internal memo focuses on DOJ's use of its dismissal authority (31 U.S.C. § 3730(c)(2)(A))
- Responding to "record increases in *qui tam* actions" and acknowledging that its "rate of intervention has remained relatively static," DOJ underscored that dismissal is "an important tool to advance the government's interests, preserve limited resources, and avoid adverse precedent"
- DOJ attorneys should consider dismissal for:
  - Facially meritless or duplicative qui tam suits
  - Cases that agencies view as interfering with policies / agency programs
  - Suits that threaten DOJ's litigation positions
  - Cases that might reveal classified information
  - Low expected-value suits
  - Actions that frustrate the government's investigative efforts

The Brand Memo (Jan. 25, 2018)

- Agencies commonly issue guidance documents interpreting legislation and regulations, and the government has sometimes employed evidence that a defendant violated such guidance to prove a violation of the underlying statute or regulation.
- The Brand Memo **prohibits DOJ from**:
  1. Using noncompliance with other agencies' "guidance documents as a basis for proving violations of applicable law in" affirmative civil enforcement cases, and
  2. Using "its enforcement authority to effectively convert agency guidance documents into binding rules."



U. S. Department of Justice

Office of the Associate Attorney General

The Associate Attorney General

Washington, D.C. 20530

January 25, 2018

MEMORANDUM FOR: HEADS OF CIVIL LITIGATING COMPONENTS
UNITED STATES ATTORNEYS

CC: REGULATORY REFORM TASK FORCE

FROM: THE ASSOCIATE ATTORNEY GENERAL

SUBJECT: Limiting Use of Agency Guidance Documents
In Affirmative Civil Enforcement Cases

On November 16, 2017, the Attorney General issued a memorandum ("Guidance Policy") prohibiting Department components from issuing guidance documents that effectively bind the public without undergoing the notice-and-comment rulemaking process. Under the Guidance Policy, the Department may not issue guidance documents that purport to create rights or obligations binding on persons or entities outside the Executive Branch (including state, local, and tribal governments), or to create binding standards by which the Department will determine compliance with existing statutory or regulatory requirements.

The Guidance Policy also prohibits the Department from using its guidance documents to coerce regulated parties into taking any action or refraining from taking any action beyond what is required by the terms of the applicable statute or lawful regulation. And when the Department issues a guidance document setting out voluntary standards, the Guidance Policy requires a clear statement that noncompliance will not in itself result in any enforcement action.

The Brand Memo (cont.)

- Under the Brand Memo, DOJ will be more limited in its ability to wield guidance affirmatively
- Guidance may still be relevant for other reasons: DOJ may continue to use "**agency guidance documents for proper purposes**":
  - where a guidance document "simply explain[s] or paraphrase[s] legal mandates from existing statutes or regulations"; or
  - as "evidence that a party read such a guidance document to help prove that the party had requisite knowledge of the mandate."
- Nothing in the Brand Memo suggests that the government will be able to use this policy decision to limit a defendant's use of guidance documents **to defend** itself.

FCA – Additional DOJ Policy Initiatives (2018)

- In a June 14, 2018 speech, ***Acting Associate Attorney General Jesse Panuccio*** described three additional DOJ policy initiatives to reform FCA enforcement:

Cooperation Credit	Whereas DOJ has delineated the benefits of cooperation in other investigations (e.g., antitrust, FCPA), less guidance has been available in the FCA space
Compliance Program Credit	DOJ will "reward companies that invest in strong compliance measures"
Efforts to Prevent "Piling On"	DOJ attorneys will promote coordination within the agency and with other regulatory bodies to ensure that defendants are subject to fair punishment and receive the benefit of finality that should accompany a settlement

Recent Jurisprudence

Implied (False) Certification & Materiality

Universal Health Srvs., Inc. v. U.S. ex rel. Escobar, 136 S. Ct. 1989 (2016)

- Relator brought FCA suit against leading nationwide provider of mental health services, alleging that hospital submitted payment claims to Medicaid program for services rendered by personnel who did not meet state-regulated staffing qualifications
- Implied certification theory advanced was that when defendant submitted the claims, it ***impliedly certified compliance with all applicable regulations***
- The Court held that implied certification theory can provide a basis for FCA liability, "at least where two conditions are satisfied":
  1. "the claim does not merely request payment, but also makes ***specific representations about the goods or services provided***," and
  2. "the defendant's ***failure to disclose noncompliance with material statutory, regulatory, or contractual requirements*** makes those representations misleading half-truths"
- The Court declined to decide "whether ***all*** claims for payment ***implicitly*** represent that the billing party is legally entitled to payment"

Implied (False) Certification & Materiality

Escobar (continued)

- Materiality "look[s] to the ***effect*** on the ***likely or actual behavior*** of the recipient of the alleged misrepresentation." Violation is "material" if:
  - "A reasonable man would attach importance to [the misrepresented information] in determining his choice of action in the transaction"; or,
  - "the defendant knew or had reason to know that the recipient of the representation attaches importance to the specific matter 'in determining his choice of action,' even though a reasonable person would not"
- Materiality does not "rest on a single fact or occurrence as always determinative," but must be ***weighed in the context of each case***:
  - Government's right to refuse payment based on noncompliance is insufficient, without more
  - Noncompliance ***cannot be minor or insubstantial***: Government may not require "contractors to aver their compliance with the entire U.S. Code and [CFR]," then deem all violations material
  - Proof can include, but is not limited to, "evidence that the defendant knows that the ***Government consistently refuses to pay claims in the mine run of cases*** based on noncompliance with the particular statutory, regulatory or contractual requirement"
  - Government's payment of "particular claim," or practice of paying "particular type of claims," with "actual knowledge" of violation of certain requirements, is "strong evidence" that those requirements are not material
  - Some courts have considered the Government's decision to intervene

Implied (False) Certification & Materiality

United States ex rel. Rose v. Stephens Inst., No. 17-15111 (9th Cir., Aug. 24, 2018)

- Former admissions representatives for an art school that received federal financial aid alleged the school had compensation programs that incentivized admissions officers to enroll students, contrary to federal statute, regulation, and contract for federal funding
- Ninth Circuit upheld denial of defendant's motion for summary judgment, holding that Relators alleged sufficient evidence that the school's noncompliance was material under *Escobar*:
  - School promised in its program participation agreement that it would comply with prohibition on incentive compensation, therefore the funds were allegedly conditioned on compliance
  - Court reviewed the Department of Education's ***treatment of similar violations***:
    - Court found there was evidence that the Department "cared" about the violations of other schools
    - Past enforcement of the incentive compensation ban was ***probative***, but not ***sufficient***
    - Court found lacking evidence that the Department had paid funds with knowledge of noncompliance
  - Court considered the ***magnitude*** of the alleged violations
    - Court found incentive payments allegedly were substantial
    - Court noted that "small occasional perks" such as $10 gift cards or coffee would be insufficient
- Affirmed that both *Escobar* conditions must be met

Government Knowledge as Evidence of Immateriality

U.S. ex rel. Spay v. CVS Caremark Corp., 875 F.3d 746 (3d Cir. 2017)

- Relator brought *qui tam* alleging that Medicare Part D sponsors used "dummy" prescriber information to facilitate payment of prescription drug claims
  - Practice of using dummy prescriber IDs was a temporary work-around for authorized claims that "errored out" due to missing or incorrectly formatted prescriber information
- Third Circuit formally recognized the "***government knowledge inference***" defense to scienter, which requires that:
  - (1) the government agency knew about the alleged false statement(s); and
  - (2) the defendant knew the government knew
  - Although the record established that government employees responsible for authorizing payments "knew that dummy identifiers were being used," there lacked evidence that defendants knew the government knew
- However, the Third Circuit ***upheld dismissal for lack of materiality*** under *Escobar*:
  - Government knew of the practice and nevertheless continued to pay
  - Misstatements at issue actually "allowed patients to get their medication," and "are precisely the type of 'minor or insubstantial' misstatements where '[m]ateriality . . . cannot be found'"

Government Knowledge as Evidence of Immateriality

United States v. Salus Rehab., LLC, 304 F. Supp. 3d 1258 (M.D. Fla. 2018)

- Set aside a $350 million FCA jury verdict against a nursing home operator finding it had submitted false claims by failing to maintain a comprehensive care plan that was "ostensibly required by Medicaid regulation," alongside other relatively minor infractions, for lack of materiality and scienter
  - "[T]he evidence and the history of this action establish that the federal and state governments regard the disputed practices with ***leniency or tolerance or indifference*** or perhaps with ***resignation to the colossal difficulty*** of precise, pervasive, ponderous, and permanent record-keeping in the pertinent clinical environment"
  - Evidence demonstrated "not a single threat of non-payment, not a single complaint or demand, and not a single resort to an administrative remedy or other sanction for the same practices that result in the enormous verdict at issue"
- Relator should not win based only on the theory that "a handful of paperwork defects" and "failure to maintain care plans made" defendants' claims to Medicare and Medicaid false or fraudulent
- Government contractors should consider this analysis when determining whether they have credible evidence of a FCA violation to trigger ***mandatory disclosure***

Government Knowledge as Evidence of Immateriality

U.S. ex rel. Folliard v. Comstor Corp., 308 F. Supp. 3d 56 (D.D.C. 2018)

- Relator alleged that the defendants sold products under their Federal Supply Schedule contract that were noncompliant with the Trade Agreements Act
- District court granted defendants' motion to dismiss because (among other reasons) the relator failed to allege sufficient materiality:
  - Relator made no allegations that the Government "consistently refuses to pay claims in the mine run of cases based on noncompliance with" the TAA
  - Relator made no allegations that the Government took any action against defendants after investigating, such as terminating the contracts or sending notices of noncompliance
    - To the contrary, the GSA had expressed willingness to work with vendors to address TAA noncompliance, rather than reject claims, which showed that the GSA was willing to make payments even knowing of TAA violations
  - "The requirement of demonstrating materiality would seem especially crucial here where the government ***declined to intervene after almost five years of investigation***, and has also declined to intervene in similar cases brought by this relator alleging similar fraudulent activity"

U.S. ex rel. Berkowitz v. Automation Aids, Inc., 896 F.3d 834 (7th Cir. 2018)

- Upheld dismissal of similar FCA claims alleging TAA noncompliance
- "It also seems worth noting that the fact that the government has allegedly paid millions of dollars for the non-compliant products suggests that Berkowitz cannot satisfy the materiality prong of the implied certification theory."

Magnitude of the Alleged Violation as Evidence of Immateriality

U.S. ex rel. Bachert v. Triple Canopy, Inc., Case No. 1:16–cv–456, 2018 WL 3018219 (E.D. Va. June 8, 2018)

- Relator was a former employee of a contractor that provided worldwide security services to the Department of State, including at the U.S. embassy in Baghdad
  - Alleged that an individual who worked as an armorer at the embassy failed to inspect weapons and failed to record his inspections
  - Also alleged that the contractor retaliated against him by transferring him back to the U.S. and demoting him
- District court granted summary judgement that the undisputed facts showed that the alleged false certifications lacked materiality under *Escobar*:
  - The allegations of failure to inspect "a handful of weapons and falsification of the accompanying inspection records" were "***minor or insubstantial***" non-compliances amounting to "***minor missteps***," particularly in relation to the overall size of the contract
  - State Department had investigated the allegations, but ***continued making payments*** and ***renewed the defendant's contract*** numerous times
- However, the relator's FCA retaliation claims survived summary judgment

Materiality & Fraud in the Inducement

Marsteller ex rel. U.S. v. Tilton, 880 F.3d 1302 (11th Cir. 2018)

- Relators were former sales and business development directors for a contractor that sold helicopters to the military
  - Alleged that defendants failed to comply with FAR 52.203-13, Contractor Code of Business Ethics and Conduct, and the Truth in Negotiations Act, in violation of the FCA under implied false certification and fraud in the inducement theories
  - The district court dismissed (prior to *Escobar*), holding that compliance must be a "prerequisite to payment" and that compliance with FAR 52.203-13 and TINA were not express conditions of payment
- Eleventh Circuit remanded the case in light of *Escobar*, and reiterated that whether compliance with contractual, statutory or regulatory obligations was an express condition of payment is ***relevant*** but not ***dispositive***
  - Further held that ***fraud in the inducement*** can support an FCA action, if the contractor's promise to comply with various provisions of law were false when made, and the Government would not have entered into the contract had it known of the defendants' unwillingness to comply

Reverse False Claims

U.S. ex rel. Patzer v. Sikorsky Aircraft Corp., No. 11-C-0560, 2018 WL 3518518 (E.D. Wis., July 20, 2018)

- Government can pursue ***direct and reverse false claims*** "relating to the same money," based on (1) the false claim for the money and (2) the failure to return it
- Contractor's certified annual indirect costs submission could be reverse false claims, even though they involved the same money as direct submissions, because they were allegedly additional wrongful acts designed to prevent the government from obtaining the money that was fraudulently claimed
- "Once someone receives the proceeds of a direct false claim, it is arguable that he has an obligation to immediately repay those very proceeds. If the person has an immediate obligation to repay, ***then any person who commits a direct false claim also commits a reverse false claim as soon as he receives the government's money unless he immediately repays it***"
- Court noted that if the government prevails, it can only recover treble damages once, but can recover civil penalties for both the direct and reverse false claim

Fed. R. Civ. P. 9(b)

- Federal Rule of Civil Procedure 9(b) requires FCA plaintiffs to plead allegations with particularity (heightened pleading requirement)

U.S. ex rel. Ibanez v. Bristol-Myers Squibb Co., 874 F.3d 905 (6th Cir. 2017)

- District court dismissed employees' FCA suit alleging that pharmaceutical companies engaged in a nationwide scheme to promote an anti-psychotic drug for off-label uses
- Sixth Circuit affirmed because ***relators failed to plead a specific, representative false claim submitted to the government for payment***
  - Refused to apply the "personal knowledge" exception to the Circuit's otherwise strict application of Rule 9(b)'s particularity requirements
  - Relators' allegations only involved ***personal knowledge of an allegedly fraudulent scheme*** rather than of the defendant's billing practice; the Sixth Circuit refused to allow the complaint to proceed based solely on their "reliable indicia" that claims actually were submitted
  - A complaint must "***adequately allege the entire chain—from start to finish***—to fairly show defendants cause[d] false claims to be filed," including any "specific intervening conduct" along the chain

Anti-Kickback Act

- The Anti-Kickback Act prohibits attempting, offering, providing, soliciting, or accepting kickbacks "in connection with a prime contract or a subcontract relating to a prime contract." 41 U.S.C. 8701 *et seq*.
- A kickback is "any money, fee, commission, credit, gift, gratuity, thing of value, or compensation of any kind that is provided to a prime contractor, prime contractor employee, subcontractor, or subcontractor employee to improperly obtain or reward favorable treatment"

U.S. ex rel. Patzer v. Sikorsky Aircraft Corp., No. 11-C-0560, 2018 WL 3518518 (E.D. Wis., July 20, 2018)

- Dismissed kickback claims alleged to be made between two sister subsidiaries of Sikorsky
- Court held that the parties' ***independence*** from one another—*i.e.*, the choice to deal with one another—is "implicit" in the definition of kickbacks
  - Without independence, "one party's providing something of value to the other ***could not be viewed as an incentive or reward for favorable treatment***–the favorable treatment would occur whether or not the thing of value changed hands"
  - Because the two subsidiaries were both controlled by the parent company, and an official of the parent company directed the subsidiaries to work together on the contract, the relationship lacked independence
  - Dismissed under Fed. R. Civ. P. 12(b)(6) for lack of plausible allegations under AKA

Kickbacks

U.S. ex rel. Greenfield v. Medco Health Sol's, Inc., 880 F.3d 89 (3d Cir. 2018)

- Relator claimed a pharmacy violated the FCA by falsely certifying that it complied with the Anti-Kickback statute when seeking reimbursement for the care provided to referred patients
- Third Circuit affirmed dismissal of *qui tam* case – "***the taint***" of the alleged kickbacks ***does not automatically render every reimbursement claim false***
- For summary judgment, it is not enough for a relator to show merely that the defendant "submitted federal claims while allegedly paying kickbacks"
- Relator must demonstrate at least one false claim, i.e., "at least one claim that covered a patient who was recommended or referred" in violation of the Anti-Kickback Statute

- Government contractors should consider this analysis when determining whether they have "credible evidence" of a False Claims allegation that would trigger ***mandatory disclosure***

Recent & Notable Settlements

Defective Goods

Toyobo Co. Ltd. of Japan and its American Subsidiary (March 15, 2018)

- A Japanese fiber manufacturer and its American subsidiary sold defective fiber used in bulletproof vests sold to law enforcement agencies
- Companies allegedly sold defective Zylon fiber used in bulletproof vests, published misleading data that understated the defect, and advocated for the continued sale of Zylon-containing vests even after a body armor manufacturer recalled the vests
- Paid approximately ***$66 million*** to settle; whistleblower (former research director for manufacturer Second Chance) received over ***$5.7 million***

3M Co. (July 25, 2018)

- 3M Co. and its predecessor, Aearo Technologies, Inc., allegedly knowingly sold defective earplugs to the Defense Logistics Agency
- Earplugs were allegedly too short for proper use and could loosen from ears, hampering their effectiveness in some individuals, and 3M allegedly failed to disclose the defect
- Agreed to pay ***$9.1 million*** to settle; whistleblower received ***$1.9 million***

Unallowable Costs

North American Power Grp. Ltd (July 6, 2018) (Unallowable Costs)

- NAPG and its owner and president agreed to pay the United States ***$14.4 million*** to resolve allegations that they violated the FCA by submitting fraudulent claims under a cooperative agreement with the Department of Energy
- The claimed costs allegedly were for expenses incurred to pay legal fees, car payments, jewelry, international travel, and other personal items unrelated to the scope of work under the cooperative agreement

Overbilling

Inchcape Shipping (May 29, 2018) (Overbilling)

- A foreign-based federal contractor and its subsidiaries provided goods and services to Navy ships at ports in several regions throughout the world, such as food and other subsistence items, waste removal, telephone services, ship-to-shore transportation, force protection services and local transportation
- The companies allegedly overbilled in excess of contract rates and double-billed the Navy
- The companies agreed to pay ***$20 million*** to resolve allegations; the whistle-blowers in the case, three former employees of the contractor, will receive approximately ***$4.4 million***

Small Business Eligibility

ADS Inc. (Aug. 10, 2017)

- Contractor and subsidiaries paid ***$16 million*** to settle allegations that they conspired with, and caused, small businesses to submit false claims for payment related to fraudulently obtained small business contracts
- The companies allegedly induced the government to award certain contracts by misrepresenting eligibility requirements, including the small businesses' affiliation with the defendant, size, and standing
- In addition, the defendant allegedly engaged in bid rigging to distort or inflate prices charged to the government under the contracts
- One of the largest settlements involving alleged fraud implicating small business contract eligibility

Zoladz Construction Co. Inc. et al. (Oct. 3, 2017)

- ZCCI, Arsenal Contracting, and Alliance Contracting, along with two owners, paid more than ***$3 million*** to settle allegations that they improperly obtained federal set-aside contracts designated for service-disabled veteran-owned small businesses

Best Practices for FCA Compliance

Minimizing Exposure

- Set a compliance-focused "tone from the top"
- Adopt and implement reasonable compliance policies and controls
  - Required by FAR 52.203-13, and strongly advised in FAR 3.1002
  - A strong internal compliance program may not prevent a rogue employee from committing fraud, but it may help to defeat scienter
- Train employees on compliance policies and reporting options
- Monitor and audit
- Investigate and remediate
  - Develop standards and procedures to prevent, detect, and respond to improper conduct

Risk Assessment

- Monitor government interactions
- Understand express certifications in government contracts and programs
- Account for use of government contract funds and grants
- Evaluate business partners, especially government subcontractors
- Document the government's knowledge, awareness, and ratification of contractual and programmatic deviations
- Take care in responding to billing inquiries as incorrect explanations may be used as evidence of fraud
- Documentation and transparency are key

Investigation Responsiveness

- Critical to uncover allegations of FCA-related complaints as early as possible
- Foster an environment in which employees and other interested parties report concerns internally
- *Qui tam* warning signs
  - HR issues;
  - Exit interview statements;
  - Unexpected audits;
  - Requests for billing explanations;
  - Increased web activity; and
  - Former employees contacted
- Proactively engage with and present your case to DOJ and USAO
- The most critical juncture is the government's intervention decision

Gibson Dunn 2018 False Claims Act Summer Webcast Series

- This has been one in a series of webcasts on the FCA and various industry sectors in which our clients and friends have an interest
  - FCA and Drug & Device Industry (August 22)
  - FCA and Financial Services Sector (August 29)
  - **FCA and Government Contracting (September 10)**
- The series is available at http://www.gibsondunn.com/publications/pages/webcasts.aspx
- If you have any unanswered questions, please feel free to contact any one of us at:
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