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Assessing PE Risk After Mass. False Claims Act Amendments

By **Jake Shields, Michael Dziuban and Danilo Risteski** (February 28, 2025, 5:11 PM EST)

In a significant development for private equity firms that operate in the healthcare and life science spaces, lawmakers in Massachusetts recently expanded the state's civil fraud enforcement powers against private equity firms and other investors.

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On Jan. 8, Gov. Maura Healey signed the state's H.B. 5159, titled "An Act Enhancing the Market Review Process," into law. In addition to expanding reporting requirements for private equity transactions, the act amends the Massachusetts False Claims Act to impose civil liability on owners or investors in entities that violate the Massachusetts FCA without disclosing it to the state within 60 days of finding out.[1]

The act represents a dramatic expansion of potential civil liability for private equity firms and other investors — regardless of their location — whose companies do business with the Massachusetts government.

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The impetus for the act appears to be increased concerns by state lawmakers over the patient care implications of private equity investment in the healthcare industry. However, the act sweeps broadly to cover investors in all industries.

The act also comes on the heels of growing scrutiny of private equity firms by the U.S. Department of Justice, which made clear during each of the last two administrations that enforcement of the federal False Claims Act against private equity firms was a DOJ priority.[2]

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Overview of the State Act

The Massachusetts FCA prohibits various types of fraudulent conduct against the state and its political subdivisions.[3] Similar to the federal FCA, the Massachusetts FCA prohibits the knowing presentment of false or fraudulent claims for payment and the knowing use of material false records or statements in the submission of claims.[4]

The Massachusetts FCA also contains a reverse provision, which, like its federal counterpart, prohibits the knowing use of a false or fraudulent statement that is "material to an obligation to pay ... money ... to the commonwealth," as well as the knowing concealment or improper avoidance of an obligation to pay money to the commonwealth.[5]

Unlike the federal FCA, the Massachusetts FCA also imposes liability on those who benefit from unintentional false claims, or overpayments discovered after the fact, within 60 days.[6]

The Massachusetts FCA applies to any person, whether or not they're a resident of Massachusetts, who engages in covered conduct as to claims for payment made to the commonwealth, its political subdivisions, officers, employees, agents, representatives and contractors, and/or as to funds the person receives or retains to which they are not entitled.[7]

Like the federal FCA, the statute imposes treble damages and per-violation civil penalties.[8]

Amendments

The act, which is set to go into effect on April 8 of this year, expands the scope of existing beneficiary liability under the Massachusetts FCA to apply explicitly to private equity firms and other investors.

The act amends the Massachusetts FCA to impose liability on any person who "has an ownership or investment interest in any person who violates [the Massachusetts FCA], ... knows about the violation, and fails to disclose the violation to the commonwealth or a political subdivision thereof within 60 days of identifying the violation."[9]

The act defines "ownership or investment interest" as any:

> any: (1) direct or indirect possession of equity in the capital, stock or profits totaling more than 10 percent of an entity; (2) interest held by an investor or group of investors who engages in the raising or returning of capital and who invests, develops or disposes of specified assets; or (3) interest held by a pool of funds by investors, including a pool of funds managed or controlled by private limited partnerships, if those investors or the management of that pool or private limited partnership employ investment strategies of any kind to earn a return on that pool of funds.[10]

The act thus appears to extend Massachusetts FCA liability to (1) private equity firms, (2) private equity managed funds, and (3) investors holding at least a 10% stake, directly or indirectly, in a company that has violated the Massachusetts FCA.

Moreover, that liability is not for the submission of false claims or for any other violation of the Massachusetts FCA actually committed by a private equity firm — but instead for the failure to disclose to the commonwealth a known violation of the Massachusetts FCA 60 days or less after identifying the issue.

This is a dramatic departure from what is required to establish liability under the federal FCA, which, at minimum, requires a showing that a party caused the submission of false claims.[11]

In the private equity context, this typically requires proof that the private equity firm or its investors exercised control over the portfolio company and then ratified the company's alleged violation of the FCA after becoming aware of it,[12] or was more actively involved in the company's alleged misconduct — such as by approving or funding the alleged scheme.[13]

The liability risks under the Massachusetts FCA to private equity firms and investors are heightened even further by a number of ambiguities in the amended statute, including what it means to identify a violation that triggers the 60-day notice requirement.

The term is not defined in the statute, but is used seemingly interchangeably with the term "knowing," which is defined as "actual knowledge," "deliberate ignorance," or "reckless disregard," with "no proof of specific intent to defraud" required.[14] It is not clear whether this definition is meant to also define "identifying," or if that term is meant to have its own separate meaning.

This is an issue that will likely be litigated under the statute, as a similar issue was in the federal context before the Centers for Medicare and Medicaid Services attempted to resolve it in a final rule issued this last November.[15]

Implications for Due Diligence and Compliance Controls

The act's amendments to the Massachusetts FCA underscore the importance of private equity firms conducting robust diligence in transactions involving companies that receive funds from the commonwealth, particularly Medicaid funds and government contract monies.

At the same time, especially given the ambiguity around the meaning of the term "identifying," it remains to be seen whether the commonwealth treats preclosing knowledge of a potential FCA violation as sufficient to start the running of the 60-day disclosure clock.

Preclosing diligence should be robust enough to identify risk areas and areas for rapid, efficient postclosing diligence — but should stop short of the sort of detailed investigation into specific government interactions or payments that is more appropriate for postclosing diligence, and that risks being misinterpreted later as having imbued the acquiring firm with knowledge of an FCA violation.

In parallel, private equity firms should consider seeking commercial terms that offset the risk of subsequent regulatory scrutiny borne of the act's broad sweep.

Postclosing, private equity firms should conduct thorough diligence into any FCA risk areas identified during preclosing diligence. Postclosing efforts should be swift, given the act's short window for reporting violations following their identification.

While each set of facts and circumstances will be unique, if a potential FCA violation is discovered, firms should strongly consider proactive disclosure to the commonwealth.

Private equity firms must also remain vigilant in monitoring portfolio companies for any potential Massachusetts FCA violations. And, of course, firms should ensure that their portfolio companies have strong compliance programs, including mechanisms for conducting regular audits and risk assessments, as well as robust processes for ongoing monitoring and reporting so that violations can be identified early and dealt with appropriately and efficiently.

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[1] Mass. Gen. Laws ch. 12 § 5B(a)(11), as amended by H.5159 § 29.

[2] See, e.g., Statement of Ethan Davis, Deputy Assistant Attorney General, DOJ's Civil Division (June 2020) (Trump Administration) ("Where a private equity firm takes an active role in illegal conduct by the acquired company, it can expose itself to False Claims Act liability.") (available at https://www.justice.gov/civil/speech/principal-deputy-assistant-attorney-general-ethan-p-davis-delivers-remarks-false-claims); Statement of Brian Boynton, Principal Deputy Assistant Attorney General, DOJ's Civil Division (Feb. 2024) (Biden Administration) ("We have already had a few cases involving private equity firms. And given the significant role that private equity is increasingly playing in the healthcare field, we anticipate that their impact on healthcare billings will continue to grow as well.") (available at https://www.justice.gov/opa/speech/principal-deputy- assistant-attorney-general-brian-m-boynton-delivers-remarks-2024).

[3] Mass. Gen. Laws ch. 12 § 5A.

[4] Mass. Gen. Laws ch. 12 § 5B(a)(1) — (2).

[5] Compare Mass. Gen. Laws ch. 12 § 5B(a)(9) with 31 U.S.C. § 3729(a)(1)(G).

[6] Mass. Gen. Laws ch. 12 § 5B(a)(10).

[7] See Mass. Gen. Laws ch. 12 §§ 5A, 5B.

[8] Mass. Gen. Laws ch. 12 § 5B(a).

[9] Mass. Gen. Laws ch. 12 § 5B(a)(11), as amended by H.5159 § 29.

[10] Mass. Gen. Laws ch. 12 § 5A, as amended by H.5159 § 27.

[11] 31 U.S. Code § 3729(a)(1)(A), (B).

[12] See, e.g., United States ex rel. Martino-Fleming v. S. Bay Mental Health Ctrs., 540 F. Supp. 3d 103, 130 (D. Mass. 2021) (private equity firm's "knowing ratification of 'the prior policy of submitting false claims by rejecting recommendations to bring South Bay into regulatory compliance constitutes sufficient participation in the claims process to trigger [False Claims Act] liability'" (citation omitted) (alteration in original)); cf. United States ex rel. Schagrin v. LDR Indus., LLC, 2018 WL 6064699, at *6 (N.D. Ill. Nov. 20, 2018) ("if the Greenspons knew that LDR — the company they owned and managed — was not paying customs duties, they can be liable under the False Claims Act for failing to rectify the situation").

[13] United States ex rel. Carmen Medrano v. Diabetic Care RX, LLC, 2018 WL 6978633, at *11 (S.D. Fla. Nov. 30, 2018) (denying dismissal of claims against private equity firm because the complaint alleged that the firm "(i) approved of PCA's decision to use marketers to generate referrals; (ii) knew that TRICARE was the source of the majority of PCA's revenue; (iii) received monthly financial statements, which reported the monthly compounding revenue and the commission paid to the

Marketers; and (iv) RLH funded $2 million in commissions to the Marketers in January 2015").

[14] Mass. Gen. Laws ch. 12 § 5A.

[15] We covered that rule and its implications for the healthcare industry in a client alert following the rule's publication.