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2020 Civil False Claims Act Update—Part II

By Scott F. Roybal and Matthew Lin*

The first part of this two-part article, which appeared in the February 2021 issue of Pratt's Government Contracting Law Report*, briefly reviewed the basic elements of the False Claims Act and its* qui tam *provisions, recent Department of Justice enforcement statistics, and developments in the Justice Department's approach to dismissal based on the Granston Memorandum.*

This second part discusses the circuit courts' continued analysis of the False Claims Act's materiality standard under Escobar*, the U.S. Court of Appeals for the Sixth Circuit's holding on the public disclosure bar, the U.S. Court of Appeals for the Fifth Circuit's holding on the use of statistics to plead false claims, and potential developments related to COVID-19 and the CARES Act.*

COURTS CONTINUE TO ANALYZE FCA'S MATERIALITY REQUIREMENT POST-*ESCOBAR*

In 2016, the U.S. Supreme Court published its decision in *Universal Health Services, Inc. v. U.S. ex rel. Escobar*,[11] confirming the viability of the implied false certification theory in False Claims Act ("FCA") cases and mandating that claims brought pursuant to that theory satisfy "demanding" materiality and scienter requirements.

More than four years after *Escobar*, courts continue to wrestle with how to interpret and apply the ruling in FCA cases.

In particular, courts have expressed a broad range of views, under a variety of factual circumstances, regarding what they consider "material" to the government's decision to pay a particular reimbursement claim.

In *United States ex rel. Janssen v. Lawrence Mem'l Hosp.*,[12] the U.S. Court of Appeals for the Tenth Circuit took a stricter approach to the materiality standard, addressing many complex applications of the materiality standard.

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[11] 136 S. Ct. 1989 (2016).

[12] 949 F.3d 533, 541 (10th Cir. 2020).

In *Janssen*, the relator alleged that Lawrence Memorial Hospital had engaged in two healthcare fraud schemes by (1) falsifying patients' arrival times in order to increase Medicare reimbursement, and (2) falsely certifying compliance with the Deficit Reduction Act.

There, the relator urged the court to apply a "broad" interpretation of the materiality standard that focused on how a false statement would impact a reasonable person. The court disagreed, holding that the materiality standard must be measured by likely reaction of the government recipient of the false statement.

Next, the court reiterated *Escobar*'s emphasis on the government's prior conduct when evaluating materiality. Centers for Medicare & Medicaid Services ("CMS") had conducted an investigation over several months into the allegations at issue in the case over six years ago and continued to pay the defendant. The court held that the government's inaction, despite awareness of detailed allegations, suggested immateriality.

The court also addressed the importance of administrative procedures designed to address noncompliance. In *Escobar*, the Supreme Court emphasized that noncompliance that goes to the "essence of the bargain" suggests materiality.

In applying that standard, the Tenth Circuit noted that the government had an extensive administrative scheme for ensuring that hospitals remain in compliance and for bringing them back into compliance when they fell short of Medicare regulations and statutory requirements.

The court considered administrative schemes regulating compliance to be highly probative, stating that imposing FCA liability for every failure to achieve perfect regulatory compliance would undermine the government administrative program and render the FCA a general anti-fraud statute.

Finally, the court held that non-compliance with boilerplate compliance documents part of a complex regulatory scheme were insufficient to establish materiality.

Jannsen is important to FCA litigants because it highlights the significance of the government's action or inaction in regard to regulatory requirements. As demonstrated in *Jannsen*, courts scrutinize the regulatory frameworks the government adopt for reviewing compliance, as well as the government's payment decisions in light of their knowledge of potential noncompliance.

Jannsen also emphasized the leadership role of lower courts in paving the way for future FCA litigation, as *Jannsen* fleshed out many aspects of the materiality standard that will affect future FCA cases.

Significantly, the Supreme Court denied certiorari on October 5, 2020, signaling the high court's current willingness to let the circuit courts lead the way in honing the materiality standard.

The U.S. Court of Appeals for the Eleventh Circuit also wrestled with the materiality standard recently.

In *Ruckh v. Salus Rehab., LLC*,[13] the relator, a registered nurse, brought a *qui tam* action against two skilled nursing facilities, two organizations that provided management services, and a company that provided rehabilitation services. She alleged that the defendants had upcoded when billing for services, engaged in "ramping" by scheduling extensive services to exaggerate required payment levels, and submitted claims to Medicaid without creating or maintaining comprehensive care plans.

The Eleventh Circuit held that upcoding and ramping were obviously material because they went to the heart of the defendants' ability to obtain reimbursement from Medicare.

However, it held that the relator had not established Medicaid fraud predicated on the failure to create or maintain comprehensive care plans. The relator, the court noted, had failed to provide any evidence that the Florida Medicaid program had refused reimbursement or sought recoupment after a defendant self-reported the lack of care plans to the state. The court also noted that the relator failed to connect the lack of care plans to specific representations regarding the services provided under an implied certification theory.

Like *Jannsen*, *Ruckh* reiterates the significance of the government's conduct after learning of misrepresentations by government contractors. The government's response to noncompliance will continue to indicate whether the regulatory requirements will be considered material.

The U.S. District Court for the District of Columbia in *United States ex rel. Adams v. Dell Computer Corp.*,[14] analyzed *Escobar*'s materiality standard in regard to alleged cybersecurity vulnerabilities.

The relator, a self-described "internationally-recognized expert in computer hardware and software systems," alleged that he discovered cybersecurity hardware vulnerabilities in computers sold by Dell to the government. Among other theories, the relator argued that Dell made false certifications of compliance with a number of government technology policies by failing to correct the vulnerability.

[13] 963 F.3d 1089 (11th Cir. 2020).

[14] No. 1:15- cv-608 (D.D.C. 2020).

However, the court found that the vulnerability was not material under *Escobar*, noting that the contracts did not require Dell to comply with federal technology policies. Even if such compliance were required, the court continued, the policies did not require defect-free products, but merely that the agencies limit vulnerabilities and attempt to remedy them if located. The court reasoned that Dell could comply with this requirement by providing computer systems with limited vulnerabilities and assist in eliminating or reducing vulnerabilities as they appear.

The court stated that "the existence of a single vulnerability . . . would not necessarily be material to the agencies' acceptance of the computer systems and payment under the contracts." In a footnote, the court also signaled agreement with Dell's argument that the government's continued purchase of its computer systems after the relator disclosed his allegations to the U.S. Attorneys' Office showed that the vulnerability was immaterial.

The court also held that the relator failed to allege that Dell had knowledge that its claims were false. The relator alleged that he discovered the vulnerability "against all odds" through his own independent investigation and development of unique methods and tools. The court found it contradictory to conclude that Dell employees knew of the defect while the relator's effort in discovering the defect demonstrated how difficult it was to detect.

Furthermore, the court found that the relator did not allege whether Dell employees had knowledge that the defect violated a material provision in the agreement with the governmental agencies.

Adams suggests to government contractors that cybersecurity vulnerabilities in their products do not necessarily give rise to liability under the FCA, especially when the vulnerabilities are difficult to detect, and where government contracts do not specify correction of those vulnerabilities as an express condition of payment.

SIXTH CIRCUIT HOLDS THAT PRIOR *QUI TAM* ACTIONS TRIGGER THE PUBLIC DISCLOSURE BAR

The U.S. Court of Appeals for the Sixth Circuit joined the majority of circuit courts to hold that a prior *qui tam* lawsuit regarding the same alleged conduct triggers the public disclosure bar of the FCA.

In *U.S. ex rel. Holloway v. Heartland Hospice, Inc.*,[15] the relator filed a *qui tam* complaint in 2010 in the U.S. District Court for the Northern District of Ohio against Heartland Hospice and related entities ("Heartland"), alleging that

[15] 960 F.3d 836 (6th Cir. 2020).

Heartland engaged in a fraudulent scheme to recruit patients and keep them in hospice care where they did not need hospice services. Heartland allegedly submitted claims to Medicare and Medicaid that falsely certified that the patients were hospice-eligible under Medicare regulations, even though many were not. The government declined to intervene.

Heartland moved to dismiss the complaint under the public disclosure bar, based on three prior *qui tam* complaints filed in the U.S. District Court for the District of South Carolina against its parent company. Among other types of public information, the FCA bars claims that were publicly disclosed in a federal proceeding "in which the Government or its agent is a party."[16]

The court rejected the relator's argument that the prior *qui tam* relators were not the government's agents and were not public unless the government intervened, reasoning that the government is the real party in interest, is the primary recipient of the damages, exerts a fair amount of control over *qui tam* litigation, and could dismiss or intervene in the case at a later date.

Thus, the court held that prior South Carolina *qui tam* complaints alleged the same conduct, triggering the public disclosure bar.[17]

FIFTH CIRCUIT HOLDS THAT STATISTICS WITHOUT MORE FAIL TO PLEAD FALSE CLAIMS

In recent years, whistleblowers have increasingly relied on statistics about an entity's business with the government—such as the percentage of a medical provider's Medicare- eligible patients—to establish false claims.

The U.S. Court of Appeals for the Fifth Circuit grappled with such a case in *United States ex rel. Integra Med Analytics, L.L.C. v. Baylor Scott & White Health*.[18] The relator, Integra Med Analytics, LLC ("Integra") accused Baylor Scott & White Health System ("Baylor") of submitting over $61 million in fraudulent claims to Medicare by using higher-value billing codes than were justified by actual medical diagnoses to increase its revenues (also known as "upcoding").

Integra specifically alleged that Baylor trained its physicians to use higher-value codes, pressured them to alter diagnoses to fit in those codes, and

[16] 31 U.S.C. § 3730(e)(4)(A)(i) (2010).

[17] The FCA was amended in 2010 as part of the Patient Protection and Affordable Care Act, including amending the public disclosure bar from barring claims "based upon" public information to claims where "substantially the same allegations or transactions" that were publicly disclosed. The amendments are not retroactive, and because Heartland's alleged scheme lasted from 2004 to 2018, the Sixth Circuit analyzed both definitions of the bar. The relator also waived the argument that she was an original source.

[18] 816 Fed.Appx. 892 (5th Cir. 2020).

provided medically unnecessary treatment in order to use the codes. To support its allegations, Integra performed a statistical analysis of Baylor's inpatient claims data from 2011 to 2017 from CMS and discovered that Baylor had claimed the higher-value codes significantly above the national average for other hospitals. Integra also included statements by a Baylor medical coder who states she was instructed to upcode.

The U.S. District Court for the Western District of Texas, however, dismissed the complaint after finding that it failed to state a particularized claim for relief.

The Fifth Circuit was not convinced, either. It found that the statistics actually supported an inference that Baylor was simply ahead of the curve in using the higher-value codes, since Integra's data showed that other hospitals were using the codes at an accelerating rate that would likely converge with Baylor's rate.

While the Fifth Circuit did not bar the use of statistics to plead false claims altogether, it held that statistical data could not meet the requisite pleading standards if the data "is also consistent with a legal and obvious alternative explanation."

The court also found that Integra failed to allege medically unnecessary treatment, despite providing statistics showing that Baylor put patients undergoing major heart surgery on ventilators at twice the rate of the national average. The court reasoned that the single statistic did not establish sufficient particular details of fraud.[19]

Integra is an example of the judiciary's skepticism of statistics as evidence of false claims, where those statistics are not supported by other allegations of falsity. It also highlights the potential to educate courts on industry trends to explain how certain conduct is evidence of cutting edge practices and not necessarily evidence of fraud.

FCA CASES RELATED TO COVID-19 AND THE CARES ACT HAVE YET TO (PUBLICLY) EMERGE

COVID-19 has touched every part of American life, and it is likely to make a huge impact on FCA enforcement as well. The combination of the COVID-19 pandemic, the related downturn in the U.S. economy, and the CARES Act, have created a perfect storm for whistleblower claims. The CARES

[19] The Fifth Circuit also found that allegations that physicians were trained to upcode were also consistent with implementing new rules issued by CMS, and thus failed to plead false claims. It also found that statements by Baylor's medical coder were too conclusory to survive dismissal.

Act was the largest economic stimulus package in U.S. history, bringing the risk of fraud with each dollar it distributed. An unprecedented number of businesses have rushed to receive government aid to survive the economic impact of COVID-19.

Many of these businesses received government funds for the first time under the Paycheck Protection Program ("PPP") and may have been unwary of the legal consequences of misrepresentations in their applications. In addition, economic challenges may have caused employees to cut corners or even cheat the CARES Act process in order to help their employers stay afloat, even without their employers' knowledge. At the same time, COVID-19 has devastated the economy, despite the government's relief efforts. Tens of millions of employees were laid off since March 2020.

Historically, whistleblowers commonly are former disgruntled employees. Accordingly, the recent layoffs, furloughs, and wage reductions undertaken in response to the pandemic may create a massive pool of disgruntled employees from which potential whistleblowers are sure to arise. Whistleblowers also may be individuals from outside a business that gain insight to potential fraud and abuse, such as suppliers, vendors, and auditors. These individuals also may see FCA claims as a potential financial opportunity.

National and regional crises and the government monetary relief that followed have historically preceded spikes in FCA enforcement actions against those that were perceived as taking unlawful advantage of government spending.

After Hurricane Katrina hit in 2005, the government and whistleblowers brought numerous FCA claims against government contractors for defrauding the government of disaster relief funds. For example, whistleblowers successfully brought FCA claims against large insurance companies for allegedly manipulating insurance claims to shift liability to the government.

The 2008 Financial Crisis and the financial stimulus that followed, including the Troubled Asset Relief Program ("TARP"), led to another round of intense and widespread FCA enforcement. A pair of whistleblowers have pursued FCA claims against one of the nation's largest financial institutions from 2011 until today, alleging that the institution misrepresented its financial condition to receive bailout funds from Federal Reserve Banks.

Many other financial institutions have paid tens of billions of dollars to settle claims—including FCA claims—related to their alleged improper acts leading up to the 2008 Financial Crisis. The COVID-19 pandemic and its corresponding massive financial relief funding will likely be a precursor to later government investigations and result in a similar spike in FCA enforcement.

The government has prioritized enforcement against fraud under the CARES Act. For example, the CARES Act itself created the Special Inspector General for Pandemic Recovery ("SIGPR") with a $50 million budget for investigating fraud under the CARES Act. The Department of Justice ("DOJ") has also created a hotline and website specifically for reporting COVID-19-related fraud.

The DOJ has initiated dozens of cases against individuals for sending fraudulent Paycheck Protection Program ("PPP") loan applications. We have yet to see any unsealed *qui tam* FCA cases predicated on violations of the CARES Act, since FCA cases often take several months, if not years, before being filed, investigated by the government and eventually unsealed.

However, whistleblower and FCA defense attorneys alike have predicted a massive spike in FCA enforcement based on CARES Act fraud in the not-too-distant future.

Government contractors can take precautions now to minimize future FCA enforcement risks. Beyond the general precautions generally taken when dealing with the government, contractors should review any statements or certifications made to the government when receiving aid under the CARES Act. The PPP and other CARES Act programs require applicants to make a number of certifications and submit supporting documents—inaccuracies in either may subject loan recipients to criminal liability or civil liability under the FCA.

Contractors also should be wary of the heightened risk of whistleblower claims. Contractors should ensure that whistleblowers or concerned employees are able to report perceived misconduct internally and promptly investigate and correct any reported errors before they report to the government. Contractors should also ensure that whistleblower rights are protected to prevent whistle-blower retaliation.