CLIENT ALERT

Ninth Circuit's *Rose* Decision Could be a Thorn in the Side of Relators (At Least for Now)

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In *Universal Health Services, Inc. v. United States ex rel. Escobar*, 136 S.Ct. 1989 (2016) (discussion by C&M attorneys here), the Supreme Court held that an implied false certification can be a basis for False Claims Act (FCA) liability, "*at least* where two conditions are satisfied:" (1) the claim 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. (Emphasis added).

Since *Escobar*, lower courts have split on whether that two-part test was necessary—or merely sufficient—for establishing such FCA liability. *Compare, e.g.*, *U.S. v. Sanford-Brown, Ltd.*, 840 F.3d 445, 447 (7th Cir. 2016) (holding that an implied-certification claim must satisfy both conditions described in *Escobar*); *with, e.g.*, *U.S. ex rel. Badr v. Triple Canopy, Inc.*, 857 F.3d 174, 178 n.3 (4th Cir. 2017) (stating that it had "already answered" the question "left open" in *Escobar* by "holding that the Government pleads a false claim when it alleges a request for payment under a contract where the contractor withheld information about its noncompliance with material contractual requirements."); *U.S. ex rel. Panarello v. Kaplan Early Learning Co*., No. 11-cv-00353, 2016 U.S. Dist. LEXIS 158193, at *13 (W.D.N.Y. Nov. 14, 2016) ("The fact that *Escobar* clarified 'some' of the circumstances creating implied false certification liability suggests that compliance with the conditions it discussed is not necessarily a prerequisite to implied false certification liability in every case.").

Last week, in *United States ex rel. Rose, et al. v. Stephens Institute,* the Ninth Circuit joined the Seventh Circuit and held that *Escobar's* two-part test is mandatory in all implied-certification cases under the FCA. That holding is welcome news to defendants at large. But the same cannot be said for the defendant in *Rose*, as the Court affirmed the district court's denial of its motion for summary judgment, ruling that there was sufficient evidence for a jury to find that the two-part test had been met and that the noncompliance at issue was material to the government's payment decision.

Background

In *Rose*, former admissions representatives alleged that the Stephens Institute (DBA Academy of Art University) violated the incentive-compensation ban in its program-participation agreement (PPA) with the Department of Education. According to the relators, the University did so by paying bonuses up to $30,000 to recruiters for enrolling higher numbers of students.

The district court denied the University's summary-judgment motion on May 4, 2016. After the United States Supreme Court decided *Escobar* just one month later, the University sought reconsideration. The district court declined to reconsider its ruling, but it certified several questions concerning *Escobar's* impact for interlocutory appeal.

***Escobar's* Two-Part Test**

In deciding whether the two conditions described in *Escobar* are mandatory for establishing a false claim based on implied certification, the *Rose* panel contended with both the Supreme Court's decision and Ninth Circuit precedent. Prior to *Escobar*,

the Ninth Circuit had recognized the implied-certification theory of FCA liability in *Ebeid ex rel. United States v. Lungwitz*, 616 F.3d 993 (9th Cir. 2010). *Ebeid* permitted implied-certification claims when (1) the defendant explicitly undertook to comply with a law, rule, or regulation that is implicated in submitting a claim for payment; (2) the defendant submitted the claim; and (3) the defendant did not comply with that law, rule, or regulation. *Ebeid* did not require that a claim for payment contain a "specific representation" that was misleading due to a failure to disclose a violation.

The *Rose* panel questioned whether *Escobar* itself necessarily overruled *Ebeid*. But in the panel's view, two prior Ninth Circuit decisions applying *Escobar* had fatally undermined *Ebeid*. First, in *United States ex rel. Kelly v. Serco, Inc.*, the panel applied only the two-part test from *Escobar*—and not the more relaxed *Ebeid* standard—in holding that the plaintiff's implied-false-certification claim failed. 846 F.3d 325, 332 (9th Cir. 2017). Second, in *United States ex rel. Campie v. Gilead Sciences, Inc.*, (discussion by C&M attorneys here), the panel held that *Escobar's* two conditions must be satisfied to give rise to an implied-certification claim. 862 F.3d 890, 901-03 (9th Cir. 2017).

Ultimately, the *Rose* panel concluded that it was bound by *Serco* and *Campie*; hence, *Escobar*'s two-part test was mandatory. During oral argument in *Rose*, however, one of the judges suggested that the Ninth Circuit may need to resolve the issue *en banc*. The *Rose* opinion repeated that sentiment, noting that the panel was constrained "unless and until our court, *en banc*, interprets *Escobar* differently."

The panel concluded that the evidence was sufficient to create an issue of material fact as to whether the University's actions met the two *Escobar* requirements. In a loan School Certification form, the University had certified that the student applying for federal aid was an "eligible borrower" and was "accepted for enrollment in an eligible program." Because the University did not disclose its violation of the incentive-compensation ban, the panel explained that the certification could be considered a "misleading half-truth."

Materiality

The *Rose* panel then split 2-1 on whether the alleged false certification was material under *Escobar*. The majority concluded that a reasonable trier of fact could find that the violation was material because "the Department's payment was conditioned on compliance with the incentive compensation ban, because of the Department's past enforcement activities [against schools for violations of the incentive compensation ban], and because of the substantial size of the forbidden incentive payments."

Judge N.R. Smith dissented. He emphasized that *Escobar* requires a "rigorous" and "demanding" inquiry into the government's "likely or actual behavior" to determine whether the alleged misrepresentation was important to its decision to pay (or not). Because the majority relied on evidence of how the government *generally* enforces the incentive-compensation ban—and not how the government would respond to the specific incentive-compensation-ban violations alleged—Judge Smith opined that the only real evidence supporting materiality was the fact that payment was conditioned on compliance with the ban. According to Judge Smith, that was not dispositive under *Escobar*.

Looking Ahead

The relators in *Rose* had argued that the two conditions described in *Escobar* were merely one way to establish implied-certification liability. The Department of Justice supported the relators' position as *amicus curiae*. In the DOJ's view, "loose

language" from other courts characterizing the two conditions "as necessary rather than merely sufficient" should not limit the implied-certification theory to cases where the alleged false claim makes "specific representations."

In contrast to *Rose*, courts, including the Fourth Circuit in *Triple Canopy*, have endorsed that more expansive view of the implied-certification theory. Given the amount of leeway that *Escobar* leaves for interpreting the scope of implied-certification liability, the conflicting interpretations from lower courts, and the implicit invitation from the *Rose* panel, this issue may be an appealing candidate for *en banc* or even Supreme Court review.

For now, the *Rose* decision is good news for those facing implied-certification claims. By holding that the two conditions expressly mentioned in *Escobar* are necessary for establishing liability under a false-certification theory, the *Rose* decision curtails *Escobar's* open-ended statement that implied-certification liability exists *at least* in those circumstances.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

Mana Elihu Lombardo
Partner – Los Angeles
Phone: +1 213.443.5563
Email: melombardo@crowell.com

Brian Tully McLaughlin
Partner – Washington, D.C.
Phone: +1 202.624.2628
Email: bmclaughlin@crowell.com

Gail D. Zirkelbach
Partner – Los Angeles
Phone: +1 213.443.5549
Email: gzirkelbach@crowell.com