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FEATURE COMMENT: The Emerging Scope Of The Implied Certification Theory Of FCA Liability—A Scalpel Or A Bludgeon?

This year has seen a number of developments regarding the implied certification theory of liability under the False Claims Act, 31 USCA § 3729 et seq. In January, the U.S. Court of Appeals for the Fourth Circuit held that implied certification liability could arise if a contractor—with the requisite scienter—withheld information about noncompliance with material contractual requirements. In June, the Seventh Circuit rejected the implied certification construct altogether, and in July, the D.C. Circuit held that liability is triggered only if a contractor falsely certifies that it is complying with a regulation or statute that is a prerequisite to payment. This recent flurry of appellate decisions underscores the importance of the implied certification theory to the Government and so-called whistleblowers (referred to as "relators" under the Act), and reignites the debate over the scope of the ever-evolving implied certification theory of FCA liability.

Since being reversed at the Fourth Circuit in January, the defendant contractor in *U.S. ex rel. Omar Badr v. Triple Canopy* has filed a petition for writ of certiorari calling on the U.S. Supreme Court to "resolve this pervasive and irreconcilable split as to the important question of the scope of FCA liability." Petition for a Writ of Certiorari, *U.S. ex rel. Omar Badr v. Triple Canopy,* No. 14-1440, 2015 WL 3542745 (U.S. June 5, 2015). Given the ever-widening circuit split, and the Supreme Court's demonstrated interest in FCA matters in recent years, it is likely that the Court will decide the scope of the implied certification theory by taking up *Triple Canopy* or another case in the near future. The key question is whether the theory will be interpreted narrowly so that it functions like a scalpel, targeting fraud with surgical precision in instances in which contractors have violated laws that were express conditions of payment, or more broadly, such that it will be used like a bludgeon to resolve contractual disputes.

Implied Certification Theory—Traditional liability arises under the FCA in cases involving claims that are *factually false*—e.g., a contractor mischarges the Government for goods or services that were never delivered. False certification liability, by contrast, involves a claim that is *legally false*—e.g., a contractor fails to satisfy a legal requirement underlying the claim for payment. The false certification theory posits that if the Government pays funds to a party, but would not have paid those funds if it had known of a violation of a law or regulation, the claim submitted for those funds is a violation of the FCA.

A false certification case can arise from an express or an implied certification. An express certification occurs if a company certifies compliance with specific legal requirements when it submits a claim for payment. But even if a contractor does not make any *express* certifications when it submits a claim for payment, it can still trigger liability by making an *implied* certification—i.e., by submitting a claim, a contractor implies that it is in compliance with an array of governing laws and regulations.

Although the FCA was signed into law by Abraham Lincoln during the Civil War, implied certification is still a relatively new theory of liability. It traces its roots to the Court of Federal Claims decision in *Ab-Tech Construction v. U.S.*, in which a small minority-owned business entered into a secret agreement with a nonminority-owned partner, even though the contract stipulated that the contractor could enter into joint ventures only with the approval of the Government. 31 Fed. Cl. 429 (1994); 36 GC ¶ 384. The COFC found that although the

claims were not factually false—nor was there a false express certification—the act of submitting the claim represented an implied certification of compliance with the contract's requirements. The *Ab-Tech* court's acceptance of this theory—and its subsequent expansion to other circuits—has exponentially increased contractors' exposure to FCA liability.

At present, eight of the 13 circuits have accepted the implied certification theory in some form, with only the Seventh Circuit rejecting the theory outright. However, the eight circuits have reached varying conclusions about the appropriate scope of the theory. This Feature Comment focuses on the two standards around which the majority of the circuits have coalesced: the "express condition of payment" standard and the "material to the Government's decision to pay" standard.

Express Condition of Payment—In *U.S. ex rel. Mikes v. Strauss*, a physician, after being fired by her medical practice, brought a qui tam action against her former colleagues, alleging that they failed to properly calibrate medical devices and violated the FCA when they submitted claims for treatments involving the devices. 274 F.3d 687, 700 (2d Cir. 2001); 44 GC ¶ 2. The Second Circuit rejected the implied certification claim, holding that the FCA "was not designed for use as a blunt instrument to enforce compliance with all medical regulations—but rather only those regulations that are a pre-condition for payment—and to construe the impliedly false certification theory in an expansive fashion would improperly broaden the Act's reach." Id. at 699. In other words, the implied false certification theory is appropriately applied, in the Second Circuit's view, only if the underlying statute or regulation on which the relator relies expressly states that the provider must comply in order to be paid.

The Third, Sixth and Tenth Circuits have since followed the Second Circuit in applying the express condition of payment standard. The Fifth Circuit has not officially adopted the implied certification theory, but has suggested in dicta that, if it were to adopt the theory, it would limit its application to circumstances in which there is an express condition of payment. Decisions from these circuits are grounded in the rationale that the FCA is a blunt tool (with Draconian fines, penalties and other sanctions) and is not appropriate to enforce mere regulatory violations. *U.S. ex rel. Hobbs v. MedQuest Assocs., Inc.*, 711 F.3d 707 (6th Cir. 2013) (holding that the FCA's hefty fines and penalties makes them an inappropriate tool for ensuring compliance with technical requirements).

In other words, the implied false certification theory should be applied only in cases in which Congress or an agency has made an explicit materiality determination and has expressly conditioned payment of a claim on statutory or regulatory compliance. See, e.g., *U.S. ex rel. Wilkins v. United Health Grp., Inc.*, 659 F.3d 295, 313 (3d Cir. 2011) (reversing dismissal of claims based on the Anti-Kickback Statute (AKS), 42 USCA § 1320a-7b, because defendants were required monthly to certify compliance with Medicare guidelines as a prerequisite to eligibility under the Medicare program, the AKS was part of those guidelines, and therefore compliance with the AKS was an express condition of payment); *U.S. ex rel. Sanchez-Smith v. AHS Tulsa Reg'l Med. Ctr.*, 754 F. Supp. 2d 1270 (N.D. Okla. 2010) (holding that Medicaid program expressly conditioned payment on compliance with "active treatment" regulations).

Material to the Government's Decision to Pay—Although the majority of circuits now follow the express condition of payment standard, it has not been universally adopted. The First Circuit departed from the express condition of payment standard in *U.S. ex rel. Hutcheson v. Blackstone Med., Inc.*, a case in which the relator filed a qui tam action against Blackstone, a medical device manufacturer. 647 F.3d 377 (1st Cir. 2011). The relator alleged that Blackstone violated the AKS by providing cash and other benefits to surgeons to induce them to use Blackstone's devices in spinal surgeries, and because hospitals submitted claims for payment to Medicare, Blackstone caused false claims to be submitted to the Government. To establish falsity, the relator cited language in the cost reports that hospitals submitted with their reimbursement claims. The cost reports certified compliance with "the laws and regulations regarding the provisions of health care services." The trial court applied the express condition of payment standard and dismissed all of the relator's claims.

On appeal, the First Circuit reversed and explicitly rejected the argument that a claim can be false or fraudulent only if it fails to comply with a precondition of payment expressly stated in a statute or regulation. The First Circuit took a much broader view of whether the hospital made a specific representation that there was no underlying AKS violation, and it sent the case back to the court for fact-finding. The upshot of the court's ruling was clear: In the First

Circuit, contractors have a duty to disclose material violations of statutes, regulations and contracts, or they risk facing FCA liability.

The Fourth Circuit has since followed the "material to the Government's decision to pay" standard articulated by the First Circuit in *Blackstone*. In *U.S. ex rel. Omar Badr v. Triple Canopy*, the relator alleged that a security contractor that was responsible for ensuring the safety of an airbase in a combat zone, knowingly employed guards who allegedly falsified marksmanship scores, and presented claims to the Government for payment for those unqualified guards. 775 F.3d 628 (4th Cir. 2015); 57 GC ¶ 24. The defendant prevailed on a motion to dismiss at the district court after demonstrating that the Government failed to plead that it ever reviewed—and therefore ever relied on—the false scorecards. The Fourth Circuit reversed after adopting the materiality test, explaining,

> Common sense strongly suggests that the Government's decision to pay a contractor for providing base security in an active combat zone would be influenced by knowledge that the guards could not, for lack of a better term, shoot straight. ... If Triple Canopy believed that the marksmanship requirement was immaterial to the Government's decision to pay, it was unlikely to orchestrate a scheme to falsify records on multiple occasions.

Id. at 637–38.

The Fourth Circuit's decision also relied on the D.C. Circuit's opinion in *U.S. v. Sci. Applications Int'l Corp.*, 626 F.3d 1257 (D.C. Cir. 2010) (hereinafter *SAIC II*); 53 GC ¶ 25. In *SAIC II*, the D.C. Circuit took an expansive view of implied certification and held that to proceed under the theory, a plaintiff needed to show that the defendant "withheld information about its noncompliance with material contractual requirements." Id. at 1269. More recently, however, in *U.S. ex rel. Davis v. District of Columbia*, the D.C. Circuit appeared to back away from the materiality standard—without expressly rejecting the holding in *SAIC II*—and returned to the position it took 15 years earlier, when it insisted that a "false certification of compliance with a statute or regulation cannot serve as the basis for a qui tam action under the [FCA] unless payment is conditioned on that certification." No. 14-7060, 2015 WL 4153919 (D.C. Cir. July 10, 2015), quoting *U.S. ex rel. Siewick v. Jamieson Sci. & Eng'g, Inc.*, 214 F.3d 1372, 1376 (D.C. Cir. 2000); 42 GC ¶ 286.

Given that the D.C. Circuit has taken several positions on implied certification in the last 15 years, it remains to be seen if *Davis* will be the last word on the issue. Nonetheless, *Davis* is a welcome decision for contractors after several years of relators seizing upon the D.C. Circuit's expansive reading of the implied certification theory in *SAIC II*.

Which Standard Gets It Right?—At present, the tides seem to be shifting in favor of the express condition of payment standard, which has been adopted by the majority of the circuits that have addressed the issue. These circuits reason that the express condition of payment standard is more consistent with the plain text, history and purpose of the FCA, which was enacted to target *fraud* with punitive sanctions, while leaving nonfraudulent violations of contracts, statues or regulations to other administrative remedies.

Indeed, the Supreme Court has warned that expanding the FCA beyond its role of targeting fraud would render the statute "almost boundless." *Allison Engine Co. v. U.S. ex rel Sanders*, 553 U.S. 662, 669 (2008); 50 GC ¶ 208. But even if the FCA is not meant to be an enforcement device to police mere breaches of contract, there is a growing trend of relators attempting to shoehorn nonfraudulent breaches of myriad statutes and regulations into FCA claims under the implied certification theory.

Undoubtedly, one of the policy objectives of the FCA is to "let loose a posse of ad hoc deputies to uncover and prosecute frauds against the government," *U.S. ex rel. Milam v. Univ. of Tex. M.D. Anderson Cancer Ctr.*, 961 F.2d 46, 49 (4th Cir. 1992); 34 GC ¶ 351, but if left unchecked, the FCA's qui tam provisions may perversely incentivize relators to use the Act to remedy mere contractual disputes in the hope of recovering a bounty. Moreover, the materiality test lowers the pleading bar that offers contractors protection from frivolous lawsuits.

To survive a motion to dismiss under the materiality standard, a plaintiff needs only to plead a *plausible* scenario in which the Government would not have paid a claim if it knew about an underlying violation. Although defendants can still prevail on a motion to dismiss if plausible materiality is not sufficiently pled, this pleading requirement is a relatively low hurdle for the Government or relators to meet.

The practical effect is that some FCA complaints with threadbare allegations of materiality will survive a motion to dismiss, and once an FCA suit makes

it past a motion to dismiss, some defendants will opt to settle a case lacking merit rather than expend significant discovery and trial costs while facing the specter of treble damages, penalties and other potential sanctions. Other defendants will be forced to litigate run-of-the-mill breach of contract claims thinly disguised as FCA violations. These increased costs will be partially shouldered by the contracting community, but also indirectly by the Government and, ultimately, the U.S. taxpayer, through decreased competition (as these risks become untenable for those companies already engaged in Government contracting and those that would otherwise seek to enter the field), and through higher costs as contractors are forced to increase their compliance and litigation budgets.

In contrast, the fact that a contract, statute or regulation expressly conditions payment on a requirement is clear evidence that the contractor's duty of compliance will be enforced via the FCA rather than through other regulatory and administrative mechanisms. Accordingly, the express condition of payment standard for FCA liability offers a bright-line rule that puts contractors on notice of their exposure to punitive sanctions if they breach certain requirements.

Will the Supreme Court Bring Needed Certainty?—Regardless of one's view as to whether the implied certification theory should be applied broadly, few would disagree that the current circuit split is untenable. At present, *where* a relator files suit—and the scope of the implied certification theory that will be applied—can be outcome-determinative. In other words, cases that would be dismissed under the "express condition of payment" standard could survive a motion under the "material to the Government's decision to pay" standard. Indeed, in *U.S. v. Kellogg Brown & Root Servs., Inc.* the district court noted that the outcome of the motion to dismiss turned on which standard was applied. 800 F. Supp. 2d 143, 157 (D.D.C. 2011).

Given that millions of dollars are on the line, and the subtle differences between the circuits can be outcome-determinative, a savvy relator's counsel is most likely to file a qui tam action in a circuit that has accepted the materiality standard because mere deviations from the terms of the contract could trigger liability. It is unreasonable that the outcome of a case should vary so dramatically simply because of *where* the case is filed.

As such, it seems likely that an implied certification case will find its way onto the Supreme Court's docket in the near future. Moreover, the Supreme Court has demonstrated great interest in the FCA in recent years. Of the 35 FCA-related cases decided by the Court, four were decided in the last five years. The implied certification theory of liability could very well be the next FCA issue taken up by the Court.

Conclusion—Contractors and defense counsel might hold out hope that the Supreme Court will follow the Seventh Circuit and reject implied certification as a viable theory of liability altogether, but such an outcome may be overly optimistic, given that the theory is now well entrenched. Rather, the Court is more likely to settle the debate on the scope of the theory, and, in so doing, it may rein in the expanding reach of liability. Regardless, whether the Court were to reject wholesale the implied certification theory of FCA liability, or simply clarify its metes and bounds, the contracting community would benefit greatly from a more consistent application of theory and bright lines as to its practical application.

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