THE GOVERNMENT CONTRACTOR®

Information and Analysis on Legal Aspects of Procurement

MARCH 6, 2024 | VOLUME 66 | ISSUE 9

¶ 56 FEATURE COMMENT: The Top FCA Developments Of 2023

2023 was a busy year for the False Claims Act. Overall recoveries remained down compared to pre-2022 levels, but the total number of settlements and judgments exceeded any prior year. Of particular note, 2023 saw the U.S. Supreme Court issue decisions concerning the Government's authority to dismiss qui tam actions and the critical element of scienter that have wide-reaching impact. As always, this Feature Comment discusses these and other top FCA developments, including enforcement trends, case law developments, and more, and looks ahead to what's to come for Government contractors in 2024.

Recovery Statistics and Notable Settlements—In 2023, Department of Justice recoveries and settlements in FCA matters totaled just over $2.68 billion. While the 2023 total surpasses the $2.2 billion recovered in 2022, the $2.68 billion recovered is still one of the lowest total recoveries DOJ has attained in recent years. This total came in the form of 543 settlements and judgments, which according to DOJ, is the highest number of judgments and settlements ever reported in a single year. Together, these two numbers suggest that there were many smaller settlements and judgments to go with the larger hauls, some of which are discussed below. As usual, the majority of the recoveries—nearly $1.8 billion—came in the form of health care fraud settlements and recoveries, including recoveries to state Medicaid programs.

Following the trend of recent years, whistleblowers led the charge in FCA enforcement by filing 712 qui tam complaints. Only Fiscal Years 2013 and 2014 had higher numbers of qui tam complaints filed. The whistleblower provisions providing for between 15 and 30 percent recoveries for FCA relators remain enticing as relator shares totaled nearly $350 million.

Significantly, 2023 also brought the highest ever number of Government-initiated matters (i.e., non-qui tams) at 500 new matters. That is a notable increase from the 305 Government-initiated matters opened in 2022 and the 212 Government-initiated matters opened in 2021. While DOJ's statistics do not identify why the increase occurred, it appears to be due in part to the Government's investigations and actions related to newer, key enforcement areas, including pandemic relief fraud. In fact, one DOJ outpost, the U.S. Attorney's Office for the Northern District of Mississippi, has singlehandedly impacted that total, as it announced in June 2023 that it had obtained more than 150 FCA judgments and recovered more than $20 million since Coronavirus Aid, Relief, and Economic Security Act (CARES Act) funds were released in response to the COVID-19 pandemic.

DOJ highlighted significant settlements in several key enforcement areas this year, including fraud related to small business, cost and pricing, military supply chains, cybersecurity, and more. Once again, small business fraud was a key area for DOJ, particularly as it relates to COVID-19 enforcement under the CARES Act and Paycheck Protection Program (PPP). In the Victory Automotive Group, Inc. (VAG) settlement announced in October, VAG agreed to pay $9 million to settle allegations that it knowingly provided false information in support of its PPP loan forgiveness application. To qualify for a loan under the PPP, a business was required to certify that it had fewer than 500 employees. According to the allegations, however, VAG shared common operational control with dozens of automobile dealerships across the country, which meant that VAG and its affiliates had 3,000 employees in total, making it ineligible for the PPP and its certification false. The VAG settlement resolved a qui tam lawsuit and led to a relator's share of $1.62 million.

In addition to the size-related provisions of the PPP, other Program requirements were also front and center in 2023 settlements. In Coyne Public Relations LLC (Coyne), a public relations firm, agreed to pay $2.24 million to resolve FCA allegations in a qui tam lawsuit that it applied for and received a $2 million PPP loan, even though it allegedly knew that it was ineligible for the PPP as it is a registrant under Foreign Agent Registration Act. In another example, the Institute for Policy Studies (IPS) agreed to pay $500,000 to resolve allegations that it falsely certified that it was not an "entity primarily engaged in political or lobbying activities" to secure a Second Draw PPP loan mere days after publicly touting itself as a "think tank." Like the VAG and Coyne settlements, the IPS settlement resolved a qui tam lawsuit brought by a relator. And in *In re Fresh Acquisitions LLC, et al.*, No. 21-30721 (Bankr. N.D. Tex.), a trustee moved a Texas bankruptcy court to approve a $13 million settlement of claims brought by DOJ against two restaurant companies that had received PPP loans which were forgiven before the companies filed for bankruptcy.

2023 also brought the first-ever settlement related to falsely certifying eligibility for Restaurant Revitalization Fund (RRF) grant funding under the American Rescue Plan Act. Feast American Diners LLC agreed to pay $2 million to resolve allegations that its owner falsely certified that Feast American Diners was eligible for an RRF grant when he knew that his company owned and operated too many restaurants to qualify for the funding. To be eligible for an RRF grant, a restaurant had to own or operate fewer than 20 locations as of March 13, 2020. Feast American Diners owned and operated 21 Denny's restaurants as of March 2020. In the settlement, the defendants "agree" that Feast American Diners and its owner "should have known" it was ineligible for the RRF grant funding. The Feast American Diners settlement also resolved a qui tam lawsuit, and the relator will receive a $200,000 relator's share.

Small business fraud in set-aside procurements was also a key area for DOJ in 2023. For example, in June, HX5 LLC, its owner, and an affiliated joint venture, HX5 Sierra LLC, agreed to settle allegations of FCA violations for more than $7.7 million. According to the qui tam complaint, the entities knowingly provided false information to the Small Business Administration relating to HX5's and HX5 Sierra's eligibility for federal set-aside contracts intended for small businesses owned and controlled by socially and economically disadvantaged individuals. Specifically, HX5 allegedly made false statements to remain a member of the 8(a) Program, and therefore, (1) improperly maintained its status as an 8(a) Program participant, and (2) HX5 and HX5 Sierra were awarded 8(a) set-aside contracts by the Army, the Air Force, and NASA for which the companies were not eligible. The settlement resolved the qui tam lawsuit, and the relator will receive a share of approximately $1.35 million.

DOJ also focused on broader procurement fraud issues in 2023. In April, DOJ announced a $21.8 million settlement with L3 Technologies, Inc., Communication Systems West (L3), to resolve allegations that it knowingly submitted false claims by charging twice for certain parts on Department of Defense contracts. Specifically, L3 submitted numerous of contract proposals for Remote Operations Video Enhanced Receivers (ROVER) and Video Oriented Transceivers for Exchange of Information (VORTEX), which operate to provide real-time video and other data from the battlefield. The proposals allegedly double-counted the cost of low-cost common-stock items, including nuts and bolts. Unlike most of the settlements discussed in this report, this case resulted from a Government-initiated investigation involving coordination with the Defense Contract Audit Agency and Defense Contract Management Agency, among others. The L3 settlement is also unique among this list as it was executed in conjunction with a nearly $8 million resolution of an L3 claim against the Government related to other costs that DOD had rejected.

Several months later, in July, DOJ announced one of the largest procurement fraud settlements ever in the form of a $377.45 million settlement with Booz Allen Hamilton to resolve allegations that Booz Allen violated the FCA by improperly billing commercial and international costs to its federal Government contracts. According to the related qui tam lawsuit, for approximately 10 years between 2011 to 2021, Booz Allen improperly allocated indirect costs associated with its commercial and international business to its Government contracts and subcontracts that either had no relationship to those contracts or were allocated to those contracts in disproportionate amounts. The allegations also stated that Booz Allen failed to disclose to the Government the methods by which it accounted for costs supporting its commercial and international businesses, which led to Booz Allen obtaining reimbursement from the Government for activities that purportedly provided no benefit to the U.S. The Booz Allen settlement is noteworthy not only for the large settlement amount, but also for the nearly $70 million that constitutes the relator's share, demonstrating the enticing nature of the FCA's whistleblower provisions.

Other noteworthy settlements last year came in the areas of disaster relief, counterfeit parts, and cybersecurity. In October, AECOM agreed to pay $11.8 million to resolve allegations that it knowingly submitted false claims to the Federal Emergency Management Agency (FEMA) for the replacement of educational facilities destroyed by Hurricane Katrina in Louisiana. AECOM served as a technical assistance contractor to FEMA and submitted requests for public assistance funding on behalf of applicants. According to the allegations, AECOM personnel reviewed and did not correct disaster assistance applications that included materially false design, damage, and replacement eligibility descriptions. AECOM's failures purportedly led to applicants receiving more disaster relief funding than FEMA rules permitted, including for unallowable replacement costs.

In another burgeoning area involving nonconforming parts and supply chain fraud, the Government agreed to settle qui tam allegations that GE Aerospace sold parts that were nonconforming or not inspected on U.S. Army and Navy contracts for more than $9.4 million. According to the allegations, GE Aerospace's Lynn Massachusetts plant did not conduct required parts inspections and sold engines containing parts that did not meet certain required specifications to U.S. military customers. The Government placed particular focus on this settlement, claiming that GE Aerospace's failures put U.S. servicemen and women at risk.

Lastly, there was a major settlement involving alleged cybersecurity fraud, which is discussed immediately below.

Cybersecurity Compliance—In 2023, the Government confirmed its intent to actively pursue contractors for failing to meet or falsely certifying compliance with cybersecurity standards under DOJ's Civil Cyber-Fraud Initiative (Initiative) launched in October 2021. DOJ announced two settlements under the Initiative in 2023. First, in March 2023, DOJ announced that Jelly Bean Communications Design (Jelly Bean) and its manager agreed to pay almost $300,000 to resolve FCA allegations that it failed to properly secure personal information on a website that Jelly Bean had created, hosted, and maintained for the Florida Healthy Kids Corp. (FHKC), a federally funded Florida children's health insurance website. According to the settlement, Jelly Bean was contractually required to provide a fully functional hosting environment that complied with HIPAA. However, contrary to its representations in agreements and invoices, Jelly Bean did not do so and failed to properly maintain, patch, and update its software systems underlying the website, which left the site and data Jelly Bean collected from applicants vulnerable to cyberattacks.

Second, in September 2023, DOJ announced a $4 million settlement with Verizon Business Network Services LLC (Verizon) addressing allegations that Verizon violated the FCA because certain telecommunications services it provided to federal agencies did not comply with applicable cybersecurity requirements. According to the settlement agreement, Verizon was awarded three General Services Administration contracts to provide various telecommunications services to the Government, including Verizon's Managed Trust Internet Protocol Service (MTIPS), which was designed to provide federal agencies with secure connections to public internet and other networks. Because of the nature of the services provided, GSA required, among other things, that the contracts comply with all critical capabilities set forth in the U.S. Department of Homeland Security's relevant reference architecture document for Trusted Internet Connection.

Verizon's settlement was a result of a written disclosure it made to GSA inspector general's office after learning of the potential issues with the implementation and maintenance of certain security controls. The recitals in the settlement noted that Verizon cooperated with the Government's investigation and took prompt steps to remediate the issues, including by implementing compensatory security controls, making substantial capital investments in its governance, risk, and compliance platforms, and disciplining or replacing those employees Verizon identified as responsible for the issues. While not stated explicitly in the press release, Verizon's cooperation appears to have affected the amount of the total settlement.

In addition to the Jelly Bean and Verizon settlements, in September 2023, a qui tam FCA lawsuit was unsealed against Pennsylvania State University alleging that the university failed to meet cybersecurity standards required for handling covered defense information under the Defense Federal Acquisition Regulation Supplement 252.204-7012 clause and uploading template self-assessments in order to "check the box" to meet requirements under the DFARS 252.204-7020 compliance. While DOJ declined to intervene, it noted that it was continuing to investigate the claims. And on Dec. 26, 2023, DOD released the proposed rule for its highly anticipated Cybersecurity Maturity Model Certification (CMMC) program, which will bring greater scrutiny to contractors' cybersecurity compliance and require DOD contractors that handle federal contract information or controlled unclassified information to make annual affirmations regarding their cybersecurity maturity. CMMC compliance will likely be another focus of the Initiative going forward.

DOJ has signaled that it has no intention of slowing down its enforcement efforts in 2024. During Assistant Attorney General Brian M. Boynton's remarks at the 2024 Federal Bar Association's Qui Tam Conference in February, Boynton stated that DOJ intends to continue dedicating resources to the Civil Cyber-Fraud Initiative to use the FCA as a mechanism to hold federal contractors accountable who fail to follow federal cybersecurity requirements, and that he anticipates it will be a "significant area of enforcement in the coming years." The relator's bar has been listening and has advised that numerous cybersecurity qui tam suits have been filed in the past year.

Grassley Tries Again—Pending Amendments to the FCA Aimed at Weakening *Escobar*'s Materiality Factors—As was the case in 2021 and 2022, Sen. Chuck Grassley (R-Iowa) tried again in 2023 to close what he called "loopholes" in the FCA created by judicial interpretations of materiality since the Supreme Court's decision in *Universal Health Servs. Inc. v. U.S. ex rel. Escobar*, 579 U.S. 176 (2016); 58 GC ¶ 219, with proposed amendments to the FCA. Unlike the prior versions that Grassley introduced in July and October 2021, this newest iteration, the False Claims Amendments Act of 2023, has bipartisan support and is cosponsored by Sens. Dick Durbin (D-Ill.), John Kennedy (R-La.) and Roger Wicker (R-Miss.). Rep. Jodey Arrington (R-Texas) introduced an identical bill in the House of Representatives in November 2023.

The 2023 Proposed Amendments are significantly shorter than the prior proposals, but still controversial, particularly with respect to the critical element of materiality. Specifically, the 2023 Proposed Amendments provide: "In determining materiality, the decision of the Government to forego a refund or to pay a claim despite actual knowledge of fraud or falsity shall not be considered dispositive if other reasons exist for the decision of the Government with respect to such refund or payment." If passed, this "if other reasons exist" language raises significant concerns as to what manner of factual allegations put forth by a relator or the Government would sufficiently demonstrate those "other reasons." There will almost always be an "other reason" for payment where the Government received the services or products. Is the mere fact that a defendant rendered services and the Government paid for those rendered services enough to be an "other reason"? Or would something more be required? The proposed language would apparently leave these interpretive questions to the courts. If passed, this provision could significantly weaken the "rigorous" test required to plead and prove materiality.

The 2023 Proposed Amendments also include language to (1) clarify that the FCA's anti-retaliation provision includes retaliation against former employees, and (2) require the Government Accountability Office to conduct a study on the benefits and challenges of enforcement efforts and amounts recovered under the FCA.

While neither the Senate nor House versions of the 2023 Proposed Amendments have made it out of committee yet, the 2023 Proposed Amendments are a key issue to watch in 2024 as they could impact materiality arguments for FCA defendants.

FCA at the Supreme Court—The FCA had another unusually active year at the Supreme Court in 2023, with the Court deciding two notable cases. In *Polansky*, the Supreme Court held that the Government may seek dismissal of a qui tam suit over a relator's objection so long as it intervenes, either during the initial seal period or afterward. The Court also held that, when handling such a motion, district courts should apply Federal Rule of Civil Procedure 41(a), the rule governing voluntary dismissal. In *Schutte*, the Court held that subjective intent is relevant to scienter even where the regulation or rule at issue is ambiguous.

Polansky—DOJ Authority to Dismiss and Constitutionality of Qui Tam Actions Questioned: In *U.S. ex rel. Polansky v. Exec. Health Res., Inc.*, 599 U.S. 419 (2023); 65 GC ¶ 181, on review from the Third Circuit, the Supreme Court considered the procedure and standard of review for Government motions to dismiss qui tam actions. The Third Circuit, in its decision, cemented a circuit split regarding the Government's authority to dismiss a qui tam action and how it may do so. Other circuits ranged from holding that the Government's dismissal power was entirely unfettered to requiring a "rational relation" between the request and a valid Government purpose. In its decision, the Supreme Court resolved two key issues: (1) whether the Government has the authority to dismiss an FCA suit after initially declining to intervene, and (2) what standard of review applies to a Government motion to dismiss a qui tam action.

First, analyzing the plain language of the statute, the Court affirmed the Third Circuit's conclusion that the Government's dismissal power endures after the initial seal period, so long as it has intervened. Even after the end of the 60-day seal period from the filing of a qui tam, the Government may intervene so long as it shows good cause. But whether, and at what point, the Government must intervene in the suit before it can file for a 31 USCA § 3730(c)(2)(A) dismissal has been a subject of debate. Under the Third Circuit's approach in *Polansky*, the Government retains its right to control and dismiss a qui tam action even if it fails to intervene during the seal period, so long as it intervenes at some point. The Supreme Court agreed with the Third Circuit that a Government motion to dismiss under § 3730(c)(2)(A) is appropriate only where it has intervened in the suit. The Court explained that the Government's role in qui tam actions, consistent with the statute's Government-centered purpose, is "seal-agnostic" because the Government's interest in the suit remains the same regardless of when it intervenes. This is also consistent with congressional intent, the Court noted, which is to allow the Government to reassess qui tam actions and change its mind if and when new information comes to light. Here, the Third Circuit found that the Government had effectively intervened in the suit when it moved to dismiss the action under § 3730(c)(2)(A). Having intervened, the Government maintained its dismissal authority, and its motion was proper.

Second, the Court turned to the standard to be applied to a Government motion to dismiss. The Court weighed both the Government's position, that its dismissal authority is essentially unfettered, against the relator's position, that Government motions to dismiss should be subject to some form of arbitrary-and-capricious review, before opting for its own "Goldilocks position." Explaining that the application of the Federal Rules of Civil Procedure to civil litigation is standard, the Court affirmed the Third Circuit's application of Fed. R. Civ. P. 41(a) to § 3730(c)(2)(A) motions to dismiss. Under Fed. R. Civ. P. 41(a), the standard for dismissal varies with the case's procedural posture. If the defendant has not yet served an answer or summary-judgment motion, the plaintiff need only file a notice of dismissal. But once that threshold has been crossed, dismissal requires a court order on "proper" terms. Procedurally, however, the FCA requires notice and an opportunity for a hearing before dismissal. Moreover, Fed. R. Civ. P. 41's "proper terms" analysis will involve considerations of the relator's interests, including the potentially substantial resources they may have committed by the time the Government seeks dismissal. Nevertheless, the Court agreed with the Third Circuit that § 3730(c)(2)(A) motions will generally satisfy Fed. R. Civ. P. 41 "in all but the most exceptional cases" because the Government's views are entitled to "substantial deference." Qui tam actions are brought on behalf of the Government, in the name of the Government, and alleging injury to the Government alone; thus, "[i]f the Government offers a reasonable argument for why the burdens of continued litigation outweigh its benefits, the court should grant the motion. And that is so even if the relator presents a credible assessment to the contrary."

While the Court's ruling in *Polansky* resolves the circuit split that led the Court to take up the case, a dissent filed by Justice Thomas may soon create another one that could affect the qui tam provisions of the FCA altogether. Thomas questioned the constitutionality of a relator's right to bring a qui tam action in which the relator stands in the shoes of the Government in the first instance. He noted that the FCA's qui tam provisions inhabit a "constitutional twilight zone," as Article II provides that only the president and those acting below him can exercise executive power. Because a relator is not appointed by Congress as an officer of the U.S., a relator cannot "wield executive authority" to be able to represent the interests of the U.S. In a concurrence, Justices Kavanaugh and Barrett agreed with Justice Thomas's point that there are "substantial arguments that the qui tam device is inconsistent with Article II and that private relators may not represent the interests of the United States in litigation." Adding fuel to the fire, Justice Kavanaugh noted "the Court should consider the competing arguments on the Article II issue in an appropriate case." With at least three justices signaling their interest, Justice Thomas's dissent has laid the ground work for vigorous debate and litigation over the constitutionality of the FCA's qui tam provisions in the coming years.

Defendants in several active qui tam cases have already sought a ruling based on the dissent in *Polansky*, although no court in 2023 sided with the defense. In one example last December, one district court rejected a defendant's argument that the qui tam provisions are unconstitutional under the Appointments Clause and Take Care Clause in *U.S. ex rel. Wallace v. Exactech Inc.*, 2023 WL 8027309 (N.D. Ala. Nov. 20, 2023). There, the Northern District of Alabama rejected the defendant's argument that relators are "officers" who have not been properly appointed under the Appointments Clause argument because relators' authorization to litigate under the FCA is temporary. Second, the court rejected defendant's Take Care Clause arguments because the qui tam provisions allow the executive branch to maintain "sufficient control" of relators due to its power to dismiss, ability to intervene throughout the litigation, oversee relators, and settle the action. Last, the court pointed to the long history of qui tam statutes as support for the FCA's provisions as constitutional. This ruling, however, is only the beginning, and it likely won't be long before one or more courts of appeals weigh in on this significant issue.

Schutte: In two consolidated cases, *U.S. ex rel. Schutte v. SuperValu Inc.*, and *U.S. ex rel. Proctor v. Safeway, Inc.*, 598 U.S. 739 (2023); 65 GC ¶ 156, the Supreme Court resolved a circuit split regarding the narrow question of "[w]hether and when a defendant's contemporaneous subjective understanding or beliefs about the lawfulness of its conduct are relevant to whether it 'knowingly' violated the False Claims Act."

More broadly, however, the Court provided interpretive guidance as to the meaning of the FCA's scienter prongs, while also addressing the question of whether the *Safeco* scienter standard applies to the FCA, such that a defendant's conduct is not reckless when (1) it acted under an objectively reasonable, albeit erroneous, interpretation of an ambiguous regulation or provision; and (2) no authoritative guidance warned the defendant away from that interpretation.

First, looking to the text of the FCA, the Court resolved a narrow question of subjective knowledge: "If respondents' claims were false and they actually thought that their claims were false … then would they have 'knowingly' submitted a false claim within the FCA's meaning?" In the cases before the Court, the lower courts had ruled that the defendants' subjective belief was irrelevant as a matter of law to proving scienter. The Court reversed holding that a defendant's contemporaneous, subjective understanding of the law at the time of submitting claims is relevant, even if the law is ambiguous. The Court first noted that, by definition, subjective knowledge is relevant to an inquiry under all three prongs of the FCA's scienter standard (actual knowledge, deliberate ignorance, and reckless disregard). Citing back to the statute's enaction, the Court noted that the FCA encompasses "the common-law meaning of fraud" under the definition of "knowingly." At common law, the Court explained, scienter focuses primarily on what respondents thought and believed. The Court interpreted the three types of knowledge that can support FCA liability, holding that "actual knowledge" refers to whether a person is "aware of" the information at issue; "deliberate ignorance" encompasses defendants "who are aware of a substantial risk that their statements are false, but intentionally avoid taking steps to confirm the statement's truth or falsity"; and "reckless disregard" similarly captures defendants "who are conscious of a substantial and unjustifiable risk that their claims are false, but submit the claims anyway." This is indicative of a subjective test that turns on the defendant's culpable state of mind. Accordingly, a scienter inquiry requires an examination of what the defendant thought when submitting the false claim—not what the defendant may have thought after submitting it. As such, a post hoc interpretation of a regulation or statute that would provide a justification for their claims will not cure a defendant's intent to defraud at the time of submitting those claims. This ruling, as well as the Court's explanation of the meaning of deliberate ignorance and reckless disregard, are certain to impact all manner of FCA cases going forward.

Second, the Court declined to extend the *Safeco* standard to FCA cases. The Court noted that, while the FCA encompasses the same common-law definitions of "knowing" and "reckless" as the statute at issue in *Safeco*, the underlying statute's mens rea standard—"willfully"—is materially different from the FCA's scienter standard. Accordingly, reading the *Safeco* standard as "establishing categorical rules for those terms would accordingly 'abandon the care we have traditionally taken to construe such words in their particular statutory context.' " The Court also noted that, even if it were to apply the *Safeco* standard to FCA cases, that application would not render a scienter inquiry intent-agnostic. Under the *Safeco* standard, a person will be considered reckless if their action involves "an unjustifiably high risk of harm that is either known or so obvious that it should be known." Therefore, even if the *Safeco* standard were applied, the Court would not consider "legal interpretations that respondents did not believe or have reason to believe at the time they submitted their claims."

In its conclusion, the Court explained that it did not need to address "the parties' policy arguments," because the legal question before the Court was decided by the statutory text. However, the Court's decision is likely to have a considerable impact on cases in which the rule or regulation at issue is ambiguous, both at the pleading stage and even potentially on the merits.

Materiality—Since *Escobar*, the lower courts have issued hundreds of decisions applying the factors set forth by the Court as to the materiality of false or fraudulent claims for payment. In 2023, the Third Circuit and Seventh Circuit issued decisions reversing grants of summary judgment on materiality grounds.

In *U.S. ex rel. Druding v. Care Alternatives*, 81 F.4th

361 (3d Cir. 2023), the relators filed suit in 2008, alleging that hospice provider Care Alternatives violated the FCA by submitting claims to Medicare with a physician certification of terminal illness, even though inadequate clinical documentation supported that diagnosis. In 2015, the Government declined to intervene. When discovery closed, Care Alternatives moved for summary judgment. Initially, the district court granted summary judgment on falsity, which the Third Circuit reversed. On remand, the district court granted summary judgment again, this time based on materiality. Specifically, it found " 'no evidence' that Care Alternatives' 'insufficiently documented certifications … were material to the Government's decision to pay." The district court based its conclusion on two grounds. First, the Government could see Care Alternatives' submissions yet never refused any of its claims for reimbursement, despite the lack of adequate underlying documentation. Second, the relator failed to produce evidence either that the Government stopped reimbursing Care Alternatives after it was aware of the alleged falsity, or that the Government's "apparent disregard" of the documentation inadequacies was "not the result of its having concluded those inadequacies were immaterial."

The Third Circuit reversed. Its opinion analyzed several *Escobar* materiality factors: whether the requirement is a condition of payment, whether the alleged violations were substantial, and Government action. On the first, the regulations were clear that the documentation requirement was a condition of payment. The Third Circuit, acknowledging *Escobar*'s guidance that such a designation is not dispositive, stated that this factor "does not necessarily preclude summary judgment." Nonetheless, the court held that the designation as a condition of payment was "certainly probative evidence of materiality," and a jury should have been permitted to weigh it. On the second, the panel held that the documentation requirement " 'addresse[s] a foundational part of the Government's' Medicare hospice program," and thus false certifications are not minor or insubstantial. Further, the alleged violations were severe: evidence showed the violations occurred in 45 percent or more of cases, leadership understood the importance of the documentation requirement, and evidence indicated that some of the patients were not, in fact, terminally ill. Therefore, the second *Escobar* factor also supported a finding of materiality.

The district court's judgment relied solely on the third *Escobar* factor, Government action, to grant summary judgment. The Third Circuit found two errors with the district court's analysis. First, the district court seemed to impute to the Government actual knowledge of the documentation deficiencies. The panel held that the evidence did not support that conclusion, as the regulations did not require submission of the clinical documentation with the claims, and the Government's investigation of the relator's complaint would have occurred after payment of the claims at issue. While the Third Circuit acknowledged that 15 years of Government inaction was probative of immateriality, actual knowledge of the alleged violations was not the sole possible explanation for that inaction and a "reasonable jury could conclude that the Government's inaction is not conclusive." Further, the Third Circuit disagreed with the district court's conclusion that the relators had to present some evidence that the Government's inaction did not reflect a decision that the violations were immaterial. Instead, the panel concluded: "relators are not required to conduct discovery on government officials to demonstrate materiality."

While the court's analysis is subject to dispute, *Druding* is an example of a court of appeals declining to find a lack of materiality based on Government inaction alone.

The Seventh Circuit also found genuine issues of fact as to materiality in *U.S. ex rel. Heath v. Wis. Bell,* 75 F.4th 778 (7th Cir. 2023) (the court issued an amended opinion in January 2024 upon denial of Wisconsin Bell's petition for rehearing; that opinion only changed the analysis of the Government funding issue not addressed in this article). The Government program at issue was the Federal Communication Commission's Schools and Libraries Universal Service Support program, which helps "to keep telecommunications services affordable for schools and libraries in rural and economically disadvantaged areas." Under the program, the services provider must charge eligible recipients the lowest price charged to similarly situated customers. Wisconsin Bell provided services to hundreds of eligible schools and libraries, which submitted requests for reimbursement to the FCC. Wisconsin Bell also submitted reimbursement claims directly. Although Wisconsin Bell was aware of the pricing rule, it allegedly did not train its representatives on it or develop a plan for compliance until 2009, even though the rule had been in place since the 1990s.

A relator filed suit, alleging that Wisconsin Bell submitted claims and caused others to submit claims for more money than was allowed to be charged under the pricing rule. The district court granted Wisconsin Bell's motion for summary judgment based on falsity, but on appeal, the Seventh Circuit reversed on several grounds, including materiality.

As to materiality, Wisconsin Bell argued that the pricing rule was not expressly designated as a condition of payment and that the Government continued to pay despite being aware of the relator's allegations. The Seventh Circuit rejected the first argument, holding that "[e]xpress certification of compliance should not have been necessary for a provider to understand that the rule is important to the program's functioning and thus that noncompliance could influence reimbursement decisions." On the second, the court held: "[t]he government's knowledge of a pending lawsuit making allegations simply does not indicate actual knowledge of actual violations." Instead, it ruled, one could reasonably infer that the Government would still deny claims if it knew of actual charges.

Both *Heath* and *Druding* are examples of appellate courts viewing Government inaction as insufficient on its own to show a lack of materiality and, instead, creating jury questions—a trend that could make summary judgment more challenging for defendants.

Scienter—The Seventh Circuit's *Heath* decision also addressed scienter, particularly with regards to legal interpretations of regulations. There, Wisconsin Bell interpreted the pricing rule as allowing it to consider cost-based factors when determining which customers were similarly situated. The district court held that this was objectively reasonable. But the Supreme Court thereafter issued its decision in *Schutte*. Applying the Supreme Court's analysis, the Seventh Circuit concluded that "Wisconsin Bell's own conduct at least raises a genuine question as to whether it acted in reckless disregard of the truth or falsity of the claims submitted." Specific evidence raising that question included evidence that Wisconsin Bell did not have processes in place for compliance until 2009, did not have a system in place for identifying similarly situated customers, and overcharged more frequently during the rollout of compliance procedures. "With this evidence, a jury could reasonably infer that Wisconsin Bell acted in reckless disregard of whether the prices it was charging schools and libraries were above the prices charged to similarly situated customers."

Heath is one of the first appellate decisions interpreting *Schutte*, and it suggests that defendants may face headwinds when moving for summary judgment based on a reasonable interpretation of an ambiguous regulation where there is contemporaneous evidence of scienter. Interestingly, Judge Hamilton, who dissented from the Seventh Circuit's *Schutte* opinion that the Supreme Court vacated, authored *Heath*.

Damages—While several liability decisions went against defendants in 2023, the Ninth Circuit issued a significant decision on damages in favor of a defendant in *U.S. ex rel. Hendrix v. J-M Mfg. Co., Inc.*, 76 F.4th 1164 (9th Cir. 2023); 65 GC ¶ 264. Specifically, the Ninth Circuit affirmed a zero-damages judgment based on plaintiffs' failure to prove damages. The relator and five intervening agencies alleged that a manufacturer violated the FCA by representing, in bids to public agencies, that its PVC pipe was compliant with industry standards when it was not. The case was bifurcated and the jury returned a verdict for the plaintiffs on liability in the first phase, but hung on damages in the second phase. The district court then ruled as a matter of law that the plaintiffs failed to prove any actual damages, while also holding that the proper application of civil penalties was not to each nonconforming product shipped but rather to each "project" involving nonconforming parts. The Ninth Circuit affirmed.

Concurring with several sister circuit courts of appeal, the Ninth Circuit held that the proper measure of damages in cases involving goods or services provided to the Government is the difference between the value of the goods or services actually provided and the value the goods or services would have had if delivered as promised. The Ninth Circuit rejected the plaintiffs' position that damages were the entire amount paid simply because the Government "would not have bought the pipe had they known the truth" about the pipe. Such a theory was akin to a strict liability standard "regardless of any evidence of actual damages" and "conflates the materiality element … with actual damages," the court held. The Ninth Circuit also rejected the argument that damages be set at the full contract amount because the Government bargained for compliance with industry standards. Cases applying that damages model generally involved completely worthless goods or ones that had to be returned/replaced, but here there was no evidence that the pipes failed to operate as promised or that an actual failure was imminent or likely. In fact, the agencies had "not ceased the use of that pipe and thereby have obtained, retained (for many years), and continue to receive value from it."

In addition, the Ninth Circuit opined that a jury may not render a verdict "based on speculation or guesswork" and thus any damages to be awarded required "evidence to establish the difference in value between the goods as actually provided and as promised." This common-sense approach to damages is an important decision for defendants accused of fraud who nevertheless delivered on the goods or services bargained for, especially given that the Government and relator's bar regularly pursue damages theories based solely on what the Government paid but without any consideration to the plain value the Government received in return.

As to penalties, the Ninth Circuit concluded that one civil penalty per project was proper because the plaintiffs could only prove that the manufacturer did not uniformly comply with industry standards and thus could have delivered some non-conforming pipe. But plaintiffs "did not establish how much non-compliant pipe they received nor were they able to identify any specific piece of non-compliant pipe." Further, the court—relying on *U.S. v. Bornstein,* 423 U.S. 303 (1976)—held that, in cases involving goods, a proper penalties award must be based on the number of contracts or invoices, not each individual good (or here, stick of pipe).

Statute of Limitations—In *U.S. v. Corp. Mgmt., Inc.,* 78 F.4th 727, 743 (5th Cir. 2023), the Fifth Circuit cut a jury award of $10 million dollars in damages by half when it rejected a Government argument that the six-year statute of limitations tolled while it investigated relators' claims. First, the Fifth Circuit rejected the district court's finding that a Government complaint in intervention—which was filed in 2015 and alleged improper expenses, excessive compensation, and luxury automobiles—related back to the relator's 2007 complaint as to inflation of costs and waiving co-payments and deductibles. Second, the court rejected the Government's argument that the tolling provision saved the Government's pre-2009 claims because of a sealed 2011 memo recommending intervention in the case, suggesting that the Government "likely did know" facts material to the right of action at that time. However, the court denied defendants' request that it dismiss the Government's complaint altogether for delaying intervention by eight years. While the court "lament[ed]" that the district court "enabled the Government's gamesmanship" by granting eighteen seal extension requests, it "decline[d] to break new ground by granting such drastic relief." Even so, this decision demonstrates the limits of the relation back doctrine for relators and the Government alike.

2024 Vision—The Year Ahead for the FCA—While 2024 will not likely involve another FCA decision from the Supreme Court, its two decisions from 2023 are already having a significant impact for FCA cases at all stages, and the constitutionality of qui tam actions may wind up before the Court within another year or two. While FCA recoveries continue to be down, the surge of new cases—many in developing or trending enforcement areas, such as pandemic-related fraud, cybersecurity, supply chains, and more—signals areas for Government contractors to watch and to evaluate their compliance measures. 2024 is likely to see growth not just in the number of investigations and settlements but also in litigation surrounding these newer enforcement areas. And with the 40th anniversary of the amendments that breathed new life into the FCA in 1986 coming closer, the prospect of additional changes to Lincoln's Law remains on the horizon.

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