American Journal of Law & Medicine
Volume 42, Issue 4, November 2016, Pages 862-864

https://doi.org/10.1177/0098858817701964

Notes and Recent Case Developments

Supreme Court Reshapes the Landscape of False Claims Act Litigation

Eugenie Reich

On June 16, 2016, the Supreme Court clarified the basis of False Claims Act (FCA) liability in a health care fraud case brought *qui tam* by respondents.[1] The Court upheld the implied certification theory under which any statutory, regulatory, or contractual noncompliance can be a basis for liability, but also cabined liability by reading a "rigorous" materiality standard into the FCA.[2] Both plaintiffs' and defense lawyers have claimed the opinion as a victory.[3]

The case stemmed from the tragic death of Yarushka Rivera, who died after experiencing an adverse reaction to medication prescribed by a staff member at petitioner's mental health facility in Lawrence, Massachusetts.[4] Rivera's parents, the respondents, subsequently learned the facility had employed twenty-three unlicensed and unsupervised staff members, including two practitioners who had treated Yarushka.[5] Her parents learned the facility had submitted reimbursement claims to Massachusetts' Medicaid program using payment codes that corresponded to "individual therapy" and "group therapy" services and using National Provider Identification (NPI) numbers that the staff members had obtained from the federal government by misrepresenting themselves as properly licensed.[6] Massachusetts investigated the matter and found petitioner had violated the Commonwealth's Medicaid regulations multiple times.[7]

The FCA imposes liability on any defendant who "knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval."[8] The respondents in *Escobar* alleged that the petitioner's reimbursement claims constituted false or fraudulent claims because petitioner had made representations about its services – that its staff were licensed and supervised – without disclosing that their arrangements violated Medicaid regulations on staff licensure and supervision.[9] The District Court for the District of Massachusetts dismissed the case for failure to state a claim because regulatory compliance was not a "precondition of payment."[10] The Court of Appeals for the First Circuit reversed and remanded, holding that a requirement from a statute, regulation, or contract need not be an express condition of payment for liability under the statute, but can be implied.[11] Because other Courts of Appeals had taken different positions on the implied certification theory, the Supreme Court granted certiorari to settle the circuit divisions.[12]

The Supreme Court held that implied certification can be a basis for liability when (although not

necessarily only when) two conditions are met: "first, the claim … makes specific representations about the goods or services provided; and second, the defendant's failure to disclose noncompliance with material statutory, regulatory or contractual requirements makes those representations misleading half-truths."[13] The Court held that the case satisfied both conditions because the payment codes and NPI numbers that the clinic submitted in its claims for payment misrepresented that staff were properly licensed and that the clinic had complied with core regulations.[14] The Court suggested that liability might be cabined, however, by what it described as a "demanding" materiality standard.[15]

The FCA defines "material" as "having a natural tendency to influence, or be capable of influencing, the payment or receipt of money or property."[16] To this, the Court added definitions from the common law, holding that a representation is material if "a reasonable man would attach importance" to it, or "if the defendant knew or had reason to know that the recipient of the representation attaches importance to the specific matter."[17] The Court elaborated by listing multiple factors that could aid in applying this standard. The defendant's knowledge that the government typically refuses to pay claims that are not in compliance with a specific requirement weighs in favor of materiality, whereas evidence that the government pays a claim or a particular type of claim despite actual knowledge of noncompliance weighs against.[18] Additionally, "the [g]overnment's decision to expressly identify a provision as a condition of payment is relevant, but not automatically dispositive."[19]

The Court's intent in promulgating these factors was clear – to ensure that the FCA is not used to punish "garden-variety breaches of contract or regulatory violations" or "minor or insubstantial" instances of noncompliance.[20] Thus, the requirement that staplers used by a contractor are American-made does not count as material, while the requirement that guns bought by the military are functioning firearms does.[21] Because this materiality inquiry differed from the First Circuit's analysis,[22] which had considered instead whether the noncompliance entitled the government to withhold payment, the Supreme Court remanded the case to the First Circuit to apply its new standard.[23]

Most commentators on *Escobar* are interpreting the materiality standard as fact-intensive, making it likely to propel more cases past the motion to dismiss and summary judgment stages and result in increased pressure on defendants to settle.[24] Interestingly, the Supreme Court does not seem to have intended this outcome. In note 6, the Court expressly rejected the petitioner's contention that materiality would be "too fact intensive for courts to dismiss [FCA] cases on a motion to dismiss or at summary judgment. The standard for materiality that we have outlined is a familiar and rigorous one. And [FCA] plaintiffs must also plead their claims with plausibility and particularity under Federal Rules of Civil Procedure 8 and 9(b) by, for instance, pleading facts to support allegations of materiality."[25] Now it is up to the lower courts to resolve the tension between the Supreme Court's promulgation of apparently fact intensive materiality factors and its declared desire to limit the scope of FCA litigation.[26]

Notes

1 Universal Health Services, Inc. v. United States ex rel. Escobar, 136 S.Ct. 1989, 1995 (2016).

2 *Id*. (holding that the implied certification theory can be a basis for liability); *id*. at 2002 (calling the FCA's materiality and

scienter requirements "rigorous").

3 *Compare Phillips & Cohen Attorneys Discuss Supreme Court Ruling in Whistleblower Case*, PHILLIPS & COHEN LLP (June 16, 2016), http://www.phillipsandcohen.com/2016/Supreme-Court-False-Claims-Act-Escobar-Universal-Health-whistleblower.shtml (calling the ruling "fantastic" for whistleblowers) *with In Escobar, Supreme Court Upholds False Claims Act's Implied Certification Theory*, SKADDEN (June 17, 2016), https://www.skadden.com/insights/escobar-supreme-court-upholds-false-claims-acts-implied-certification-theory (calling the ruling "helpful to the defense").

4 136 S.Ct. at 1997.

5 *Id*.

6 *Id*.

7 *Id*.

8 31 U.S.C. § 3729 (a) (1) (A).

9 Complaint and Claim for Jury Trial Filed Under Seal at 23-33, United States ex rel. Escobar, 2014 WL 1271757 (D. Mass. Mar. 26, 2014) (No. 1:11-cv-11170-DPW); Escobar, 136 S.Ct. at 1997-98.

10 2014 WL 1271757 at *1 (dismissing the case), *10 (giving the rationale that the plaintiff's complaint does not allege that compliance was a precondition of payment).

11 780 F.3d 504, 512-13 (2015).

12 *Escobar*, 136 S.Ct. at 1998-99 (citing United States v. Sanford-Brown, Ltd., 788 F.3d 696, 711-12 (7th Cir. 2015) (rejecting implied certification) *reversed in part* 2016 WL 6205746 (7th Cir. 2016) and Mikes v. Straus, 274 F.3d 687, 700 (2d Cir. 2001) (limiting the reach of implied certification)).

13 *Id*. at 2001.

14 *Id*. at 2000-01.

15 *Id*. at 2003. *See also id*. at 2002 (calling the FCA's materiality requirement, along with its scienter requirement, "rigorous.")

16 31 U.S.C. 3729 (b)(4).

17 *Escobar*, 136 S.Ct. at 2002-03 (quoting the RESTATEMENT (SECOND) OF TORTS § 538, at 80 (1977)).

18 *Id*. at 2003-04.

19 *Id*. at 2003.

20 *Id*.

21 *Id*. at 2001-02 (giving the example of a government contract to buy firearms); *id*. at 2004 (finding that the FCA does not "adopt such an extraordinarily expansive view of liability" as to hold contractors liable for failing to buy American-made staplers").

22 780 F.3d 504, 514, 514 n.14 (holding that relators adequately pleaded falsity when they alleged defendants "misrepresented compliance with a condition of payment" while implicitly communicating that they were entitled to be paid).

23 136 S.Ct. at 2004.

24 *E.g*., Harold B. Hilborn, *Supreme Court Holds Implied Certifications Create False Claims Act Liability*, NATIONAL LAW REVIEW, http://www.natlawreview.com/article/supreme-court-holds-implied-certifications-create-false-claims-act-liability (Sept. 1, 2016) (predicting defendants will find it harder to "secure dismissal of FCA lawsuits at their outset"); Joan H. Krause, *Reflections on Certification, Interpretation and the Quest for Fraud that "Counts" Under the False Claims Act*, U. ILLINOIS L. REV. (forthcoming) ("Proving that the defendant's misrepresentation *actually* affected the outcome, as the Court appears to require, will demand a far more fact-intensive inquiry into the government's payment procedures, not just for this defendant but potentially for similarly situated providers as well.")

25 136 S.Ct at 2004 n.6.

26 *Compare id*. at 2003-04 (apparently encouraging inquiry into government's payment decisions) *with id*. at 2004 n.6.