

# FCA

## FCA 101

A Practitioner's Guide to the False Claims Act

BY DOUGLAS K. ROSENBLUM AND JOHN A. SCHWAB

# 101

Elizabeth is a junior partner in the white collar criminal defense practice group of a Philadelphia law firm. Having just received a signed engagement letter and substantial retainer from a very profitable pharmaceutical company, Elizabeth packed her briefcase and turned to leave and meet her colleagues for a celebratory drink. Her marketing efforts had paid off, and responding to a subpoena from the US Attorney's Office should be a simple enough task. Just as she turned off her desk lamp and grabbed her keys, her office telephone rang. The caller ID revealed a call that she knew she had to answer—it was her newest client.

The general counsel, and Elizabeth's point of contact on this new matter, was calling with a simple enough question. "Elizabeth, I was just speaking with our chief compliance officer, who raised an interesting issue. Is it possible that a whistleblower went to the government about us? What do we do if someone filed a False Claims Act case against us?"

Elizabeth froze. Her transition from prosecutor to private practice was not so long ago, and her knowledge of the federal False Claims Act was limited to flyers for CLEs that cluttered her desk. Elizabeth extricated herself from the awkward situation. "That's a great point. We can absolutely explore that possibility. It's nothing to lose sleep over tonight, but let me gather some information for you, and we'll speak tomorrow."

"Great. Thanks, Elizabeth."

As Elizabeth dropped her keys on the desk and turned the desk lamp on, she picked up her Blackberry and let her colleagues know she would be late . . . perhaps, very late.

### A Variety of Prohibited Activity

What makes the False Claims Act such a powerful tool in the federal government's fight against fraud is the breadth of activities it covers. Under 31 U.S.C. § 3729(a)(1)(A), it is unlawful to knowingly present, or cause to be presented, "a false or fraudulent claim for payment or approval" to the government. It is similarly unlawful to knowingly make "a false record or statement material to a false or fraudulent claim." (31 U.S.C. § 3729(a)(1)(B).) This naturally leads one to question what constitutes a "claim" under the False Claims Act.

Under 31 U.S.C. § 3729(b)(2), a "claim" is defined as follows:

(A) . . . [A]ny request or demand, whether under a contract or otherwise, for money or property and whether or not the United States has title to the money or property, that—

(i) is presented to an officer, employee, or agent of the United States; or

(ii) is made to a contractor, grantee, or other recipient, if the money or property is to be spent or used on the Government's behalf or to advance a Government program or interest, and if the United States Government—

(I) provides or has provided any portion of the money or property requested or demanded; or other recipient for any portion of the money or property which is requested or demanded; or

(II) will reimburse such contractor, grantee, or other recipient for any portion of the money or property which is requested or demanded.

But how does this relate to our junior partner, Elizabeth, and her advice to in-house counsel? In the many years since the federal False Claims Act was first passed, certain trends and common schemes have become evident. Although applicable to everything from government procurement to research grants, the majority of recoveries by the federal government under the False Claims Act have been in the health care and defense sectors. This should come as no surprise, given the massive amounts of federal spending each year in each of these areas.

Defense contracting cases can be the most straightforward. When a defense contractor building a plane for the United States military overcharges the government for landing gear, the identification of a claim is not overly challenging. Contractors have also been very active in building infrastructure overseas in places such as Iraq and Afghanistan. It takes just one whistleblower to bring to light the hours billed but not worked on such projects as paving roads or running substandard electrical wiring to government buildings.

Unfortunately for Elizabeth, health-care cases can pose greater challenges in identifying claims. Billing the federally funded Medicare and Medicaid programs for services that were never rendered to patients certainly qualifies as a false claim under the False Claims Act. However, paging through billing records to determine whether services actually rendered to patients were medically necessary can be a tedious process.

The pharmaceutical industry has proven to be one of the most lucrative industries for False Claims Act cases. Recently Pfizer paid \$2.3 billion related to unlawful kickbacks and off-label marketing of numerous drugs. Of that amount, \$1.3 billion represents criminal fines while \$1 billion represents a settlement for violations of the False Claims Act. Off-label marketing is just one example of how courts have interpreted the definition of "claim" in the False Claims Act to extend to practices

not as clear cut as overcharging for landing gear. In off-label cases, it is alleged that pharmaceutical companies promoted prescription medication for uses other than those approved by the Food and Drug Administration. Although doctors are permitted to prescribe medication for any use they see fit, it is unlawful for the manufacturer to market the medication for any unapproved uses. The off-label marketing of the medication is then deemed to have tainted the prescriptions that are submitted to Medicare and Medicaid for payment. (See, e.g., *United States ex rel. Franklin v. Parke-Davis*, 147 F. Supp. 2d 39 (D. Mass. 2001).)

### Filing a Case Under the False Claims Act

The esoteric procedural rules of the False Claims Act and the often quirky local rules of the courts in which these cases are filed, make the False Claims Act the statute that Elizabeth sought to avoid. While the federal gov-

ernment may bring a civil action under the False Claims Act without any assistance from a whistleblower, 31 U.S.C. § 3730 permits private citizens to take advantage of the “qui tam” provision of the statute and file suit as a private attorney general on behalf of the citizens of the United States. “Qui tam” is actually an abbreviated version of “*qui tam pro domino rege quam pro se ipso in hac parte sequitur*” that can be translated as “he who sues in this matter for the king as well as for himself.”

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facts of the case). A copy of the complaint must be served on the government, and the complaint remains under seal for a minimum of 60 days to provide the government time to investigate the matter without the defendant knowing of the allegations. The 60-day seal is routinely extended by order of the court upon motion of the government for good cause shown. Perhaps most frustrating to Elizabeth and her corporate client is that the company under scrutiny may be unaware of the matter under investigation for several years.

Upon conclusion of its investigation, the government notifies the whistleblower whether or not it will intervene in the case. Intervention is a crucial decision in these cases. Whistleblowers have the right to prosecute these cases themselves in the event that the government declines to intervene. However, some whistleblowers and their attorneys do not have the financial wherewithal to prosecute these cases without the government’s assistance. It is not

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If a whistleblower wishes to file such a suit, that person must do so through an attorney; pro se actions are not permitted under the False Claims Act. Prior to filing a complaint, the whistleblower—also termed a “relator”—must serve a pre-filing disclosure of all allegations and material evidence on the government. Thereafter, the complaint is filed under seal in the US district court of the relator’s choosing (dependent, of course, on the

until final disposition of the matter that the whistleblower will receive the statutory 15–30 percent of the government’s recovery.

Contrary to popular belief, many whistleblowers are not motivated by the pot of gold at the end of the qui tam rainbow but rather by their concern to do the right thing. Nonetheless, these cases are lucrative; from October 1987 to September 2010, the False Claims Act recovered over \$27 billion of which \$2.87 billion was relators’ shares. The cases are so lucrative because, for each false claim proven, the defendant is liable for treble damages, attorneys’ fees, and expenses, and up to \$11,000 in civil penalties *per claim*.

### History of the False Claims Act

The intent behind the False Claims Act can be best understood when placed in a historical perspective. Congress passed the False Claims Act on March 2, 1863, at the height of the American Civil War, to combat fraud by government contractors. Throughout the Civil War, the Union Army was plagued by dishonest contractors who sold the army dead or sickly mules, boxes of sawdust billed as rifles or ammunition, faulty uniforms, and spoiled rations.

The new legislation—known as the “Informer’s Law” or the “Lincoln Law”—made it illegal for an individual to make a false claim for payment to the federal government to improperly obtain more money than was actu-

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ally owed. The act also provided for the recovery of attorneys' fees and expenses, thereby encouraging support of the relator's counsel.

The most significant amendments to the False Claims Act came in 1986 when President Ronald W. Reagan and Congress sought to address increased waste and fraud due to record levels of federal spending. These amendments resulted in increased financial incentives for relators and increased monetary penalties to a minimum of \$5,000 and a maximum of \$10,000 per false claim. In addition, relators were able to retain a larger share of the recovery of 10–15 percent in cases where the government intervenes and 25–30 percent in cases where the government does not. The amendments also enabled the government to recover treble damages compared to only double damages under preceding legislation. The length of the statute of limitations was increased from six years to as many as 10 years; changes were made to the standard of proof required as well as the jurisdiction and venue components of the act.

On May 20, 2009, President Obama signed the Fraud Enforcement and Recovery Act of 2009 (FERA) into law. This legislation included the most comprehensive changes to the False Claims Act (FCA) since 1986. These changes included redefining a "claim" to the more expansive definition of "any request or demand, whether under a contract or otherwise, for money or property, and whether or not the United States has title to the money or property" where that claim is "presented to an officer, employee, or agent of the United States" or "made to a contractor, grantee, or other recipient, if the money or property is to be spent or used on the Government's behalf or to advance a Government program or interest." (31 U.S.C. § 3729(b)(2).) In addition, the intent requirement was revised to now require that a false statement be "material" to a false claim. Moreover, FERA expanded FCA liability to encompass "reverse false claims" whereby a party would conceal or decrease an obligation to pay the government. Equally important, the 2009 amendment expanded the grounds for a retaliation claim under the FCA by expanding the category of those entitled to whistleblower protection from "any employee" to "any employee, contractor, or agent." In our example above, the expanded scope of statutory protection is important for Elizabeth to consider in her advice to the company.

On March 23, 2010, President Obama signed the Patient Protection and Affordable Care Act (PPACA), which enacted further amendments to the False Claims Act. These changes prohibit potential relators from filing cases merely based upon the public disclosure of information, such as media reports or civil, criminal, or administrative hearings. Additionally, overpayments un-

der Medicare and Medicaid must now be reported within 60 days of discovery or by the date a corresponding hospital report is due. The PPACA also changed liability for kickbacks so that all claims submitted in violation of the Anti-Kickback Statute, 42 U.S.C. § 1320a-7b(b), automatically constitutes a false claim under the False Claims Act. Similarly, actual knowledge or specific intent is no longer required under the Anti-Kickback Statute pursuant to the 2009 amendments.

### Intent Requirement Under the FCA

Section 3729(b) of the False Claims Act establishes liability for false claims submitted "knowingly," which is defined as (1) having actual knowledge of the information, (2) acting in deliberate ignorance of the truth or falsity of the information, or (3) acting in a reckless disregard of the truth or falsity of the information. (31 U.S.C. § 3729(b)(1).) However, the statute makes clear that "no proof of specific intent to defraud" is required. (31 U.S.C. § 3729(b)(1)(B).) These definitions, part of the changes made in 2009 under FERA, were designed to combat a series of federal cases, such as *Allison Engine Co., v. United States ex rel. Sanders*, 553 U.S. 662 (2008), which endeavored to increase the government's burden of proof. In *Allison Engine*, the US Supreme Court reversed the decision of the United States Court of Appeals for the Sixth Circuit, which held that the government was not required to prove intent to cause a false claim to be paid by the government. Congress effectively

### FCA STATISTICS

- From October 1987 to September 2010, the False Claims Act recovered over \$27 billion of which \$2.87 billion was relators' shares.
- The Taxpayers Against Fraud Education Fund estimates that approximately 80 percent of False Claims Act recoveries occur in the health-care sector but there are recoveries from the defense, education, transportation, and the oil and gas areas as well.
- The Justice Department's total False Claims Act recoveries since January 2009 are over \$7.3 billion.
- Over 1,200 False Claims Act cases were under investigation by the Department of Justice as of September 30, 2010.
- At present, 28 states and the District of Columbia have their own qui tam statutes, which resulted in the return of hundreds of millions of dollars in Medicaid funds.

## RECENT FCA AMENDMENTS

- In 2009, the Fraud Enforcement and Recovery Act of 2009 redefined a “claim” to now include “any request or demand, whether under a contract or otherwise, for money or property, and whether or not the United States has title to the money or property”; expanded liability to “reverse false claims”; and extended the grounds for a retaliation claim under the FCA.
- In 2010, the Patient Protection and Affordable Care Act limited potential relators to those with actual knowledge of a false claim, expanded FCA liability to correspond with claims submitted in violation of the Anti-Kickback Statute, and eliminated the requirements for actual knowledge or specific intent under the Anti-Kickback Statute.

overruled *Allison Engine* and similar cases with the 2009 FERA amendments and explicitly stated that no proof of specific intent to defraud was required.

### The IRS “Bounty” Program

As detailed above, whistleblowers who file suit under the qui tam provision of the False Claims Act become named litigants in civil litigation. Within certain areas of the federal government, that is not the case. Specifically, under procedures of the Internal Revenue Service (IRS) and the Securities and Exchange Commission (SEC), whistleblowers provide information in exchange for a bounty if and when a recovery occurs. Criminal defense practitioners such as Elizabeth should be aware of such programs as they impact the advice they give to their corporate clients.

Under Internal Revenue Code § 7623(a), the IRS must pay awards to people who provide “specific and credible information” to the IRS if the information results in the collection of taxes, penalties, interest, or other amounts from a noncompliant taxpayer. The IRS wants specific information about significant tax issues. “Significant” is defined by the IRS as taxes, penalties, and interest owed in excess of \$2 million. This is not the venue to report speculative concerns, air personal disputes, drop a dime on a former spouse, or raise isolated events like a server failing to declare tips as income.

In fact, there are two basic tracks for whistleblower complaints filed with the IRS. On the first track, whistleblowers submit information concerning amounts in dispute (back taxes, interest, and penalties) in excess of

\$2 million. In these cases, the IRS is looking for non-compliant taxpayers with annual gross income of more than \$200,000. If the IRS successfully obtains a recovery from a noncompliant taxpayer, the IRS is required to pay the whistleblower between 15–30 percent of the recovery. If the whistleblower is not satisfied with the reward, an appeal may be filed with the United States Tax Court located in Washington, D.C.

The second track applies to cases involving less than \$2 million in dispute. If the IRS obtains a recovery in these cases, payment of a reward to the whistleblower is discretionary, with a maximum of 15 percent of the recovery up to a maximum of \$10 million. Whistleblowers on this track cannot appeal to the United States Tax Court.

An attractive component of the IRS program is its confidentiality. According to the IRS website, the IRS protects the identity of whistleblowers “to the fullest extent permitted by law.” Under some circumstances, a whistleblower might become a necessary witness in a judicial proceeding. In such cases, the IRS will inform the whistleblower and decide whether to proceed with the case. The drawback of confidentiality is that the whistleblower does not have open access to the status of the government’s case. The government will confirm receipt of the whistleblower’s claim, but thereafter it is largely a game of “hurry up and wait” for a check in the mail. There is no way to know if the IRS follows up on the proffered allegations. The IRS must wait until all appeal rights of the offending taxpayer have either expired or been exhausted before a reward to the whistleblower is even contemplated.

### SEC Whistleblower Program

In addition to the changes made under the PPACA in 2010, that year also saw an overhaul of the financial regulatory system through the Dodd-Frank Wall Street Reform and Consumer Protection Act, which created whistleblower protections for violations of securities laws. (*See* 15 U.S.C. § 78u-6.) Under this new law, whistleblowers may obtain payments for information used in furtherance of a SEC enforcement action.

These SEC whistleblowers may file a complaint anonymously or choose to disclose their identity. However, whistleblowers submitting anonymous complaints must be represented by counsel but may maintain their anonymity until just before the award is paid. The whistleblower’s complaint is submitted directly to the SEC and does not require filing a complaint with a federal district court as required under the False Claims Act. After receiving the complaint, the SEC investigates to determine whether to bring an enforcement action against the alleged violators.

However, a SEC whistleblower must have “original information,” defined as information that is (1) derived from the independent knowledge or analysis of the whistleblower; (2) not known to the SEC from any other source, unless the whistleblower is the original source of the information; and (3) not exclusively derived from an allegation made in a judicial or administrative hearing, in a governmental report, hearing, audit, or investigation, or from the news media, unless the whistleblower is the source of the information. (*Id.* § 78u-6(a)(3).)

Like a similar provision under the False Claims Act, a SEC whistleblower may collect between 10–30 percent of the total monetary sanctions recouped through a SEC

Federal cases construing section 3730(h) have held that the whistleblower subject to retaliation does not need to be familiar with the False Claims Act or even know about its existence. (*United States ex rel. Yesudian v. Howard University*, 153 F.3d 731, 740–41 (D.C. Cir. 1998).) It is sufficient that the whistleblower is investigating matters that are calculated to be or could lead to viable False Claims Act actions. (*Id.*) In fact, the False Claims Act has been construed so broadly that only where a suit was a “distinct possibility” when the whistleblower acted, most courts consider this requirement to be met. (*See Hutchins v. Wilentz, Goldman & Spitzer*, 253 F.3d 176 (3rd Cir. 2001).)

## **To protect whistleblowers, the SEC program prohibits a corporation subject to a claim from retaliating whatsoever.**

enforcement action, but only if the monetary sanctions exceed \$1 million. However, the amount of the award is entirely left within the discretion of the SEC. The SEC program specifically exempts from those able to receive an award anyone who gains the information through an audit required under the Securities Exchange Act; anyone convicted of a criminal violation related to the whistleblower’s action; or anyone who is a member of a regulatory agency, the Department of Justice, or a law enforcement agency.

In an effort to protect whistleblowers, the SEC program prohibits any corporation that is subject to a whistleblower claim or investigation from retaliating whatsoever against a whistleblower. A whistleblower is empowered to file a civil suit in federal court for damages resulting from the retaliation and may receive reinstatement, double back pay, and attorneys’ fees and costs.

### **Whistleblower Protection**

The False Claims Act provides protection for any whistleblowing employee, contractor, or agent who is subject to discrimination due to his or her lawful acts done in furtherance of a False Claims Act action. (*See* 31 U.S.C. § 3730(h).) The prohibited discrimination extends to a whistleblower who is “discharged, demoted, suspended, threatened, harassed, or in any other manner discriminated against in the terms and conditions of employment” by his or her employer. (*Id.*) Section 3730(h) also entitles a whistleblower subject to retaliation to reinstatement with the same seniority status, two times the amount of back pay with interest, and compensation for any special damages sustained as a result of the retaliation, including costs and attorneys’ fees.

Courts look to the following elements in a section 3730(h) action: (1) was the whistleblower’s conduct protected under the False Claims Act; (2) was the defendant aware of the protected conduct; and (3) was the discrimination due to the protected conduct? (*See United States ex rel. Karvelas v. Melrose-Wakefield Hosp.*, 360 F.3d 220, 235 (1st Cir. 2004); *McKenzie v. BellSouth Telecommunications, Inc.*, 219 F.3d 508 (6th Cir. 2000).) To succeed in a retaliation suit, the employee must demonstrate a “causal connection” between the alleged retaliation and the whistleblower’s involvement in a protected conduct. (*Hutchins*, 253 F.3d at 186.) However, once the whistleblower establishes the “causal connection,” the burden of proof falls on the defendant to show that the same decision would have been made despite the whistleblower’s involvement in a protected conduct. (*Id.*)

### **Conclusion**

Whether you are a junior partner like Elizabeth in a large firm, a solo practitioner, or anyone in between, it is essential for any attorney practicing white collar criminal defense to have a working knowledge of the False Claims Act. It is also wise to have an in-house expert on the statute or a colleague at another firm with whom you feel comfortable working on such issues. Use of federal and state false claims acts is on the rise. In the health-care industry alone, the federal government has collected \$15 from defendants for every \$1 spent on investigation and prosecution under the False Claims Act. This is a wonderful source of revenue for the government, and prosecutors at the highest levels of the Department of Justice know it. ■