FCA Scrutiny and Penalties on the Rise:

Federal Contractors Beware

INTRODUCTION

Two major developments in 2016 have altered the scope of both liability and damages under the False Claims Act ("FCA"). First, the Supreme Court has endorsed the "implied false certification" theory of liability. Second, federal agencies have implemented a new federal regulation that almost doubled FCA penalties. These developments continue the federal government's trend of increased scrutiny and enforcement of the FCA, and signal a warning to federal contractors to take extreme precaution in submitting any payment or claim for money to the government.

In 2015, for example, the Justice Department recovered $3.6 billion (down from a record $5.7 billion in 2014) in either settlements or judgments involving fraud, waste, abuse or other false claims brought under the FCA. Early reports indicate that this amount will increase by the end of 2016. Increased scrutiny of contractors under the FCA is due to certain factors that have caused FCA enforcement to increase in recent years, including financial incentives for whistle-blowers, attorneys, and the government. These incentives are not going away, and the increase is likely to continue. A key indicator that investigation and enforcement will continue to increase is the Obama Administration's most recent budget, which increased funding for fraud and compliance enforcement. That budget demonstrates a focus on fighting fraud, waste, and abuse in government contracting by increasing the number of compliance and fraud enforcers at several agencies, including the Department of Labor, the Department of Defense, the Department of Health and Human Services, and the General Services Administration. This added enforcement

IMPLIED FALSE CERTIFICATION RULE

A recent Supreme Court ruling opened a new avenue of liability for contractors. For years, the circuit courts have been split in determining whether a defendant's "implied false certification" of its compliance with contractual, regulatory, or statutory requirements is a valid basis for liability under the tenets of the FCA. On June 16 of this year, the U.S. Supreme court issued its long-awaited decision on the "implied false certification" theory of liability under the FCA. In June 2016, the Court held in *United States ex rel. Escobar v. Universal Health Services*, that, "at least in certain circumstances, the implied false certification theory can be a basis for liability." No. 15-7, 1 (2016). In the same decision, however, the Court defined the FCA's materiality requirement as rigorous and demanding, thus bolstering that standard.

In *Escobar*, the parents of a mental health patient alleged that the hospital providing inadequate treatment to their son by using under qualified personnel to deliver counseling services. The parents filed suit under the FCA alleging that the hospital "impliedly certified" that the counseling services were provided by certain types of professionals as required by state Medicaid requirements, when in reality, they were not. The parents' claims hinged on the viability of the "implied false certification" theory because the hospital's claims for payment did not expressly state anything about the medical professionals.

The Court held that the "implied false certification" theory can provide a basis for FCA liability, given, however, that the claims meet two conditions: (1) that the claim makes specific representations about the goods or services provided, and (2) that the defendant's failure to disclose noncompliance with material legal requirements "makes those representations misleading half-truths." *Id*. The Court also limited the kinds of undisclosed violations that can support an "implied false certification" claim, and did not address the question of whether all claims for payment implicitly represent that the billing party is legally entitled to payment." *Id*. at 9-10.

FCA PENALTIES DOUBLED

The impact of this new theory of liability was compounded when Congress mandated an increase in FCA penalties due to inflation, as part of a budget deal struck last year. Agencies were required to implement the new rule by August 1st of this year, which rule almost doubled FCA penalties on a per-claim basis. Under the new rule, minimum per-claim penalty rose to $10,781 (from $5,500), and maximum per-claim penalty rose to $21,563 (from $11,000). This increase in per-claim penalties could result in an explosion of big-dollar judgments and settlements, especially in cases involving thousands of potential claims or payments.

Such potentially astronomical judgments and settlements are expected to be accompanied by proportionally heightened challenges to the same, as being unconstitutionally excessive under the Eighth Amendment and Due Process Clause. Historically, contractors have been successful in challenging FCA penalties as "excessive fines" prohibited under the Eighth Amendment, especially in cases involving an immense number of fraudulent billing claims compared to a relatively small amount of actual damages. While doubled penalties under the new rule will greatly increase the disparity between the claimed amount and actual damages in some cases –seemingly increasing a contractor's odds of a successful challenge – a contractor still must overcome significant hurdles, and success is not guaranteed.

For example, in the 2013 case of *Bunk v. Gosselin*, the Fourth Circuit allowed a whistleblower to seek FCA penalties below the statutory minimum per-claim amount in order to avoid an Eighth Amendment challenge. Interestingly, the court also allowed the whistleblower to recover an amount far in excess of its actual damages. In that case, defense contractor Gosselin allegedly conspired in a price-fixing scheme that resulted in the submission of thousands of fraudulent invoices. Although the district court judge recommended only $500,000 in FCA penalties, the Fourth Circuit held that a $24 million recovery "appropriately reflects the gravity of Gosselin's

offenses and provides the necessary and appropriate deterrent effect going forward." Now subjected to the potential impacts of this new rule, federal contractors should take precautionary measures and prepare themselves for higher-stakes FCA cases.

Given these two major developments in FCA enforcement, contractors and their counsel should be ever vigilant and disciplined in assuring compliance to all regulations and contract provisions pertaining to the submission of claims for payment to the government. The consequences for failing to do so are far too great, as evidenced by the increasing intensity and rate by which the government is now detecting and prosecuting FCA violations.

In the end, you will be glad you made the call; by the way, it's a FREE CALL.

EXCELL CONSULTING "HERE TODAY FOR YOUR TOMORROW"

Author's note: The information contained in this article is for general informational purposes only. This information does not constitute legal advice, is not intended to constitute legal advice, nor should it be relied upon as legal advice for your specific factual pattern or situation. – John G. Balch, CEO CPCM

Authors: John G. Balch is CEO, and Taylor Benson is Assoc. General Counsel at Excell Consulting International, Inc., a Colorado Springs based firm specializing in government contracts.