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eINSIGHT

THE FALSE CLAIMS ACT

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There have been no significant changes to the law this past year. All the big news from 2013-2014 thus far has emerged from the courts.

In November, 2013, a jury in federal court in California found a company guilty of False Claims Act violations by stamping its pipe with certifications ratings of the Underwriters Laboratories ("UL") and the American Water Works Association ("AWWA") despite the pipes not meeting those standards. A separate trial will be held on damages, but given that the company sold approximately $2.2 billion (yes, billion) worth of pipe to the government over the period in question, the eventual damages award could be gigantic.

At the appellate level—where judicial decisions are published to guide the lower trial courts on how to address legal disputes—there was significant activity in the arena of the False Claims Act. The two biggest topics over the past year are two topics which consistently generate a lot of litigation: (1) employers retaliating against employees who became whistleblowers, and (2) what constitutes the "knowing" submission of a false claim. As is shown below by this explication of key California and federal cases, those issues are clearer now than they were a year ago.

CALIFORNIA STATE CASES:

1. *Contreras v. First Student, Inc.* 213 Cal.App.4th 1212

Background: This is a continuation of the Laidlaw Transit case which had a very important appellate holding in 2010. (Laidlaw Transit is now known as First Student, Inc.) In that opinion, the appellate court followed other jurisdictions, including federal False Claims Act rulings, and held that a violation of the California False Claims Act can occur if an implied certification is alleged to have occurred. In other words, if a contract with the government conditions payment on compliance with all the contract terms, any material breach of contract

can create False Claims Act liability when a request for payment on the contract is made for a period during which a breach of contract occurred. In Laidlaw Transit, it was alleged that the school bus company was not properly maintaining its bus fleet (regarding safety, pollution, etc.) and each payment application made while the bus fleet was in disrepair included an implied certification that the company was not in breach of its contract. With the Laidlaw Transit opinion, this is now enough to impose False Claims Act liability.

Facts: As the case was moving forward, the trial court ordered that the individual plaintiffs (i.e., the former bus company employees who were the qui tam whistleblowers) could not discuss the case with the bus company's current employees. The order was based in part on the fact that the bus company's employees were being represented by the bus company's attorneys, and therefore communications should not take place outside the presence of attorneys.

Ruling: The appellate court struck down the trial court's order, finding that it violated First Amendment free speech rights as well as the provisions of the False Claims Act itself. It is within the trial court's power to restrict attorneys from causing communications to occur through the plaintiffs. For example, it is perfectly acceptable for a court to order that attorneys not script questions for the plaintiffs to ask, or draft a document for the plaintiff to get others to sign. However, a trial court cannot forbid an individual plaintiff from speaking with current employees about a False Claims Act case on his/her own initiative.

What this means: This ruling makes it more difficult for an employer who is a defendant in a False Claims Act suit from restricting access to current employees. Plaintiffs are free to call current employees and talk about the case and even seek evidence which might help the plaintiff's case, outside the presence of the employer's counsel. As long as there is no evidence that the plaintiff's attorney directed, or at least significantly assisted, the plaintiff in doing so, there is nothing a trial court can do to prevent it. This diminishes the ability of employers to manage employee communications with involvement of their attorneys. Evidence of direct attorney involvement (i.e., scripting) may be hard to come by, of course, and even putting that aside, due to the amount of money which may be awarded to the plaintiff with a victory in court, one can expect qui tam plaintiffs to become increasingly significant investigators for their own cases as they reach out to current employees while the lawsuit is ongoing with greater freedom.

2. *McVeigh v. Recology San Francisco* 213 Cal.App.4th 443

Facts: The plaintiff suspected fraud is taking place at recycling centers. He discovered that other employees were falsifying/inflating the weight of recyclable materials being sold, and receiving kickbacks in return. The plaintiff reported these violations to the police. The plaintiff, who was initially tasked with investigating instances of fraud, also became very aggressive over

the next few years in trying to root out this fraud and other wrongs. He had significant trouble getting along with other employees, as he took on a "police" or "vigilante" mentality, which resulted in multiple, valid arrests of fellow employees. The employer eventually moved the plaintiff to a different position, but the plaintiff continued to press for the company to adopt enhanced surveillance and other security measures to prevent fellow employees from committing fraud. The plaintiff's employment review scores declined, and three years after his initial report of fraud, was terminated. He sued for retaliation under the False Claims Act, but the trial court threw the case out after determining that there were no False Claims Act violations (i.e., the employer was harmed by virtue of the employees' fraud, but the reimbursements from the state under the CRV program were measured differently and no government funds were paid as a result of the fraud.

Ruling: There are two significant holdings in this case. First, the appellate court ruled gave wide latitude to whistleblower protections, emphasizing that an employee is protected from retaliation if he/she has a reasonable belief that fraud is taking place. Although the court made clear that a completely baseless belief that wrongdoing was taking place was not protected activity, and therefore could not give rise to a retaliation claim, if an employee's belief that the government was being defrauded had a plausible basis, then the False Claims Act protects his activity into trying to prevent it. As long as he/she reasonably believes false claims to the government are occurring, an employer cannot retaliate against him/her. Second, people whose job it is in a company to investigate fraud and report it to their employers are generally not able to become plaintiffs under the False Claims Act. Since the False Claims Act encourages people to become whistleblowers who would not normally blow the whistle, it is not a vehicle to vindicate people who investigate fraud in their company for a living. But the appellate court held that since the plaintiff had reported illegal activity to the police, he had gone above and beyond the scope of his employment, and therefore came within the protection of the statute.

What this means: This case is about a man who was a mix between Serpico and a paranoid. He made some allegations during his employment that were strange, unfounded and disruptive. But just because one engages in the latter does not make it safe for an employer to fire him. Whistleblowers such as the plaintiff will be allowed to have their day in court and try to persuade a jury that he/she was retaliated against in violation of the False Claims Act, even if reasonably but incorrectly believed the government was being defrauded, and even in some instances when his job was to investigate his fellow employees and he did it in an unprofessional manner. In short, the protections given to whistleblowers against retaliation are broad, and employers should use great caution in terminating an employee who exposes the possibility of fraud and other wrongdoing.

3. *Driscoll v. Superior Court California Appellate Court* — January, 2014

Facts: A former employee sues his employer in California state court, claiming among other things that he was fired because he had complained about fraudulent billing practices made to Medicare. He sought relief under the federal False Claims Act under the "retaliation" protections of the statute. 31 U.S.C. 3730(h). The trial court dismissed that cause of action on the basis that a federal False Claims Act suit must be brought in federal District Court.

Ruling: A claim for retaliation under the federal False Claims Act can be tried in state court as well as in federal court.

What this means: Employers facing suits from former employees who are suing for wrongful termination and other grievances in state court can expect to face allegations of liability under the federal False Claims Act when the employee had complained of company practices involving billing to the federal government.

What this does not mean: Since the Driscoll decision relies in part on the fact that the federal government is not a real party in interest in a "retaliation" claim, this decision does not by itself open the door to normal federal False Claims Act suits being tried in state court.

FEDERAL CASES:

4. *United States v. Science Applications Int. Corp.* 2013 WL 3791423 (D.D.C.)

Facts: The federal government brought a False Claims Act suit against a company defendant who multiple consultant contracts over the years with the Nuclear Regulatory Commission ("NRC"). The company was hired to assist the NRC in developing potential regulatory rules and providing technical assistance—work which could impact the entire private nuclear power industry. The contracts with the NRC expressly required that neutrality was essential, and therefore the company had an obligation to be free of conflicts of interest and avoid doing business which would create conflicts of interest. The government claimed in its suit that the company instead entered into at least five different contracts performing work for other industry leading companies—companies who would be directly impacted by rules developed by the NRC with the assistance of the defendant. The government alleged in the suit that the defendant had implicitly certified with each payment request that it was in compliance with all regulations, laws and contract terms. A jury ruled against the defendant company in an amount totaling more than $6 million. The defendant sought reversal of the jury's verdict, and the D.C. District Court overturned the verdict based on an erroneous jury instruction allowing the jury to find the defendant company guilty of False Claims Act violations if the jury determined the "collective knowledge of all employees" of the company knowingly submitted false claims.

Ruling: In an "implied certification" case such as this, False Claims Act liability can be established if both: (a) the defendant knows it violated a contractual obligation, and (b) the defendant also knows its compliance with that obligation was material to the government's decision to pay. If both elements are met, then payment requests made with that knowledge are false claims under the statute. The key question in this matter is whether the same person must know both things, or whether it is sufficient that one person in a business has knowledge of one element, while a different person has knowledge of the other element. The court determined that at least one person at an organization must have knowledge of both, and liability under the False Claims Act cannot be imposed under a theory of "collective knowledge."

What this means: This case is one of the few that has limited the reach of the "implied certification" theory, which has caused a great expansion in the ease with which to prosecute a claim under the False Claims Act. For owners, this holding can likely be overcome by requiring express certification of material contract terms with each payment request. The more specific the certification, the better. This places the onus on the person actually requesting payment and actually certifying compliance to investigate compliance, or be guilty of deliberate ignorance, which itself opens up liability under the False Claims Act. For government contractors, this case provides some shelter for those companies who, innocently, has a right hand which does not know what the left hand is doing.

5. *Ulysses, Inc. v. United States* 110 Fed.Cl. 618

Facts: When a contractor filed suit against the U.S. government seeking payment for materials it produced under a purchase order, the government cross-complained against the contractor, charging violations of the False Claims Act. The contractor had provided its own manufactured circuit boards on previous government contracts. In response to a request for quotation which did not specify that the circuit board was exclusively single-source, the company faxed a quote to the contracting officer offering to fulfill an order. When the contractor was approximately 85% complete manufacturing the order, the government cancelled it and refused to compensate the contractor for any of its work because the contractor was manufacturing its own circuit board, instead of sourcing it from a company which was not listed in its request for quotation. The court resolved the dispute by deeming the cancellation of the purchase order as a termination for convenience, because the contractor was not at fault, and awarded damages to the contractor accordingly. The court also rejected the government's demand for False Claims Act violation.

Ruling: This case is similar to the Science Applications case in that it hinges on whether the contractor "knowingly" submitted a false claim. All the government was able to actually prove in this case was that the government and the contractor interpreted the request for

quotation, the quote, and the purchase order differently. When the issue of whether a contract interpretation constitutes a false claim, the proper inquiry is whether the contractor's interpretation "borders on the frivolous." The government in this matter argued just that—the contractor's interpretation was frivolous to the point of falsity. The court disagreed. The conduct of the contractor over multiple procurements, combined with the vague and arguably misleading language contained in the request for quotation, meant the contractor (whose interpretation was consistent from beginning to end) did not knowingly submit any false claim for payment.

What this means: This case is the most recent in a long line of decisions that found differing contract interpretations will not give rise to False Claims Act liability unless the interpretation proffered by the contractor is either frivolous or "borders on the frivolous." This case demonstrates how important it is for government requests for proposals to be clear about what is the scope of work to be performed. Vague and uncertain requests can cause reasonable responding contractors to devote significant resources to something the government does not want. This can lead not merely to a lawsuit and damages awarded against the government, but also an effective shield against False Claims Act liability, because the government is unable to establish a "knowing" violation.

For more information about this topic please contact:

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