

False Claims Act “Implied Certification” Update: Supreme Court Oral Argument Forecasts Continued Vitality of Controversial Doctrine

By C. Joël Van Over, Alexander B. Ginsberg and Danielle Vrabie

The U.S. Supreme Court heard oral argument on April 19, 2016, in United Health Services v. United States ex rel. Escobar, No. 15-7, a case expected to resolve the current split among federal appellate courts on the so-called “implied certification” theory of liability under the federal False Claims Act (FCA).¹ Although government contractors are hoping the Supreme Court invalidates implied certification altogether, this outcome seems increasingly unlikely after the oral argument. Rather, the Supreme Court may be expected to endorse at least some version of implied certification liability.

Background

The FCA, originally enacted during the Civil War to address frauds committed by military contractors against the Union Army, has become the government’s favorite enforcement tool against modern-day federal contractors. The FCA, imposes significant financial penalties for “knowingly present[ing], or caus[ing] to be presented, a false or fraudulent claim for payment or approval.”² The FCA also prohibits contractors from making false statements “material to a false or fraudulent claim.”³ The scope of the act and its application have been ever-expanding.

¹ This Alert is a follow-up to our earlier piece, [“Supreme Court to Hear False Claims Act ‘Implied Certification’ Appeal.”](#)

² 31 U.S.C. § 3729(a)(1)(A). The FCA defines “knowing” to include not only actual knowledge but also “deliberate ignorance” of and “reckless disregard” for the truth and clarifies that “no proof of specific intent to defraud” is required, *id.* § 3729(b)(1).

³ 31 U.S.C. § 3729(a)(1)(B).

The government has pursued FCA cases based on both “factually false” and “legally false” claims, a distinction recognized by several federal appellate courts.⁴ The former describes an “incorrect description of goods or services provided or a request for reimbursement for goods or services never provided” while the latter “is predicated upon a false representation of compliance with a federal statute or regulation or a prescribed contractual term.”⁵ Further, the courts have recognized two types of “legal falsity”—“express” and “implied” false certification.⁶

The FCA has been uniformly understood to create potential liability for a contractor who expressly certifies compliance with certain requirements that are material to payment when in fact the contractor has not complied with such requirements. The federal appellate courts have divided, however, regarding FCA liability for implied false certification—or liability where a contractor is out of compliance with a statute, regulation or contract requirement, but the contractor does *not* expressly certify such compliance.

The federal contractor community (including many health care providers) has long complained that implied certification creates undue and unjustified liability—with the potential for the government to escalate minor statutory, regulatory or contractual non-compliances into FCA actions, which expose defendants to tremendous financial penalties, including treble damages. Last year, the Seventh Circuit agreed and rejected the theory altogether, finding that it would be “unreasonable for us to hold that an institution’s continued compliance with the thousands of pages of federal statutes and regulations incorporated by reference into the [government contract in question] are conditions of payment for purposes of liability under the FCA.”⁷

The Seventh Circuit, however, currently holds the minority view. The majority of federal appellate courts—including the First, Second, Third, Fourth, Sixth, Ninth, Tenth, Eleventh and D.C. Circuits—have recognized at least some form of implied certification liability, several of them holding that such liability extends to knowing non-compliance with statutory, regulatory or contractual requirements that are clear preconditions of payment. The First and Fourth Circuits, on the other hand, appear to have adopted the broadest view of implied certification liability, holding effectively that *any* knowing, material non-compliance with government regulations or contract requirements potentially gives rise to FCA liability.⁸ As a result of this “circuit split,” the Supreme Court granted *certiorari* in *Escobar*.

Escobar and the First Circuit’s FCA Jurisprudence

Escobar, a case out of the First Circuit, involves allegations that a mental health clinic violated the FCA by seeking Medicaid reimbursement despite the fact that it failed to comply with certain regulations pertaining to staffing and employee supervision. The claims for reimbursement did not contain express certifications of compliance with the regulations. The First Circuit, reversing the district court’s dismissal of the

⁴ See, e.g., *Mikes v. Straus*, 274 F.3d 687, 696 (2d Cir. 2001).

⁵ *Id.*

⁶ See, e.g., *United States ex rel. Wilkins v. United Health Grp., Inc.*, 659 F.3d 295, 305-06 (3d Cir.2011)

⁷ *United States v. Sanford-Brown, Ltd.*, 788 F.3d 696, 711 (7th Cir. 2015), *petition for cert. filed*, No. 15-729 (U.S. Dec. 2, 2015).

⁸ See, e.g., *United States ex rel. Badr v. Triple Canopy, Inc.*, 775 F.3d 628, 636-37 (4th Cir. 2015), *petition for cert. filed*, No. 14-1440 (U.S. June 5, 2015) (“[W]e hold that the Government pleads a false claim when it alleges that the contractor, with the requisite scienter, made a request for payment under a contract and ‘withheld information about its noncompliance with material contractual requirements.’”).

complaint,⁹ held that “alleged noncompliance with regulations pertaining to supervision ... provided sufficient allegations of falsity to survive a motion to dismiss.”¹⁰

While embracing an expansive view of implied certification liability, the First Circuit notably followed its earlier precedents in “eschew[ing] distinctions between factually and legally false claims, and those between implied and express certification theories, [which] ‘create artificial barriers that obscure and distort [the FCA’s] requirements.’”¹¹ Instead, the First Circuit explained that it determines FCA liability by engaging in a “fact-intensive and context specific inquiry” to determine whether a contractor “knowingly misrepresented compliance with a material precondition of payment,” which need not be “expressly designated” as such.¹²

In briefing filed with the Supreme Court prior to oral argument, Petitioner Universal Health Services, Inc. asked the Court to rule that the FCA does not permit liability based on an implied certification theory, “under which claims that contain no affirmative misstatements are deemed to be ‘false or fraudulent.’”¹³ Petitioner argued that “false” under the FCA must be understood as “factually false” while “fraudulent” denotes “legally false.” Further, according to Petitioner, the common law definition of “fraudulent” does not impose liability for fraud absent the existence of special disclosure duties—which the FCA, in turn, does not contain.¹⁴ As an alternative argument, Petitioner asked the Court to hold that any application of implied certification liability must be “limited to circumstances in which a contractor has violated a statutory, regulatory, or contractual provision that is expressly designated as a precondition to payment.”

Respondents’ brief, by contrast, argued that “[k]nowingly billing the government for services that fail to meet material conditions falls squarely within the scope” of the FCA and that “the relevant payment condition need not bear a formal label as long as it is material and the defendant demands payment while knowingly violating it ... Nothing in the FCA’s text supports restricting it to violations of expressly designated payment conditions.”¹⁵ Numerous other interested parties also filed briefs on both sides of these issues.

Oral Argument

The recent oral argument, which echoed the foregoing themes, gave few indications that the Supreme Court plans to invalidate the implied certification doctrine—or even significantly to narrow its breadth.¹⁶

Petitioner’s counsel was peppered with hypothetical questions from the Court’s liberal contingent—many of the questions reflecting that certain Justices, like the First Circuit, do not accept the distinction between factual and legal falsity. Harkening back to the FCA’s Civil War roots, Justice Sotomayor queried skeptically whether: “providing a gun that doesn’t shoot to the Army is simply a contract breach?” Petitioner’s counsel stated it would depend on the facts, to which Sotomayor responded: “What—what

⁹ The district court had opined that, although the allegations against the clinic “raise serious questions about the quality of care provided[,] ... the False Claims Act is not the vehicle to explore those questions.”

¹⁰ *United States ex rel. Escobar v. Universal Health Servs., Inc.*, 780 F.3d 504, 514 (1st Cir. 2015), *cert. granted*, No. 15-7 (U.S. Dec. 4, 2015).

¹¹ *Id.* at 512 (quoting *United States ex rel. Hutcheson v. Blackstone Med., Inc.*, 647 F.3d 377, 385 (1st Cir.2011)).

¹² *Id.* at 512-13 (internal citations and quotations omitted).

¹³ Petitioner’s Brief is available [here](#).

¹⁴ Citing § 551 of the Restatement (Second) of Torts (limiting liability for nondisclosure to circumstances in which a person fails “is under a duty” to “exercise reasonable care to disclose the matter in question”).

¹⁵ Respondents’ Brief is available [here](#).

¹⁶ A transcript of the oral argument is available [here](#).

more facts do you need. Government contracted for guns. All of a sudden you deliver guns that don't shoot."

Justice Kagan similarly stated: "The government contracts to buy boots ... the boots fell apart after 12 hours. The government contracts to buy food, the food was rancid. ... And you're suggesting that all these hypotheticals—that somehow that's not a fraudulent claim. And I guess that leaves me sort of wondering what do you think would be a fraudulent claim? ... In demanding payment for satisfaction of the contract, you are not making a recommendation that you have satisfied the contract?" Petitioner's counsel replied: "Not that broadly ... not every jot and tittle of the contract."

For his part, Justice Breyer questioned whether a distinction between "material" and "non-material" contract provisions is sufficient to allay Petitioner's concerns (and those of the contractor community); Breyer stated: "you might implicitly imply that you fulfilled provision No. 43876(b) which says paper should be three inches long, okay? Or there could be an implicit lie that that person in your hospital was a doctor. The first you'd say is not material. The second is material. ... I wonder if a distinction like that ... would ... satisfy most of the concerns." Petitioner's counsel answered no and explained that "[s]omething that is capable of influencing a decisionmaker is material under the False Claims Act ... a very, very low standard."

Chief Justice Roberts' questioning of Respondents' counsel evinced a perspective more favorable to Petitioner. In response to a fact pattern describing a gross breach of contract or regulatory violation, Roberts stated: "I suspect most cases are a little more complicated than that, and that's where the difficulty comes in when you have hundreds, thousands of pages of regulations." Respondents' counsel explained that regulations in question must be "material" to impose FCA liability. Later, Roberts asked counsel for the United States whether the following hypothetical facts give rise to implied certification liability: "So the contract is to provide all these health services, and by the way, you've got to buy, you know, staplers made in the United States, not—not abroad. And they do everything, but they don't buy staplers made in the United States." When counsel responded that if "the government would be legally entitled to withhold payment or a portion of the payment in that circumstance, then that would be a false claim," Roberts responded, "then I don't understand the difference between material and immaterial."

Ultimately, Petitioner's counsel urged the Court to apply the definition of fraud found in section 551 of the Restatement of Torts and warned of the "parade of horrors" that will befall government contractors if the Court fails to limit scope of implied certification.

Conclusion

The Supreme Court's forthcoming decision will, at minimum, bring greater clarity to an extremely high-stakes but heretofore equally unpredictable and inconsistent area of law. If the recent oral argument is any guide, however, it is unlikely that the Court will dispose of implied certification theory altogether. The extent to which five Justices will be able to agree on reasonable boundaries for implied certification is not apparent from the oral argument. If the Supreme Court is unable to agree on such boundaries, however, or permits the First Circuit's expansive view of the doctrine to persist, the government contractor community will remain vulnerable. Stay tuned for our coming Alert on the Supreme Court's decision, which may be issued at any point during the current 2016 Supreme Court term which ends on October 2, 2016.

If you have any questions about the content of this alert please contact the Pillsbury attorney with whom you regularly work, or the authors below.

C. Joël Van Over [\(bio\)](#)
Northern Virginia
+1.703.770.7604
joel.vanover@pillsburylaw.com

Alexander B. Ginsberg [\(bio\)](#)
Northern Virginia
+1.703.770.7521
alexander.ginsberg@pillsburylaw.com

Danielle Vrabie [\(bio\)](#)
New York
+1.212.858.1683
danielle.vrabie@pillsburylaw.com

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