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SCOTUS Oral Argument Suggests FCA Implied Certification Theory Is Here to Stay – But Perhaps with Limits

Oral argument in **Universal Health** ***indicates Justices disinclined to categorically reject False Claims Act implied certification theory, though may limit its scope.***

On April 19, 2016, the United States Supreme Court heard oral argument in *Universal Health Services, Inc. v. United States ex rel. Escobar,* No. 15-7 (U.S.), to review the so-called "implied certification" theory of liability under the federal False Claims Act (FCA). This theory has the potential to drastically expand the FCA's scope, converting any request for payment from the government into a statement that the contractor is in compliance with all governing statutes, regulations and contract provisions.

While predicting exactly what the Supreme Court will do is never wise, particularly with an eight-member Court, it seems unlikely that the Court will issue a categorical rejection of the implied certification doctrine. Several Justices made statements indicating their belief that this theory was reasonable, and that any definition of a "false or fraudulent claim" that requires the falsity or fraud to be express on the face of the claim would be too narrow.

Several Justices, however, expressed concern with the doctrine's breadth. Notably there was no discussion of the "condition of payment" limit imposed by many federal courts of appeal, even though the validity of that limit was an issue under review. It remains uncertain as to whether the Court's decision will provide some welcome limits on the doctrine's reach — or whether the Justices will find that the materiality and scienter elements in the statute are sufficient.

Universal Health Services Inc. v. United States Ex Rel. Escobar

The relators who filed suit are the parents of a teenager who died of a seizure at a Massachusetts mental health clinic owned and operated by Universal Health Services, Inc., a national operator of hospitals and other healthcare facilities. The Massachusetts clinic received federal and state Medicaid funds and relators claimed that because the clinic failed to comply with state regulations in hiring and supervising staff, the clinic's submission of Medicaid claims violated the federal and Massachusetts FCA. The district court dismissed the relators' complaint, distinguishing between conditions of *payment* and conditions of *participation* and holding that only noncompliance with a condition of *payment* — that is, a statutory or regulatory provision that must be met in order for the payment to be made — could render a claim "false" and trigger FCA liability. Upon review of the specific state regulations at issue, the district court found that because the regulations lacked explicit text stating they were conditions of payment, the licensing and

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supervising rules were conditions of *participation* in the state Medicaid program and therefore noncompliance did not render claims for payment "false" and result in FCA liability.[1]

The First Circuit reversed, holding that the state regulations "clearly impose conditions of payment"[2] and noting that "[a]lthough the record [was] silent as to whether [the clinic] explicitly represented that it was in compliance with conditions of payment when it sought [Medicaid] reimbursement …, we have not required such 'express certification' in order to state a claim under the FCA."[3]

Universal Health Services sought review of the First Circuit's decision in light of the circuit split on the validity of the implied certification theory. The US Supreme Court granted *certiorari* and certified two questions for review: (1) whether the theory of implied certification is valid at all and, if so, (2) whether the theory applies only if a government contractor fails to comply with a statute, regulation or contractual provision that is expressly identified as a condition of receiving payment from the government.

Court's Decision Will Resolve Complex Circuit Split

The Court's June 2016 decision will resolve a circuit split on the implied certification theory's validity and scope. Most recently, the Seventh Circuit in *United States v. Sanford-Brown, Ltd.*, held that implied certification claims cannot be brought under the FCA. The court stated that to hold that "thousands of pages of federal statutes and regulations … are conditions of payment for purposes of liability under the FCA" would be "unreasonable."[4] Further, "[t]he FCA is simply not the proper mechanism … to enforce conditions of participation" in a government program.[5]

The majority of the federal circuit courts (First, Second, Third, Fourth, Sixth, Ninth, Tenth, Eleventh and D.C. Circuits) have recognized the doctrine's validity in various forms. As explained in its opinion in this case, the First Circuit "take[s] a broad view of what may constitute a false or fraudulent statement" and any knowing misrepresentation of "compliance with a material precondition of payment" is sufficient to trigger FCA liability.[6] In the First Circuit, a "material precondition of payment … may be found in sources such as statutes, regulations, and contracts, [and] need not be 'expressly designated.'"[7] The Fourth and D.C. Circuits apply a similarly broad view of the implied certification theory of liability, posing considerable risk to government contractors and healthcare providers operating in these jurisdictions.[8]

The Second, Third, Sixth, Ninth, Tenth and Eleventh Circuits endorse a narrower view of the implied certification theory, rejecting liability based on conditions of participation and instead limiting liability to situations where compliance with the particular regulation is expressly identified as a condition of payment.[9] In rejecting a broad application of the implied certification theory — such as that endorsed by the First, Fourth and D.C. Circuits — the Second Circuit reasoned that a broad application would be particularly inconsistent with the needs of government contractors in the healthcare field "because the False Claims Act was not designed for use as a blunt instrument to enforce compliance with all medical regulations."[10]

The Supreme Court's decision will resolve the circuit split as to whether the implied certification theory is a valid trigger of FCA liability, and, if so, the theory's proper scope.

Justices' Questions Suggest Reluctance to Categorically Reject the Implied Certification Theory

Several Justices — Justices Ginsburg, Breyer, Sotomayor and Kagan — expressed skepticism at the petitioner's argument that a claim for payment does not imply compliance with other regulations and contract provisions. These Justices indicated concern that eliminating the implied certification theory

would improperly narrow the FCA's reach — even to the point that the types of misdeeds by contractors in the Civil War that led to the FCA's enactment would no longer constitute FCA fraud.

Below are examples of the lines of questioning the petitioner fielded from these Justices:

- Justice Ginsburg: "It can't mean misleading, then? So 'false' can only mean false? It can't mean deceptive, misleading?"[11]
- Justice Breyer: "[T]here can be implicit lies. Of course, there has to be an implicit lie."[12]
- Justice Kagan: "In demanding payment for satisfaction of the contract, you are not making a recommendation that you have satisfied the contract?"[13]
- Justice Kagan: "[T]he entire idea behind this statute is that in that demand of payment is a representation. The representation is that I've given you guns that shoot and boots that wear and food that can be eaten … when that is not true, that is a fraudulent claim."[14]
- Justice Sotomayor: "I always thought that when you asked for payment, you're making a promise: I did what I agreed to do. Pay me, please. That's, to me, what's sort of understood. If I hired you to provide me with doctor services, you ask me for money, I'm assuming you provided me with doctor services. And you know you didn't. Why isn't that a fraud?"[15]
- Justice Sotomayor: "I have a very hard time accepting that … if you claim money for a service that you don't render, not a qualified individual, unsupervised by a qualified individual, which is a requirement specifically in the regulations, I'm having a hard time understanding how you have not committed a fraud."[16]

Justices Search For Possible Limitations to Implied Certification Theory

At the same time, however, some lines of questioning indicated that the Justices were also troubled by the potential breadth of the implied certification theory, suggesting that the Court may set limitations on the theory's scope. For example, Chief Justice Roberts seemed to be troubled by the government's affirmative response to his question as to whether the implied certification theory would reach the case in which a health services contractor submits a claim for payment but fails to comply with a wholly ancillary requirement, such as the obligation to buy staplers made in the US rather than abroad. Chief Justice Roberts responded: "If that would be a false claim ... and a relator can sue for that, then I don't understand the difference between material and immaterial."[17]

Justice Kennedy expressed a concern that some type of limiting principle was needed, stating that "it seems to me we just can't think about fraud unless we have materiality in some sense. And it could be a very strict standard of materiality."[18]

Even Justice Breyer, who pushed back on the petitioner's position that implied certification is never proper, posited that the principle of materiality from contract law may provide a workable test: "A material breach of contract is a … breach that allows one party to repudiate the contract. A nonmaterial breach is a breach that gives rise to damages but cannot serve as the basis of repudiation."[19] Justice Breyer also engaged in a line-drawing exercise with the petitioner, asking "what the sentence in the opinion should say that describes the circumstances under which the person who submits a form … [has] committed fraud."[20]

Of particular note, neither the Justices nor the oral advocates mentioned the second issue before the Court: whether the implied certification theory applies only if the statute, regulation or contractual provision expressly provides that compliance is a condition of receiving payment from the government. Given the fact that several courts of appeal have embraced this limiting principle, the Court may follow suit and adopt this approach.

Conclusion

The Court's decision in this case is expected in June 2016. While it is unclear from the argument how the case will be decided, two themes emerged. First, it appears that a majority of the Court is not prepared to invalidate the implied certification theory in its entirety. And second, it is possible that the Court will nevertheless adopt some form of limiting principle on the implied certification theory to address the issues of overbreadth, notice and fairness. As a practical matter, companies receiving government funding should be mindful of the high-risk nature of government contracting, and focus on internal controls and risk mitigation strategies.

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Endnotes

[1] *United States ex rel. Escobar v. Universal Health Servs.*, Inc., No. CV-11-11170-DPW, 2014 U.S. Dist. LEXIS 40098, *20-32 (D. Mass. Mar. 26, 2014). Relators did identify one regulation, 130 C.M.R. § 429.439, that was a condition of payment. However, the district court found that relators had not sufficiently pled that the clinic violated the requirements of this regulation. *See id.* at *27-28.

[2] *United States ex rel. Escobar v. Universal Health Servs.*, 780 F.3d 504, 513 (1st Cir. 2015).

[3] *Id.* at 514 n.14 (citing *United States ex rel. Hutcheson v. Blackstone Med., Inc.*, 647 F.3d 377, 385—86 (1st Cir. 2011)).

[4] *See United States v. Sanford-Brown, Ltd.*, 788 F.3d 696, 711-12 (7th Cir. 2015).

[5] *Id.*

[6] *Escobar*, 780 F.3d at 512.

[7] *Id*. (citing *Hutcheson*, 647 F.3d at 387-88).

[8] *See United States v. Triple Canopy, Inc.*, 775 F.3d 628, 636 (4th Cir. 2015) (“[W]e hold that the Government pleads a false claim when it alleges that the contractor … made a request for payment under a contract and withheld information about its noncompliance with material contractual requirements.”) (internal citations omitted); *United States v. Sci. Applications Int'l Corp.,* 626 F.3d 1257, 1269 (D.C. Cir. 2010) (“[T]o establish the existence of a ‘false or fraudulent’ claim on the basis of implied certification of a contractual condition, the FCA plaintiff … must show that the contractor withheld information about its noncompliance with material contractual requirements. The existence of express contractual language specifically linking compliance to eligibility for payment may well constitute dispositive evidence of materiality, but it is not … a necessary condition.”).

[9] *See United States ex rel. Mikes v. Straus,* 274 F.3d 687, 699-700 (2d Cir. 2001) (“”[I]mplied false certification is appropriately applied only when the underlying statute or regulation … *expressly* states the provider must comply in order to be paid.”); *United States ex rel. Wilkins v. United Health Group, Inc.*, 659 F.3d 295, 307 (3d Cir. 2011) (“Thus, under this theory a plaintiff must show that if the Government had been aware of the defendant's violations of the Medicare laws and regulations that are the bases of a plaintiff's FCA claims, it would not have paid the defendant's claims.”); *United States ex rel. Augustine v. Century Health Servs.*, 289 F.3d 409, 414 (6th Cir. 2002) (“[L]iability can attach if the claimant violates its continuing duty to comply with the regulations on which payment is conditioned.”); *Ebeid v. Lungwitz*, 616 F.3d 993, 996-98 (9th Cir. 2010) (recognizing a theory of implied certification under the FCA, which “occurs when an entity has previously undertaken to expressly comply with a law, rule, or regulation, and that obligation is implicated by submitting a claim for payment even though a *certification* of compliance is not required in the process of submitting the claim”); *United States ex rel. Conner v. Salina Reg'l Health Ctr., Inc.*, 543 F.3d 1211, 1218 (10th Cir. 2008) (“If a contractor knowingly violates [a prerequisite to the government's payment] while attempting to collect remuneration from the government, he may have submitted an impliedly false claim.”); *McNutt ex rel. United States v. Haleyville Med. Supplies, Inc.*, 423 F.3d 1256, 1259 (11th Cir. 2005) (“The violation of the regulations and the corresponding submission of claims for which payment is known by the claimant not to be owed makes the claims false...”).

[10] *Mikes*, 274 F. 3d at 699.

[11] Transcript of Oral Argument at 4.

[12] *Id*. at 10.

[13] *Id*. at 17.

[14] *Id*. at 16.

[15] *Id*. at 12.

[16] *Id*. at 54.

[17] *Id.* at 40-41.

[18] *Id.* at 14.

[19] *Id.* at 42.

[20] *Id*. at 21.