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The False Claims Act: Implied Liability, Knowing Misrepresentation, and Materiality
Universal Health Services v. Escobar, 579 U.S. ____ (2016)

Background

The False Claims Act (“FCA”) imposes significant penalties on those that defraud the Government. The focus of the FCA is on those that present or induce others to present false or fraudulent claims to the Government for payment. There has been a split between the circuit courts in regards to how far that liability extends. Specifically, some courts have held contractors liable for “implied” certifications, meaning a Government contractor impliedly certifies that everything is true that is a condition of payment. Other courts have imposed liability only when such certification is explicit. A few circuits have found themselves in the middle-not imposing an automatic liability trigger, which all out implied certification seems to do, and not requiring full and explicit certifications to hold a Government contractor liable.

Executive Summary

On June 16, 2016, the U.S. Supreme Court unanimously resolved the circuit split. The key questions resolved were the following: (1) omissions are misrepresentations, thereby implied certifications that are false may be a basis for liability if they are made knowingly and are material; (2) the FCA’s definition of what constitutes a defendant’s state of mind (or knowingly) when submitting an invoice is that the defendant must have implied or actual knowledge that the subject is material to inducing payment; and (3) the FCA definition of materiality **cannot** be so expansive so as to include every minor or insubstantial violation; especially when the Government routinely knows about the minor violation and pays such invoices anyway.

Analysis

Key Points

- When evaluating materiality under the FCA, the Government’s decision to expressly identify a provision as a condition of payment is relevant, but not automatically dispositive.
- Proof of materiality can include, but is not necessarily limited to, evidence that the defendant knows the Government consistently refuses to pay claims based on noncompliance with the particular statutory, regulatory, or contractual requirement.



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- Conversely if the Government pays a particular claim in full despite its actual knowledge that certain requirements were violated, that is very strong evidence that the requirements are not material.
- Additionally, if the Government pays a particular type of claim in full despite actual knowledge that certain requirements were violated, and has signaled no change in position, that is strong evidence the requirements are not material.
- The Court rejected the position that the Government may refuse to pay part or all of any invoice despite the fact that the Government may otherwise routinely pay such invoices knowing minor or insubstantial violations may be contained in those invoices.

Knowingly in a Nutshell

As one would imagine, there are fighting words in this decision that can be expected to be litigated for years to come. In that regard, knowingly and materiality, their definitions as well as application are going to be key in FCA cases. The FCA statute defines the state of mind for **knowingly** (or knowing) as a person who acts that has “actual knowledge of the information” *or* “acts in reckless disregard of the truth or falsity of the information.” In applying this standard, the Court found the defendant can have actual knowledge that a condition (such as a gun being able to fire) is material without the Government specifically saying it is so.

Material in a Nutshell

The FCA defines **material** to mean “having a natural tendency to influence, or be capable of **influencing**, the payment or receipt of money or property.” (Materiality later comes into play in the decision as to whether or not the misrepresentation influenced the Government’s course of action-not just resting on a single fact or occurrence as determinative.)

The Definition of Fraud Including Omission, thereby Allowing Implied Certification Liability

The Court defined fraud using its well-settled meaning at common law, which includes omission; thereby allowing for implied certifications to be considered fraud under the FCA. Accordingly, the Court held “that the implied certification theory can be the basis for liability where at least two conditions are satisfied: first, the claim does not merely request payment, but also makes specific representations about the goods or services provided; and second, the defendant’s failure to disclose noncompliance with material statutory, regulatory, or contractual requirements makes these representations half-truths.”

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The Court also concluded that “not every undisclosed violation of an express condition of payment automatically triggers liability.” That is, whether “a provision is labeled a condition of payment is relevant to but not dispositive of the materiality inquiry.”

How Materiality Should be Enforced

The Court did not decide whether the FCA’s materiality requirement was governed by the Act or derived directly from the common law because under “any understanding of the concept,” materiality ‘looks to the effect on the likely or actual behavior of the recipient of the alleged misrepresentation.’ For purposes of the FCA, the Court found that the materiality standard is demanding because the FCA is not “an all-purpose anti-fraud statute.”

That is, a misrepresentation **cannot** be deemed material merely because the Government designates compliance with the particular statutory, regulatory, or contractual requirement as a condition of payment. Nor is it sufficient for a finding of materiality that the Government would have the option to decline to pay if it knew of the defendant’s noncompliance.” Additionally, “materiality **cannot** be found where noncompliance is minor or insubstantial.”

Conclusion

While the Court did allow implied certification to become the law of the land, it also seemingly limited the application of the FCA by defining and applying the terms “knowingly” and “materiality” more narrowly than the Government had hoped it would do. Look for additional lawsuits to iron out the details further.