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## Supreme Court Endorses FCA Implied False Certification Theory of Liability with Limitations

BY S. JEANINE CONLEY AND AUNDREA GAMBLE HOLT

In a unanimous decision, the U.S. Supreme Court issued its highly anticipated False Claims Act (“FCA”) opinion in *Universal Health Services, Inc. v. United States ex rel. Escobar*. The June 16, 2016, Court decision resolves a split among the circuit courts and holds that the “implied false certification theory” is a viable theory of liability under the FCA. Under this theory, a contractor seeking payment from the government may be liable for violations of government regulations if it “makes specific representations about the goods or services provided but knowingly fails to disclose violations of material requirements regarding those goods and services.”<sup>1</sup> Liability may attach even if the contractor did not expressly certify compliance with the regulation requirements and the regulations are not designated conditions of payment. The Court, however, limited liability under the theory by establishing a demanding standard for what constitutes materiality. As discussed below, the Court’s decision is significant not only due to its adoption of the implied false certification theory, but also because new litigation brought under this theory will likely cause far-reaching implications for employers.

### Background

The claimants in *Escobar* sued a hospital management company after its subsidiary, a mental health facility, provided medication to the claimants’ daughter. She suffered an adverse reaction to the medication and later died from a seizure. The claimants alleged that the company (through the subsidiary) violated the FCA when it submitted claims to Medicaid for payment but failed to disclose that the employees providing the services were not properly qualified as licensed physicians or psychologists. According to the complaint, even though the company did not expressly certify that the individuals were qualified to render services, it was liable under the implied false certification theory because its omission rendered its claim misleading.

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<sup>1</sup> *Universal Health Services, Inc. v. United States ex rel. Escobar*, No.15-7, 2016 WL 3317555 (June 16, 2016).

The district court dismissed the complaint, holding that a contractor could only be held liable if the violated regulations constituted a condition of payment under the regulatory scheme. However, on appeal, the First Circuit held that any statutory, regulatory or contractual violation can be material whether expressly identified or through implication, and is therefore actionable as long as the defendant knows that the government would be entitled to refuse payment were it aware of the violation.

### **The Supreme Court's Decision**

Although the Supreme Court rejected the district court's condition of payment interpretation, it did not adopt the First Circuit's expansive view of liability. Instead, the Court held that the implied false certification theory is viable in "at least certain circumstances." Specifically, a contractor may violate the FCA if it submits a claim for payment and knowingly fails to disclose its noncompliance with a statutory, regulatory, or contractual requirement that renders the contractor's specific representations about its goods or services misleading. In other words, the party violates the FCA if it knowingly submits a "half-truth[]," in that it omits critical qualifying information that the party knows is material to the government's payment decision. The Court reasoned that the FCA "encompasses claims that make fraudulent misrepresentations, which include certain misleading omissions," and here, by using payment codes and identification numbers without also disclosing the violations of basic staff and licensing requirements, the claims constituted misrepresentations.

The Court rejected the company's argument that the FCA limited liability to only those claims of misrepresentation about express conditions of payment but also held that the mere fact that a statutory, regulatory, or contractual requirement is a condition of payment does not mean that a submitting party's noncompliance violates the FCA. The Court reasoned that such arguments could result in the government designating everything a condition of payment. Instead, the Court ruled that whether noncompliance is actionable turns on whether the misrepresentation is material. The Court set forth a rigorous standard of analysis for making that determination. The determination does not rest on whether the government had the option of withholding payment, but whether a contractor should have known that the government was likely to withhold payment if it knew of the undisclosed regulatory violation. Furthermore, the government's payment of a particular claim despite actual knowledge that certain requirements were violated or its continuous payment in that instance is strong evidence that those requirements are not material.

The Court further held that the FCA is not an "all-purpose antifraud statute . . . or a vehicle for punishing garden-variety breaches of contract or regulatory violations" and that "materiality cannot be found where noncompliance is minor or substantial."

The Court therefore vacated the First Circuit's decision and remanded the case to determine whether claimants stated a claim under the FCA.

### **Takeaways**

The implied false certification theory provides yet another means for whistleblowers to bring claims against their employers. In this case, employees of the company's subsidiary brought the violations to the claimants' attention. Thus, compliance training continues to be critical as well as having numerous reporting mechanisms in place for employees to report any suspected violations of government regulations, whether or not expressly provided in a claim or submission to the government. Accordingly, employees must be able to report wrongdoing without fear of retaliation.

The ruling is not a complete loss for employers. The Court established stringent limitations on what constitutes a "material" misrepresentation under the FCA, an area employers will be able to address at the summary judgment or trial stage.