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Whistleblower Defense Alert: Escobar: The Supreme Court Upholds Implied Certification Theory

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On Thursday, June 16, 2016 the United States Supreme Court released its decision in *Universal Health Services, Inc. v. United States ex rel. Escobar* (No. 15-7). In *Escobar*—argued on April 19, 2016—the Court decided the legal validity of the “implied certification” theory of liability under the False Claims Act (FCA). Specifically, the Court addressed:

1. Whether the “implied certification” theory of legal falsity under the FCA – applied by the First Circuit below but recently rejected by the Seventh Circuit – is viable; and
2. whether, if the “implied certification” theory is viable, a government contractor's reimbursement claim can be legally “false” under that theory if the provider failed to comply with a statute, regulation, or contractual provision that does not state that it is a condition of payment, as held by the First, Fourth, and D.C. Circuits; or whether liability for a legally “false” reimbursement claim requires that the statute, regulation, or contractual provision expressly state that it is a condition of payment, as held by the Second and Sixth Circuits.

Under the implied certification theory, a company may be held liable under the FCA if it is out of compliance with regulations, but certifies that it is in compliance with those regulations when seeking payment from the government.

In the unanimous decision, delivered by Justice Thomas, the Court ruled that implied certification, “at least in some circumstances,” was a viable theory of liability under the FCA. Specifically, the Court held that when “a defendant makes representations in submitting a claim but omits its violations of statutory, regulatory, or contractual requirements, those omissions can be a basis for liability if they render the defendant’s representations misleading with respect to the goods or services provided.” (P. 8) Moreover, the Court held that the regulations underlying an implied certification violation of the FCA need not be explicit conditions of payment in order to establish FCA liability. (Pp. 11-12)

Although defendants will be disappointed that the Court did not recognize the “condition of payment” limitation on liability, the Court greatly tempered the potential breadth of the implied certification theory by concluding that “not every undisclosed violation of an express condition of payment automatically triggers liability.” (P. 12) The Court created a very strict materiality standard, making it clear that liability would not lie where “noncompliance is minor or insubstantial.” (P. 16) The Court also rejected the government’s ability to declare by itself what it deems material, stating that “a misrepresentation cannot be deemed material merely because the Government designates compliance with a particular statutory, regulatory, or contractual requirement as a condition of payment.” (P. 15) Accordingly, the Court rejected the “extraordinarily expansive view of liability” espoused by the First Circuit—that “any statutory, regulatory, or contractual violation is material so long as defendant knows that the Government would be entitled to refuse payment were it aware of the violation.” (P. 17)

The Court also held that the government’s continued payment of claims after actual knowledge of a noncompliance is “very strong evidence” that the requirement at issue was not material. (P. 16) This suggests that the government’s continued payment of claims after it investigates a relator’s allegations of wrongdoing could defeat the relator’s claims.

While the validity of the implied certification of FCA liability may no longer be subject to attack, the Court’s decision in *Escobar* allows for potent defense arguments associated with the FCA’s materiality requirement, particularly at the motion to dismiss and summary judgment stages. The clear rejection of an “extraordinarily expansive view of liability” based solely on the ability to characterize a provision or regulation as a condition of payment will allow potential FCA defendants to more effectively battle claims and allegations associated with immaterial regulations and instances of minor or insubstantial noncompliance.