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False Claims Act: Weakening The Public Disclosure Defense

The Editor interviews Peter B. Hutt II, Partner, Akin Gump Strauss Hauer & Feld LLP. See Mr. Hutt's editorial on page 16.

Editor: Please give us a little background on the False Claims Act.

Hutt: The False Claims Act is, and has been for more than 20 years, the principal tool used by the government to combat fraud in federal programs, including defense contracting, Medicare and Medicaid. Almost everyone would agree that this statute has been very effective in doing so.

The unique feature of the law is that the statute permits not only the Department of Justice but also whistleblowers known as *qui tam* plaintiffs to file lawsuits alleging fraud or false claims. *Qui tam* plaintiffs have a tremendous financial incentive to file these lawsuits because they stand to receive up to 30 percent of the ultimate United States recovery if fraud is proven. The recoveries can be astronomical, because there are treble damages and penalties for each false claim.

What has happened over the course of the last quarter century is that a large, well-funded and highly sophisticated *qui tam* plaintiffs' bar has grown up. There had been no substantial amendments to the False Claims Act in the past 25 years. About three years ago, the *qui tam* plaintiffs' bar decided it was a propitious time to seek changes to the statute. The explicit goal of these lawyers was to increase the incentives for *qui tam* lawsuits and to remove various statutory obstacles to filing suit.

About a year ago, Congress passed FERA, which amended the False Claims Act by broadening the liability provisions and overturning several cases that the *qui tam* bar disliked. These changes expanded the categories of persons who might face False Claims Act lawsuits. This now includes any person who does business with the government by contract or receives a grant from a federal agency, whether directly or indirectly; who does business with any person who receives Medicare or Medicaid money; or who receives money in any other way, directly or indirectly, from the federal government.

Peter B. Hutt II

As a result of FERA, the False Claims Act has become a much more dangerous and very far-reaching law. You may be submitting a claim to an entity that on its face has no connection to the federal government, but may be deriving some of its funding from the United States. It can be difficult for a submitter of claims to tell when the statute might apply and when the statute will not apply.

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Editor: What happened after the enactment of FERA?

Hutt: Although FERA made several changes, it did not get rid of all the procedural obstacles that the *qui tam* plaintiffs' bar faced, including two defenses that were a thorn in the plaintiffs' side.

The first of those defenses was Rule (9)(b), which is the general provision that all plaintiffs coming into federal court must plead fraud with particularity. The *qui tam* plaintiffs sought an amendment to the statute that would relieve them of this obligation to plead fraud with particularity. So far they have been unsuccessful in their efforts.

Second, *qui tam* plaintiffs sought to essentially eliminate the other important defense available to defendants in False Claims Act cases, known as the public disclosure bar. The public disclosure bar, which was added to the False Claims Act back in 1986, was intended to guard against so-called "parasitic" lawsuits, by which Congress meant lawsuits that were based upon public disclosures of information in certain specified ways, including the news media as well as disclosures in government hearings, audits and investigations.

The public disclosure bar included an exception for actions that were asserted by original sources. An original source was defined as someone who had direct and independent knowledge of the information and who had voluntarily provided that information to the government.

The basic idea of the public disclosure bar was that individuals couldn't cash in on knowledge about fraud unless they were true whistleblowers coming forward with fresh information before any public disclosure or, if there had already been a public disclosure, if they were the individuals responsible for the public disclosure.

The public disclosure bar worked very well over the course of 25 years because it weeded out those lawsuits that were parasitic in nature – namely, lawsuits that didn't provide any fresh, new information about fraud to the federal government.

The problem with the statute from the *qui tam* plaintiff perspective was that many lawsuits were getting thrown out under Rule 12(b)(1) or on summary judgment motions. That's what motivated the *qui tam* plaintiff lawyers to suggest various changes to the public disclosure bar.

Editor: Has the *qui tam* plaintiffs' bar achieved its objective of narrowing or eliminating the public disclosure defense?

Hutt: Last year's FERA statute did not include any change in the public disclosure bar. However, the *qui tam* plaintiffs have now been partially successful in weakening the public disclosure bar as a result of the passage of the Patient Protection and Affordable Care Act (PPACA).

Some earlier proposals would have stripped defendants of the ability to raise the public disclosure defense at all. But PPACA as enacted did not strip defendants of their ability to raise the public disclosure defense, and they can probably raise this defense at any point during a proceeding as long as it is preserved as an affirmative defense. It can also be raised up front as a Rule 12(b)(6) defense. So at least defendants still have the ability to raise the public disclosure bar, even though the scope of the bar has been somewhat weakened.

Editor: Under PPACA the public disclosure defense is no longer labeled as jurisdictional. What is the effect of that?

Hutt: In the past the public disclosure defense was clearly labeled a jurisdictional defense, which meant in practice that defendants could often seek early targeted discovery of the issues on which plaintiffs based their cases. This meant that the jurisdictional issue could be resolved at the outset of the case. If defendants were successful in getting the case dismissed, they would not face expensive discovery into the merits of the *qui tam* lawsuit. Since under the new law the defense is no longer labeled as jurisdictional, it may be much harder in the future for defendants to get early targeted discovery into public disclosure issues.

Editor: PPACA provides that the court shall dismiss a case if there has been public disclosure unless "opposed by the Government." What is the intent of this provision?

Hutt: Under the prior version of the law, the Department of Justice did not have any say in the public disclosure question. It was up to the court alone to determine whether or not an action should be dismissed on public disclosure grounds. The new version of the law states that the Department of Justice has some sort of a veto over a defendant's motion to dismiss on public disclosure grounds, but the statute is not clear about what the phrase "opposed by the Government" means.

There are a variety of possibilities as to how courts are going to view this new language. One possibility is that courts will conclude that the government needs to provide a factual or a legal basis for its opposition. Some courts might conclude that a government opposition must be filed before a court has ruled on a public disclosure motion. Courts might even conclude that the Department of Justice has to formally intervene in a *qui tam* lawsuit before it can file an opposition.

But most important is the question of how the Department of Justice as a policy matter is going to decide when to oppose a public disclosure motion and when not to oppose a public disclosure motion. On the one hand, it might be passive and let the courts decide in most cases. On the other hand, it might be proactive and make explicit decisions about whether or not to file oppositions in most cases. Time will tell.

Editor: Under PPACA, public disclosures are narrowed to exclude disclosures made in state investigations, hearings, reports and audits as well as in private litigation.

Hutt: The prior statute was not entirely clear about whether disclosures made in a state investigation, hearing, report or audit should serve as a qualifying public disclosure, or if the disclosure had to be made in a federal proceeding. The Supreme Court answered that question very recently this year by deciding that such state proceedings qualified, in the *Graham County* case. But that decision is now moot because PPACA clearly changed the law to provide that disclosures made in state proceedings *do not* qualify as public disclosures.

Moreover, in the past, courts had found that disclosures made in private-party litigation could qualify as public disclosures. The new law changes the standard by excluding disclosures made in litigation, unless the federal government or its agent is a party. This is unquestionably a narrowing of the prior law.

The net effect of these changes is that

disclosures in state proceedings or private-party litigation will not trigger the public disclosure bar – unless of course they are also reported in the news media or in federal proceedings, in which case they will still qualify as triggering public disclosures.

Editor: Perhaps the provisions of greatest concern are the changes in the standard for a *qui tam* plaintiff qualifying as an original source.

Hutt: Before PPACA, *qui tam* plaintiffs had to have "direct and independent" knowledge of publicly disclosed allegations to qualify as original sources. The new law eliminates that requirement and replaces it with two possible tests. One test can be met where the plaintiff discloses the information to the government before the public disclosure is made. The second test can be met if the plaintiff had knowledge independent of the disclosure that "materially adds" to the disclosure and is provided to the government before the plaintiff files his or her lawsuit.

That second prong is a substantial problem because it permits *qui tam* plaintiffs to go forward after a public disclosure is made if they have some unclear additional amount of information. There is no definition of what quantum of information is necessary to satisfy the materiality test.

Nor is there any requirement that the plaintiff have direct knowledge of fraud. Before PPACA, the statute required both direct and independent knowledge. That's no longer required. Instead, a *qui tam* plaintiff can rely solely upon secondhand information that is heard around the water cooler. This runs directly contrary to the entire purpose of the public disclosure bar, which is to ensure that bounties are awarded only to true whistleblowers with firsthand knowledge of fraud.