

Investigating Allegations of Fraud: Questions to Ask When Evaluating Whether Cost Report Claims Breach the False Claims Act

IN NOVEMBER 1999, the Department of Justice (“DOJ”) announced its latest statistics regarding its enforcement of the False Claims Act (“FCA”), 31 U.S.C. § 3729 et seq.¹ Those statistics reveal that the United States has now recovered more than \$2.9 billion in actions that private persons (known as “relators”) have filed under the FCA (known as “qui tam” actions).² They also reveal that more than 60 percent of all qui tam actions are brought against those in the healthcare industry.³

Further, it does not appear that FCA recoveries will abate any time soon. For example, in January 2000, DOJ announced its blockbuster FCA settlement agreement with Fresenius Medical Care, the world’s largest provider of kidney dialysis products and services. Under the terms of the settlement, Fresenius agreed to pay a record-setting \$385 million to resolve claims under the FCA.⁴ Moreover, in February 2000, DOJ announced that nursing

home and home health operator Beverly Enterprises will pay a total of \$170 million to settle FCA allegations that it overbilled the Medicare program.⁵

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The DOJ’s statistics demonstrate its long-term commitment to enforce vigorously the FCA and its recent settlement announcements illustrating the potential liability providers can confront in FCA litigation underscore the importance to any entity of ensuring that its conduct does not run afoul of the FCA.

COST REPORT CERTIFICATIONS AND THE FCA

However, the line between conduct that breaches the FCA and that which is innocent is not always apparent. Moreover, discerning this line is especially difficult for healthcare entities that must submit a cost report. This is because these entities – hospitals, skilled nursing facilities, and home health agencies – must certify to the United States that to the best of their “knowledge and belief, th[e] [cost] report and statement are true, correct, complete and prepared from the books and records of the provider in accordance with applicable instructions, except as noted” and that the officer who signs the certification is “familiar with the laws and regulations regarding the provision of healthcare services, and that the services identified in its cost report were provided in compliance with such laws and regulations.”⁶

Given that the submitted cost report contains literally thousands of entries and the rules and regulations governing the Medicare program literally encompass several volumes of statutes, regulations, and policy statements, simple administrative violations may occur resulting in the submission of a “false” certification.

But those who stand accused are not defenseless. Instead, the government or the relator must, at a minimum, further prove that the provider “knew” that the claim was false – meaning it sought reimbursement for the claimed costs in reckless disregard or deliberate ignorance of the truth or falsity of the information.⁷ Thus, in assessing liability stemming from the submission of claims on a cost report, the analysis is not complete by simply determining that the claimed costs were inaccurate but must also include an analysis of why the costs were claimed in the first instance.

This article focuses on specific defenses that may arise when the provider’s certification is false because services reported in the cost report were not performed in compliance with the rules and regulations underlying the Medicare or Medicaid programs. Specifically, separate inquiries are set forth which, if followed, will assist the provider in gauging its potential exposure under the FCA.

FCA COST REPORT INQUIRIES

An inquiry into potential FCA liability must begin with an analysis of the provider's basis for claiming the challenged cost. As was noted above, the FCA does not generate liability unless the person acted in reckless disregard or deliberate ignorance of the truth or falsity of the claim. If a particular claim or cost is questioned, the provider should inquire into the following questions:

- ***Was reimbursement sought for the cost in accordance with regulatory guidance?*** – Compliance with the rules and regulations governing the Medicare and Medicaid programs is a dispositive defense to FCA liability.⁸ Thus, in recent actions, courts rejected relators' claims that defendants breached the FCA by failing to furnish the government the same discount provided to their best customers because, under the rules governing the pertinent government program, the companies were not obligated to bill the government at their best prices.⁹

Hence, when confronting an allegation that a cost report certification is false, defense counsel should carefully inspect the basis underlying the provider's claim and, if it is found that the entity complied with the applicable rules and regulations, then the government or relator will not be able to prove a violation of the FCA as a matter of law.

- ***Was the underlying regulatory guidance inherently ambiguous?*** – There may be occasions when defense counsel cannot establish that the challenged costs were compelled (or at least permitted) by the underlying regulatory guidance. However, if the defendant can prove that the regulatory guidance was inherently ambiguous, a court would be less likely to find that the entity "knowingly" submitted a false claim since more than one interpretation was possible.¹⁰ Thus, in one case, when the government contended that the applicable billing code (from the American Medical Association's Current Procedural Terminology ["CPT"]) required 45 to 50 minutes of "face-to-face" contact with the patient, while the defendant pointed out that the CPT itself was silent as to whether the time component included only "face-to-face" time or included all the time a physician worked on the session (including reviewing the chart, speaking with relatives, etc.). The court dismissed the government's claims because the regulatory instruction, the CPT, was "ambiguous."¹¹ Accordingly, when the government or relator asserts that the costs a provider claimed are false because they are not permitted by law, the provider should carefully evaluate whether the government's or relator's interpretation of the provision is valid or inherently ambiguous.

- ***Did the provider rely upon statements of government officials?*** – At times health care providers confer with government employees and agents prior to claiming costs on cost reports. Courts have ruled that when an entity engages in an open and active dialogue with the government regarding a billing practice, the government cannot establish a FCA violation as a matter of law because the entity can hardly be accused of acting with reckless disregard or deliberate ignorance of the truth or falsity of a claim when it informed the government of the underlying billing practice and sought advice.¹² Hence, in one case, a court ruled that although the defendant's contract had mandated that in providing paternity testing it conduct two tests and the company had in fact only

performed one test, the company was not liable because it had informed the government that it would only perform one test – a new DNA test that, unlike the type of test originally contemplated, did not scientifically require a second test to ensure accuracy.¹³ Under these circumstances, the government's knowledge undermined the relator's claim that the defendant acted with the requisite intent to violate the FCA. Accordingly, whenever a cost is questioned, a provider should determine the extent to which it had previously disclosed to or discussed with the government the questioned practice.

- ***Even if in hindsight the provider recognizes that it erroneously claimed the cost, did it have a plausible basis to claim the cost in the first instance such that its conduct is merely negligent?*** – There are occasions in which a person or an entity may be mistaken in claiming reimbursement for certain costs. However, Congress expressly provided that mere negligence was not actionable under the FCA.¹⁴ Thus, in instances in which the plaintiff's contention is simply that the defendant's business practices could have been more efficient or effective, or where an errant claim resulted from an honestly mistaken scientific calculation or other such judgment, the plaintiff cannot state a cause of action under the FCA.¹⁵

- ***Was the allegedly false claim material to the government's determination to pay?*** – Further, courts have ruled that when the defendant's representation is not capable of influencing the government's decision to pay funds, the government cannot establish a cause of action under the FCA. The issue of a non-material representation generally arises in one of two contexts: (1) when responsible government officials have reviewed or are cognizant of the underlying allegedly false material and, notwithstanding that notice, authorize payment;¹⁶ and (2) when responsible government officials are not aware of the underlying representations, but even if they had known that the representation was false, would have authorized payment because the falsity is unrelated to the government's decision to pay.¹⁷ Given this defense, providers should examine any allegedly false representation (especially those that are only technically false or concern relatively trivial matters) and assess whether the falsity of the information could have induced the government to pay; if not, then the provider has a defense to FCA liability.

CONCLUSION

As the use of the FCA continues to rise and the government and relators trot out novel theories of liability, it becomes increasingly essential that providers be prepared to inquire into the precise basis of their potential liability under the FCA. This inquiry is even more critical in the cost reporting context because the government, through its expansive certification, essentially obligates the provider to adhere to every rule and regulation underlying the payment of the providers' claims or face potential FCA liability. A carefully planned and executed internal review, considering the five basic questions discussed above, is a starting point for evaluating the extent to which potential FCA exposure may exist.

Notes

¹ The FCA is the government's "primary litigative tool for combating fraud." *United States ex rel. Kelly v. Boeing Co.*, 9 F.3d 743, 745 (9th Cir. 1993) (quoting Senate Judiciary Committee, False Claims Amendments Act of 1986, S. Rep. No. 345 (1986), reprinted in 1986 U.S.C.C.A.N 5266). It imposes liability on those who, *inter alia*, "knowingly" present, or cause to be presented, "a false or fraudulent claim for payment." 31 U.S.C. § 3729(a). Defendants found to have violated the FCA face paying treble damages plus a \$5,000 to \$10,000 penalty for each false claim submitted before September 29, 1999. *Id.* § 3729(a). For all violations committed on or after September 29, 1999, the defendant would be liable for treble damages plus penalties ranging from \$5,500 to \$11,000 per claim (see Civil Monetary Penalties Inflation Adjustment, 64 Fed. Reg. 47,099, 47,103-04 [1999] (to be codified at 28 C.F.R. pt. 85)).

² See <http://www.taf.org> (setting forth statistics regarding DOJ's recoveries); see also 31 U.S.C. § 3730. *Qui tam* "is an abbreviation for *qui tam pro domino rege quam pro seipso*, which means 'he who is as much for the king as for himself.'" *United States ex rel. Springfield Terminal Ry. v. Quinn*, 14 F.3d 645, 647 n.1 (D.C. Cir. 1994) (citation omitted). In bringing a *qui tam* action, a private person enforces the statute by filing a complaint, under seal, setting forth allegations of fraud committed against the government. 31 U.S.C. § 3730(b)(2). In *qui tam* actions, the United States may elect to intervene in the relator's action, and, if so, assumes primary responsibility for prosecuting the action. See *id.* §§ 3730(b)(4), (c)(1). If the United States intervenes in the relator's action, the relator receives, under most circumstances, 15 to 25 percent of the government's recovery (depending upon her contribution to the action) plus reimbursement of reasonable legal fees and related expenses. *Id.* § 3730(d)(1). However, if such a relator's action was based upon primarily public information, the relator's recovery would be capped at 10 percent. *Id.* Should the United States decline to intervene, the relator would receive 25 to 30 percent of the government's recovery, plus reimbursement of reasonable legal fees and related expenses. *Id.* § 3730(d)(2).

³ For the best compilation of FCA actions and settlements, see Taxpayers Against Fraud, *False Claims Act and Qui Tam Quarterly Review*, which is available on the internet at <http://www.taf.org>.

⁴ Fresenius also agreed to pay \$101 million in criminal fines. The relator in the FCA action received \$65.8 million. In a statement discussing the Fresenius settlement, June Gibbs Brown of OIG expressed her continued commitment to combating fraud and abuse aggressively:

This record \$486 million settlement is the culmination of five years of hard work by dedicated investigators, auditors and prosecutors. It is an excellent example of multiple law enforcement agencies working together on a long, complex Medicare fraud investigation. We are committed to working with our partners to investigate these complicated schemes, to hold the responsible parties accountable and to return ill-gotten gains to the Medicare Trust Fund.

Statement of June Gibbs Brown, Inspector General, U.S. Department of Health and Human Services, Settlement with Fresenius Medical Care (Jan. 19, 2000).

⁵ See <http://pubs.bna.com/ip/BNA/hce.nsf/id/a0a2u0h7j7>. Beverly Enterprises-California, Inc., a subsidiary, will plead guilty to mail fraud and false statement charges and pay a \$5 million criminal fine.

⁶ 42 C.F.R. § 413.24(f)(4)(iv). According to the government, the certification plays an important role in ensuring the integrity of the Medicare program. For example, in

its complaint against Columbia/HCA, the government noted that it receives for review more than 35,000 cost reports each year and that field audits are performed on only 5,000 cost reports (that is, 14 percent of all cost reports that are submitted). See United States' Complaint in *United States ex rel. Alderson v. Columbia/HCA*, No. 97-2035-CIV-T-23E (M.D. Fla. filed Feb. 2, 1999) ¶ 60. The government pointed out that because it "lacks adequate resources to conduct a full-scope [sic] audit of each of the over 35,000 providers nationwide," the "Medicare program depends heavily upon the truthfulness of providers in completing their cost reports." *Id.* ¶ 58.

⁷ 31 U.S.C. § 3729(a). To establish a violation of the FCA, the plaintiff must generally prove that the (a) "person," (b) "present[ed]" or "cause[d] to be presented," (c) "a false or fraudulent," (d) "claim," "record or statement," (e) "knowingly," (f) to "the United States Government," that was (g) "material" to the government's determination to pay. A detailed body of case law has developed construing each of these elements. See generally Robert Salcido, FALSE CLAIMS ACT AND THE HEALTHCARE INDUSTRY: COUNSELING AND LITIGATION, at Chapter 2 (1999) (setting forth an analysis of the case law applying each of these elements).

⁸ See *United States ex rel. Hochman v. Nackman*, 145 F.3d 1069, 1075 (9th Cir. 1998) (finding no falsity when defendants' acts conformed with the government's payment guidelines); *United States ex rel. Lindenthal v. General Dynamics Corp.*, 61 F.3d 1402, 1412 (9th Cir. 1995) (holding that whistleblower's FCA claims for payment based on work that satisfied contractual obligations "could not have been 'false or fraudulent' within the meaning of the [False Claims Act]"); *United States ex rel. Glass v. Medtronic, Inc.*, 957 F.2d 605, 608 (8th Cir. 1992) (concluding that a statement cannot be "false" or "fraudulent" under the FCA when the statement is consistent with Medicare's rules and regulations); *United States ex rel. LaCorte v. SmithKline Beecham Clinical Labs., Inc.*, No. 96-1380, 1999 U.S. Dist. LEXIS 13036 (E.D. La. Aug. 20, 1999) (same); *United States ex rel. Gathings v. Bruno's, Inc.*, 54 F. Supp.2d 1252 (M.D. Ala. 1999) (finding no falsity when defendants' practices conformed with Medicaid requirements); *United States ex rel. Cox v. Iowa Health Sys.*, 29 F. Supp.2d 1022, 1026 (S.D. Iowa 1998) (stating that where defendant engages in a "standard billing practice within an industry" and relator can point to "no controlling authority" which would require defendant to bill in a contrary fashion, the court "must dismiss th[e] action" because the relator "cannot pursue a FCA allegation without a legitimate false claim"); *United States ex rel. Joslin v. Community Home Health*, 984 F. Supp. 374, 379 (D. Md. 1997) (finding that where defendants' practices conformed with the law, "any representation to the Federal Government . . . is correct . . . and did not violate the FCA"); *United States ex rel. Milam v. Regents of the Univ. of Cal.*, 912 F. Supp. 868, 883 (D. Md. 1995) ("[A]s a matter of law, . . . False Claims Act liability cannot be imposed on the basis of a literally true statement."); cf. *United States ex rel. Gublo v. Novacare, Inc.*, 62 F. Supp.2d 347 (D. Mass. 1999).

⁹ See, e.g., *SmithKline Beecham Clinical Labs., Inc.*, 1999 U.S. Dist. LEXIS 13036, at *30-*32 (dismissing relator's allegation that defendant submitted false claims when it billed the government for a price higher than it billed its best customers because relator could not point to any "statute or regulation imposing the obligation it asserts defendant has breached" and the "statute does not state that providers must charge Medicare the lowest rate billed to anyone"). Similarly, in *Novacare*, relators alleged, in part, that defendant's claims were false on the grounds that it overstated its Medicare fee schedule because it did not reduce it by the amount of the discounts it furnished to substantial customers other than Medicare, thereby misrepresenting its "actual charge." *Novacare, Inc.*, 62 F. Supp.2d at 350 & n.5. The court dismissed relators' claims under Fed. R. Civ. P. 9(b) because "relators fail to point to any section of the regulations that requires [the defendant] to factor discounts given to

private insurers into the determination of its “actual charges” for government billing purposes.” *Id.* at 354-55.

¹⁰ See, e.g., *United States v. Data Translation, Inc.*, 984 F.2d 1256 (1st Cir. 1992) (finding that where supplier’s actions conformed with industry practice and were otherwise reasonable, the government could not state a cause of action under the FCA); *United States v. Napco Int’l, Inc.*, 835 F. Supp. 493, 498 (D. Minn. 1993) (declining to permit the Government to apply “an interpretative afterthought by the agency” against the contractor in a FCA action where underlying regulation was ambiguous); *United States v. Krizek*, 859 F. Supp. 5, 9-10 (D.D.C. 1994), *aff’d in part, rev’d in part*, 111 F.3d 934 (D.C. Cir. 1997).

¹¹ *Krizek*, 859 F. Supp. at 9-10. Specifically, the court noted:

The Court will not impose False Claims Act liability based on such a strained interpretation of the CPT codes. The government’s theory of liability is plainly unfair and unjustified. Medical doctors should be appropriately reimbursed for services legitimately provided. They should be given clear guidance as to what services are reimbursable. The system should be fair. The system cannot be so arbitrary, so perverse, as to subject a doctor whose annual income during the relevant period averaged between \$100,000 and \$120,000 dollars, to potential liability in excess of 80 million dollars

Id. at 10-11. However, while the court did not find the defendants guilty on this claim, the court nonetheless concluded that the defendants had violated the FCA by submitting an excessive – erroneous – number of claims to the government (because of inadequate office procedures, the defendant physician had billed, on occasion, for more than twenty hours of services within a twenty-four hour period). *Id.* at 12.

¹² See, e.g., *United States ex rel. Bennett v. Benetics & IVF Inst.*, No. 98-2119, 1999 U.S. App. LEXIS 27911 (4th Cir. Oct. 28, 1999); *United States ex rel. Durholz v. FKW, Inc.*, 189 F.3d 542, 545 (7th Cir. 1999) (“If the government knows and approves of the particulars of a claim for payment before that claim is presented, the presenter cannot be said to have knowingly presented a fraudulent or false claim. In such a case, the government’s knowledge effectively negates the fraud or falsity required by the FCA.”); *United States ex rel. Butler v. Hughes Helicopters, Inc.*, 71 F.3d 321 (9th Cir. 1995) (holding that where the contractor disclosed to the Army various nonconforming tests and the Army officials on site had approved of the tests, the government’s knowledge defeated any inference that the defendant “knowingly” presented false claims to the government); *Wang v. FMC Corp.*, 975 F.2d 1412, 1421 (9th Cir. 1992) (finding that where the government knew of the defendant’s “mistakes and limitations, and that [defendant] was open with the Government about them, suggests that while [defendant] might have been groping for solutions, it was not cheating the Government in its effort”).

¹³ *Bennett*, 1999 U.S. App. LEXIS 27911, at *7-9.

¹⁴ 132 CONG. REC. 20,536 (1986) (Congress settled upon the “reckless disregard” standard “to assure that mere negligence, mistake, and inadvertence are not actionable under the False Claims Act”) (statement of Sen. Grassley).

¹⁵ See, e.g., *United States ex rel. Hochman v. Nackman*, 145 F.3d 1069, 1074 (9th Cir. 1998) (finding that the “plaintiffs at best have shown only innocent mistake or mere negligence, neither of which can form the basis for False Claims Act liability”) (citations omitted); *Wang v. FMC Corp.*, 975 F.2d 1412, 1420-21 (9th Cir. 1992); *United States v. United Techs. Corp.*, 51 F. Supp.2d 167, 199 (D. Conn. 1999); *United States v. Raymond & Whitcomb Co.*, 53 F. Supp.2d 436, 448 (S.D.N.Y. 1999) (denying United States’ motion for summary judgment because defendant’s proof that it relied on the expertise of others in submitting its statements to the United

States established that a “reasonable fact finder could conclude that [defendant], in relying on [their] expertise . . . , acted unjustifiably and negligently, but not recklessly or in deliberate ignorance”). Similarly, in *United States ex rel. Rueter v. Sparks*, the relator alleged that the defendants had misrepresented his time and wages on certified payroll records because the defendants reported that the relator received \$18.00 per hour to perform his work operating heavy equipment when, for approximately one half hour per day, he received a rate of only \$8.00 per hour because for that half hour he performed maintenance work on that equipment. *Rueter*, 939 F. Supp. 636, 637-38 (C.D. Ill. 1996), *aff’d mem.*, 111 F.3d 133 (7th Cir. 1997). The district court concluded that, at most, the defendants were merely negligent in reporting the time and wages as required by Davis-Bacon and related statutes. *Id.* at 638. The court noted that the government, during previous audits, had never informed the defendants that their method of reporting time and wages was erroneous, and that the company did not receive guidance from the government on the proper method to report maintenance hours until several years after it had performed work on the government contract that was the subject of the lawsuit. *Id.* at 638-39. Moreover, in *Haynes v. United States through Food & Nutrition Serv.*, the district court ruled that the owner of a general store could not be held responsible for the acts of managers of the store (the owner’s mother and aunt) who improperly purchased food stamps because he had no knowledge that these persons had acquired, possessed, or redeemed illegally obtained food stamps. *Haynes*, 956 F. Supp. 1487, 1495-96 (E.D. Ark. 1995), *aff’d*, 106 F.3d 405 (8th Cir. 1997). The court rejected the government’s contention that the owner had “turned his back” to avoid learning of the misdeeds, ruling that at most the owner “could be said to have been negligent in failing to more closely monitor the store’s compliance with the Food Stamp Act since his name remained on the license despite his lack of further involvement in running the store. Nonetheless, any negligence on his part would not rise to the level of ‘reckless disregard.’ Given that the store is run by his mother and aunt, it is conceivable that [he] would not have felt the need to monitor the business as closely as he might otherwise have done.” *Id.*

¹⁶ See, e.g., *United States ex rel. Harrison v. Westinghouse Savannah River Corp.*, 176 F.3d 776 (4th Cir. 1999). In *Harrison*, the relator alleged that the defendant had submitted claims that were not authorized under the terms of its contract with the federal government, but the defendant pointed out that the government had a copy of the contract and could best judge whether its work was unauthorized. The court agreed with the defendant and dismissed the relator’s claim. Specifically, the court pointed out that the government “was aware of the terms of the contract – it could have objected to the inclusion of procedure development costs if it had believed that such work was not authorized. [The relator] does not allege that [the defendant] tried to conceal the nature of the work. Thus, [the relator’s allegations] do not involve any material falsity, if any falsity at all.” See also *United States ex rel. Lamers v. City of Green Bay*, 168 F.3d 1013, 1019 (7th Cir. 1999) (holding that even if defendant’s representation “was an outright lie,” the lie would be immaterial if defendant’s practices had conformed (unbeknownst to defendant) with the underlying regulation); *United States v. Robbins*, 207 F. Supp. 799, 807 (D. Kan. 1962) (finding that the government cannot charge that it was defrauded by the false representations of another party where it has made an independent investigation prior to paying any money to defendants); *United States v. Goldberg*, 158 F. Supp. 544, 548 (E.D. Pa. 1958) (same).

¹⁷ See, e.g., *United States ex rel. Berge v. Trustees of Univ. of Ala.*, 104 F.3d 1453, 1461-62 (4th Cir.) (rejecting the relator’s claim that the defendant had made false representations to the government to obtain federal grant funds by, among other things, identifying the relator as a post-doctoral graduate student when in fact she was a doctoral candidate because such a misrepresentation would not be material to the government’s decision of whether to fund a multimillion dollar grant since the government would be interested in the internationally respected scientists working on the project and not an unknown graduate student), *cert. denied*, 118 S. Ct. 301 (1997).