AN A.S. PRATT PUBLICATION
MARCH 2016
VOL. 2 • NO. 3

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Library of Congress Card Number:

ISBN: 978-1-6328-2705-0 (print)

Cite this publication as:

[author name], [article title], [vol. no.] PRATT'S GOVERNMENT CONTRACTING LAW REPORT [page number] (LexisNexis A.S. Pratt);
Michelle E. Litteken, GAO Holds NASA Exceeded Its Discretion in Protest of FSS Task Order, 1 PRATT'S GOVERNMENT CONTRACTING LAW REPORT 30 (LexisNexis A.S. Pratt)

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An A.S. Pratt® Publication

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(2016–Pub.4938)

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Understanding When an Overpayment Can Result in False Claims Liability and Why Current Court Precedent and Regulatory Guidance is Mistaken—Part I

By Robert S. Salcido*

One of the most vexing issues confronting any health care entity is the determination of when precisely it has a duty to disclose an "overpayment" to the government. In this two-part article, the author discusses the issue and why court precedent and regulatory guidance is mistaken. This first part discusses Congress' 2009 False Claims Act amendments. The second part of the article, which will appear in an upcoming issue of Pratt's Government Contracting Law Report, *will explain the Affordable Care Act amendments and relevant regulatory and case law developments.*

An issue every health care entity that submits claims to the government must frequently confront is when and how to disclose an overpayment to the government. This issue arises when, for example, an employee expresses concern about a claim or an internal audit or review questions a claim, or a Medicare Administrative Contractor inquires into a claim. Under amendments to the Affordable Care Act ("ACA"), if an overpayment is not reported to the government within 60 days, the entity could be held liable under the False Claims Act ("FCA") for treble damages and substantial civil penalties.[1]

Yet, notwithstanding the high stakes underlying the issue, one of the most vexing issues confronting any health care entity is the determination of when precisely it has a duty to disclose an "overpayment" to the government. There are at least two reasons for the lack of clarity. First, the limited regulatory guidance and case law that regulators and courts have promulgated are mistaken. They are demonstrably wrong, because they have used the FCA's general intent standard—defining knowledge, at a minimum, to be acting with "reckless disregard" or "deliberate ignorance"—when the FCA's provision governing the repayment of an overpayment requires the higher standard that

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[1] *See* Pub. L. No. 111-148, 124 Stat. 119 (2010).

the person act "knowingly and improperly."[2] Congress used the standard "knowingly and improperly" as a term of art, to proscribe conduct, as Congress described, that is "*malum in se*," or "inherently wrongful," or "willful" and where a person "employed means that are inherently tortious or illegal."[3] This is to be distinguished from the substantially lower FCA general constructive knowledge standard of "reckless disregard" and "deliberate ignorance." A person knowing that, in light of the evidence, the person's retention of governmental funds is "inherently wrongful" or "*malum in se*"—both in a legal and commonsensical manner—describes a vastly different circumstance than the person being merely recklessly disregardful or deliberately ignorant regarding whether the person possesses an overpayment. These different circumstances trigger different duties to investigate.

Second, because the government's guidance and court precedent have misconstrued the plain statutory language regarding what knowledge standard applies in determining whether there is an obligation to repay an overpayment, there is related confusion regarding when the overpayment is "identified." And, because there is a lack of clarity regarding when an overpayment is identified, there is correspondingly uncertainty regarding when the 60-day period is triggered to report the overpayment.

To adumbrate the root cause of the error in regulatory guidance and court precedent regarding the FCA overpayment provision, the relevant 2009 FCA statutory and legislative history will be chronicled. What this statutory review reveals, consistent with the express statutory language, is that Congress intended that the standard that courts use when assessing whether a health care entity breached its duty to report an overpayment, is whether, in light of the information the entity had, it would be inherently wrongful to not investigate further and not the lower standard of whether it would be recklessly disregardful or deliberately ignorant not to conduct an additional investigation.

CONGRESS' 2009 FCA AMENDMENTS

The legislative path that the FCA's overpayment provision traversed is important to study in detail, because it demonstrates Congress' resolve that a higher, more stringent standard governs FCA overpayments and that the duty to repay does not arise from contingent obligations, but from an "established duty" to repay a debt owed.

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[2] *Compare* 31 U.S.C. 3729(b)(1) *with* 31 U.S.C. § 3729(a)(1)(G).

[3] *See* 155 Cong. Rec. S4539–40 (2009); *see also* S. Rep. No. 111-10, at 15 (2009) (hereinafter S. Rep. 10), *reprinted in* 2009 U.S.C.C.A.N. 430, 442.

Senate Bill 386 to Amend the FCA

On February 5, 2009, Sens. Patrick Leahy (D-VT) and Chuck Grassley (R-IA) introduced S.386, a bill to improve the enforcement of mortgage, securities, and financial institution fraud and other frauds related to federal assistance and relief programs.[4]

The Senate bill proposed expanding the scope of the reverse false claims provision. Prior to 2009, the FCA lacked an express provision mandating the repayment of a known overpayment and, under the interpretation of a majority of courts, a person had an obligation to pay the government only when it submitted a false record or statement to the government that breached a fixed duty to pay an owed amount to the government. Under the 2009 amendments, Congress sought to enact two significant revisions to close this "loophole": (1) expand the provision so that it would apply to a knowing avoidance to repay an overpayment to the government, and (2) enlarge the provision to apply to merely contingent obligations. Specifically, Congress proposed the following revisions (proposed revisions to the FCA's existing provision in italics):

> (G) knowingly makes, uses, or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government, *or knowingly conceals, avoids, or decreases an obligation to pay or transmit money or property to the Government,*
>
> * * *
>
> (3) *the term 'obligation' means a fixed duty, or a contingent duty arising from an express or implied contractual, quasi-contractual, grantor-grantee, licensor-licensee, fee-based, or similar relationship, and the retention of any overpayment.*[5]

Thus, under the amendment, the provision would no longer require that a person submit an actual false record or statement, but could apply when a person simply received an overpayment, because the amendment would prohibit a person from "knowingly . . . avoid[ing] . . . an obligation to pay" and an obligation was defined to include the retention of any overpayment.

DOJ's February 24, 2009, Letter

Approximately three weeks after Sens. Leahy and Grassley proposed their bill, the Department of Justice, on February 24, 2009, wrote to Sen. Leahy to

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[4] *See* 155 Cong. Rec. S.1681 (Feb. 5, 2009).

[5] *Id*. at S. 1683–84.

recommend additional revisions to the bill.[6]

As to revisions to the reverse false claims provision, DOJ proposed the following amendment to the Senate's bill:

> (G) knowingly makes, uses, or causes to be made or used, a false record or statement *material* to ~~conceal, avoid, or decrease~~ an obligation to pay or transmit money or property to the Government, or knowingly conceals, *or improperly* avoids; or decreases, an obligation to pay or transmit money or property to the Government.

DOJ noted that the apparent purpose underlying the Senate bill's definition of "obligation" was to overrule cases that found that an obligation encompassed only duties that were "fixed in all particulars, including the specific amount owed."[7] However, DOJ also recognized that this amendment created the danger that those who merely sought to avoid or decrease an obligation to pay during an audit process may be subjected inappropriately to FCA liability. Specifically, DOJ noted:

> Section 4(a)(1) amends the FCA's reverse false claim provision to make the knowing concealment or avoidance of an obligation to pay a violation, and adds a definition of the term "obligation." The Department supports these changes . . . While the affirmative FCA provisions currently impose liability even in the absence of any false statement or record, there is no analogue in the reverse false claim context. Additionally, the new definition of obligation would address those cases that unduly narrowed the reverse false claim provision by holding or suggesting that the term "obligation" encompasses only a duty to pay that is fixed in all particulars, including the specific amount owed. *See, e.g.*, *American Textile Mfrs. Inst. v. The Limited, Inc.*, 190 F.3d 729 (6th Cir. 1999); *United States v. Q Int'l Courier, Inc.*, 131 F.3d 770 (8th Cir. 1997).
>
> Although the Department supports the Committee's efforts to revise and clarify the scope of the reverse false claim provision, the Department recommends . . . refinements to ensure that the provision reaches only a party's wrongful attempts to minimize the party's obligations to the Government. [T]he Department recommends inserting the words "or improperly" before the term "avoids" in the last clause of proposed

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[6] Letter from M. Faith Burton, Acting Assistant Attorney General, Department of Justice, to The Honorable Patrick J. Leahy, United States Senate, Committee on the Judiciary (Feb. 24, 2009) (hereinafter, "DOJ Letter").

[7] *Id.* at 2.

> subparagraph 3729(a)(l)(G), as follows: " . . . or knowingly conceals, or improperly avoids or decreases, an obligation to pay . . ."[8]

Senate Judiciary Committee Report (March 2009)

On March 5, 2009, the Senate Judiciary Committee issued its Report.[9]

As to amendments to the reverse false claims provision, the Committee proposed the following revisions to the amendment that DOJ proposed to create the "knowingly and improperly" standard:

> (G) knowingly makes, uses, or causes to be made or used, a false record or statement material to an obligation to pay or transmit money or property to the Government, or knowingly conceals, or *knowingly and* improperly avoids or decreases an obligation to pay or transmit money or property to the Government.

Further, the Committee proposed an additional revision to the definition of "obligation":

> (3) the term "obligation" means a fixed duty, or a contingent duty arising from an express or implied contractual, quasi-contractual, grantor-grantee, licensor-licensee, *statutory*, fee-based, or similar relationship, and the retention of any overpayment~~.~~;

When comparing the Senate's bill to the actual language in the FCA's reverse false claims provision, the bill reported out of the Committee proposed the following revisions:

> (7)G knowingly makes, uses, or causes to be made or used, a false record or statement *material* to ~~conceal, avoid, or decrease~~ an obligation to pay or transmit money or property to the Government, *or knowingly conceals or knowingly and improperly avoids or decreases an obligation to pay or transmit money or property to the Government,*

As drafted at this point, the Committee's provision would create liability in two situations: (1) when a person knowingly uses or causes to be used, "a false record or statement material" to an obligation to pay, or (2) when a person "knowingly conceals or knowingly and improperly avoids or decreases" an obligation to pay.

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[8] *Id*. For a detailed history of the FCA's reverse false claims provision and a description of its case law, *see* Robert Salcido, FALSE CLAIMS ACT & HEALTHCARE INDUSTRY: COUNSELING & LITIGATION §§ 1:05; 2:03 (American Health Lawyers Ass'n Supp. 2014); *see generally* Robert Salcido, FALSE CLAIMS ACT & HEALTH CARE INDUSTRY: COUNSELING & LITIGATION (2d ed. American Health Lawyers Ass'n 2008).

[9] S.Rep. 10, at 4, *reprinted in* 2009 U.S.C.C.A.N., at 433.

Also, at this point, it appears that the Committee envisioned that the reverse false claims provision would apply to merely contingent obligations, such as the creation of false statements to avoid the payment of tariffs:

> Further, this legislation addresses current confusion among courts that have developed conflicting definitions of the term "obligation" in Section 3729(a)(7). The term "obligation" is now defined under new Section 3729(b)(3) and includes fixed and contingent duties owed to the Government—including fixed liquidated obligations such as judgments, and fixed, unliquidated obligations such as tariffs on imported goods. It is also noteworthy to restate that while the new definition of "obligation" expressly includes contingent, non-fixed obligations, the Committee supports the position of the Department of Justice that current section 3729(a)(7) "speaks of an 'obligation,' not a 'fixed obligation." By including contingent obligations such as "implied contractual, quasi-contractual, grantor-grantee, licensor-licensee, fee-based, or similar relationship," this new section reflects the Committee's view, held since the passage of the 1986 Amendments, that an "obligation" arises across the spectrum of possibilities from the fixed amount debt obligation where all particulars are defined to the instance where there is a relationship between the Government and a person that "results in a duty to pay the Government money, whether or not the amount owed is yet fixed."[10]

Finally, the Committee addressed the balance that it intended to strike by inserting the prohibition against the "retention of an overpayment" in the statute. Specifically, the Committee noted that it simply intended to capture instances where a person knowingly used estimates to retain governmental funds to which the person was not entitled, but not capture instances like hospital cost reports, where an entity may receive overpayments (or underpayments) as a natural byproduct of the regulatory scheme:

> The new definition of "obligation" includes an express statement that an obligation under the FCA includes "the retention of an overpayment." The Department of Justice supported the inclusion of this provision and provided technical advice that the proper place to include overpayments was in the definition of obligation. This new definition will be useful to prevent Government contractors and others who receive money from the Government incrementally based upon cost estimates from retaining any Government money that is overpaid during the estimate process. Thus, the violation of the FCA for

[10] S.Rep. 10 at 14, *reprinted in* 2009 U.S.C.C.A.N., at 441–42 (footnote omitted).

> receiving an overpayment may occur once an overpayment is knowingly and improperly retained, without notice to the Government about the overpayment. The Committee also recognizes that there are various statutory and regulatory schemes in Federal contracting that allow for the reconciliation of cost reports that may permit an unknowing, unintentional retention of an overpayment. The Committee does not intend this language to create liability for a simple retention of an overpayment that is permitted by a statutory or regulatory process for reconciliation, provided the receipt of the overpayment *is not based upon any willful act* of a recipient to increase the payments from the Government when the recipient is not entitled to such Government money or property. Moreover, *any action or scheme created to intentionally defraud the Government* by receiving overpayments, even if within the statutory or regulatory window for reconciliation, is not intended to be protected by this provision. Accordingly, *any knowing and improper retention of an overpayment* beyond or following the final submission of payment as required by statute or regulation—including relevant statutory or regulatory periods designated to reconcile cost reports, but excluding administrative and judicial appeals—would be actionable under this provision.[11]

April 22, 2009, Floor Statements

On April 22, 2009, on the Senate floor, Senator Jon Kyl (R-AZ) proposed significant revisions to the Committee's definition of "obligation." The Senate agreed to Senator Kyl's amendments, and those amendments were ultimately adopted into law unchanged. Specifically, Senator Kyl proposed the following revision to the definition:

> (3) the term "obligation" means ~~a fixed~~ *an established* duty, *whether* or ~~a~~ ~~contingent duty~~ *not fixed,* arising from an express or implied ~~contractual, quasi-~~contractual, grantor-grantee, *or* licensor-licensee~~,~~ ~~statutory,~~*relationship, from a* fee-based, or similar relationship, ~~and~~ *from statute or regulation or from* the retention of *any* overpayment.[12]

As to the purpose underlying these proposed revisions, Senator Kyl pointed out that the definition of obligation previously proposed was too broad, because it would include "contingent" obligations, such as a duty to pay a fine upon the commission of some transgression. If the statute were expanded in that fashion,

[11] S.Rep. 10 at 15, *reprinted in* 2009 U.S.C.C.A.N., at 442 (footnote omitted) (emphasis supplied).

[12] 155 Cong. Rec. S.4539.

as Senator Kyl pointed out, a person conceivably could be held liable to pay treble damages for a fine before the duty to pay the fine was established. Thus, he proposed to strike the words "contingent duty" and that the language "established duty" be inserted in its place. By revising the statutory language in this fashion, Senator Kyl believed that the reverse false claims provision would not be inappropriately expanded to reach contingent obligations like duties to pay penalties or fines:

> The bill's new definition of the word "obligation," in particular, posed several problems. The original language spoke of "contingent" obligations. Such contingent or potential duties could include duties to pay penalties or fines, which could arise—and at least become "contingent" obligations—as soon as the conduct that is the basis for the fine has occurred.
>
> Obviously, we don't want the Government or anyone else suing under the False Claims Act to treble and enforce a fine before the duty to pay that fine has been formally established. It is unlikely that Justice would ever have brought suit to enforce a claim of this nature, but the FCA can also be enforced by private relators who often may be motivated by personal gain and not always exercise the same good judgment that the Government usually does.
>
> To preclude such a reading of the act, my amendment strikes contingent obligations from the FCA's new definition of "obligation."[13]

Also consistent with the limited scope of the provision, Senator Kyl reiterated prior governmental statements that "overpayments" would be a source of obligation only when a defendant "knowingly and improperly" retains an overpayment. Specifically, Senator Kyl clarified that this standard applied only when defendant's conduct was "*malum in se,*" or inherently wrongful, and does not apply when the defendant is "pursuing in good-faith the exhaustion of a reconciliation procedure":

> I might also say a few words about aspects of the definition of obligation that I ultimately concluded that it was not necessary to address in this amendment. At the Judiciary Committee's mark up of this bill, I circulated an amendment that would limit obligations arising out the retention of any overpayment so as to make clear that no obligation arises if the defendant is pursuing some type of administrative, judicial, or other process for reconciliation of alleged

[13] *Id.* (emphasis supplied).

overpayments. The sponsors of the bill raised the concern, however, that such a safe harbor might immunize parties that intentionally and maliciously obtain an overpayment, and then spend years exhausting a reconciliation process, all in bad faith and knowing full well that they must repay the money, but earning interest on the overpayment in the interim. Apparently incidents like this have occurred, in cases involving sums that allowed the defendant to earn tens of millions of dollars in interest. The sponsors of the bill also noted to me that, under subparagraph (G)'s modification of the reverse False Claims Act, avoiding or decreasing an obligation is only actionable, in relevant part, if the defendant "knowingly and improperly avoids or decreases an obligation to pay or transmit money or property to the Government." Therefore, a good-faith pursuit of a reconciliation process would not be actionable.

I asked my staff to research the meaning of "knowingly and improperly" to confirm that a person who pursues reconciliation of an overpayment in good faith could not be held liable under the reverse False Claims Act. The answer that I received is that the term "knowingly and improperly," though infrequently used in the case law, is consistently construed to mean that a person either acted with bad intent or that he employed means that are inherently tortious or illegal.

. . . In the False Claims Act context, this list may include other *improper means, but "improper means" must be means that are malum in se—that is, means that are inherently wrongful and constitute an independent tort.*

* * *

Given that the words "knowingly and improperly" have a fixed meaning that, at the very least, requires either improper motives or inherently improper means, the changes made by this bill cannot be read to make actionable the retention of an overpayment when the defendant is pursuing in good faith the exhaustion of a reconciliation procedure. It is with this understanding that I have declined to insist on further qualification of the bill's predication of liability on the retention of an overpayment.[14]

Thus, significantly, Congress' precise intent, as reflected in the plain language it employed, the "knowingly and improperly" standard—rather than to use the FCA's general knowledge standard, reckless disregard and deliberate

[14] *Id.* at S4539–40.

ignorance—was to ensure that the FCA would *never* be used unless the plaintiff established that the person's conduct in retaining an overpayment was "*malum in se*," or "inherently wrongful," or "willful" and where a person "employed means that are inherently tortious or illegal."[15] Moreover, in another clause of the reverse FCA provision, although Congress initially intended to expand the reverse FCA provision to reach contingent obligations, ultimately, Congress struck that language to mandate that the provision would apply only to established duties.

* * *

The second part of this article will appear in an upcoming issue of *Pratt's Government Contracting Law Report*.

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[15] *See* 155 Cong. Rec. S4539–40 (2009); *see also* S. Rep. 10 at 15, *reprinted in* 2009 U.S.C.C.A.N., at 442.