

CLIENT ALERT

Supreme Court Addresses Limits on “Implied Certification” Theory Under The False Claims Act: *Universal Health Services, Inc. v. U.S. ex. rel Escobar*

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In a much-anticipated decision, the U.S. Supreme Court held in *Universal Health Services, Inc. v. United States ex rel. Escobar* that the “implied false certification” theory of liability “can, in at least some circumstances, provide a basis for” False Claims Act (“FCA”) liability, but identified the Act’s materiality requirement as a substantive limit on the scope of such liability. The decision is important for all industries that participate in federal programs or receive federal money, and replaces a geographic patchwork of precedents with a uniform substantive standard for this significant theory of liability and associated treble damages and civil penalties.

Under the implied false certification theory, when a provider submits a claim to the government, it impliedly certifies that it has complied with all contracts, statutes, and regulations material to the provision of the goods or services for which it seeks payment. If that claim fails to disclose a violation of such conditions, the provider has made a misrepresentation that renders the claim “false or fraudulent” under the FCA. In a unanimous decision authored by Justice Clarence Thomas, the Court held that the implied certification theory of falsity can provide a basis for liability where (i) the claim at issue does not merely request payment, but also makes specific representations about the goods or services provided; and (ii) the defendant’s failure to disclose noncompliance with material statutory, regulatory, or contractual requirements makes those representations “misleading.”

In reaching this conclusion the Court rejected the argument that a claim can be legally “false” under the implied certification theory only where the implied term is an express condition of government payment. And it likewise rejected the position that every requirement expressly designated as a payment condition is necessarily material for FCA purposes. The Court held that liability does not turn on labels, and that the controlling question is one of substantive materiality—an FCA requirement that the Court characterized as “demanding.” The Court emphasized that although the Government’s label of a provision as a condition of payment is “relevant” to the materiality inquiry, it is not “automatically dispositive.” The Court’s opinion thus provides important guidance on the materiality requirement and its role in limiting FCA liability.

Background

In *Escobar*, two private individuals—known as relators—brought a *qui tam* action against Universal Health Services, Inc., the operator of a mental health clinic in Massachusetts whose unlicensed staff prescribed medication that

caused their teenage daughter's death. Relators alleged that the clinic's violation of state licensing and supervision requirements rendered all of its Medicaid reimbursement claims false under the FCA. The Government declined to intervene, and the district court dismissed the complaint for failure to plead falsity because Universal Health's compliance with state regulations was not an express "precondition of payment" for Medicaid claims.

The First Circuit reversed and accepted the implied certification theory of falsity, stating that although the record was silent on whether Universal Health "explicitly represented that it was in compliance with conditions of payment when it sought reimbursement," the First Circuit has "not required such 'express certification' in order to state a claim under the FCA." The court further noted that each time Universal Health submitted a claim, it was "implicitly communic[ating] that it had conformed to the relevant program requirements, such that it was entitled to payment."

The Supreme Court granted certiorari to resolve a circuit split on two questions: (i) whether the implied certification theory of legal falsity is viable under the FCA; and (ii) if so, whether that theory applies where a claim can be legally "false" under that theory if the statute, regulation, or contractual provision at issue did not expressly state that compliance is a condition of payment.

The Court's Decision

A. The Court Accepts the Implied False Certification Theory of FCA Liability

The Court first considered the threshold viability of the implied false certification theory, which some circuits had rejected as incompatible with the FCA.

In doing so the Court cautioned that it "need not resolve whether all claims for payment implicitly represent that the billing party is legally entitled to payment," because the claims at issue "do more than merely demand payment." The Court then explained that by submitting claims for payment using payment codes corresponding to specific counseling services, Universal Health represented that it had in fact provided such services. In addition, the claims included National Provider Identification numbers for specific job titles of the clinic's staff, when those staff members were not qualified to hold the positions associated with the identification numbers. The Court concluded that in this context—by using payment and other codes that conveyed this information without disclosing the many violations of relevant staff and licensing requirements—"Universal Health's claims constituted misrepresentations."

Based on this analysis the Court held that "the implied certification theory can be a basis for liability, at least where two conditions are satisfied: first, the claim does not merely request payment, but also makes specific representations about the goods or services provided; and second, the defendant's failure to disclose noncompliance with material statutory, regulatory, or contractual requirements makes those representations misleading half-truths."

B. The FCA's "Demanding" Materiality Requirement Limits the Scope of Implied Certification Liability

The Court then addressed the question of whether implied certification liability turns on whether the implicit certification of compliance concerns a requirement that the Government has *expressly* designated a condition of payment. The Court held that implied certification liability does not turn on such labels one way or the other. The Court stated that a defendant can be liable for violating requirements even if they were not expressly designated as conditions of payment, and, conversely, that not every violation of a requirement that is expressly designated a condition of payment will trigger liability. "What matters is not the label the Government attaches to a requirement, but whether the defendant knowingly violated a requirement that the defendant knows is material to the Government's payment decision." In so holding, the Court focused on strict enforcement of the False Claims Act's "rigorous" materiality and scienter requirements as a means of addressing concerns about "open-ended liability." The Court then provided guidance as to how the materiality requirement should be enforced.

The Court started by defining a "material" misrepresentation or omission as one as "having a natural tendency to influence, or be capable of influencing, the payment of receipt of money or property." The Court reemphasized that this "materiality standard is demanding" because the FCA is "not an all-purpose antifraud statute . . . or a vehicle for

punishing garden-variety breaches of contract or regulatory violations” or for “imposing treble damages and other penalties for insignificant regulatory or contractual violations.”

The Court then provided examples for evaluating materiality under the FCA. In doing so the Court observed that proof of materiality could include facts showing that a defendant knew the government consistently refused to pay claims based on noncompliance with the specific statute, regulation or contract requirement at issue. Conversely, the Court emphasized that the Government’s payment of a claim despite a known violation would be “strong evidence” that the violation was not “material” for FCA purposes, just as materiality should not be found where noncompliance with the requirement at issue “is minor or insubstantial.”

In reaching these conclusions the Court rejected the Government’s and First Circuit’s “extraordinarily expansive” view that any statutory, regulatory, or contractual violation is material so long as the defendant knows the Government would be “entitled to refuse payment were it aware of the violation.” The Court also expressly rejected the “assertion that materiality is too fact intensive for courts to dismiss False Claims Act cases on a motion to dismiss or at summary judgment.” The Court thus vacated the First Circuit’s decision and remanded the case for further proceedings consistent with its opinion.

Conclusion

Although the Supreme Court accepted the viability of the more expansive implied false certification theory, it imposed meaningful limits on its scope by focusing on the facts of the claims at issue and emphasizing the “demanding” and “rigorous” nature of the FCA’s materiality requirement. In so doing and rejecting the First Circuit’s “extraordinarily expansive” view of materiality, the Court resolved deep geographic division over a critical legal standard and provided needed substantive and procedural guidance on the proper application of that standard going forward.

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