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# 7th Circ. Rejects FCA Implied False Certification Theory

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On June 8, 2015, the U.S. Court of Appeals for the Seventh Circuit rejected the doctrine of implied false certification in a False Claims Act lawsuit, U.S.ex rel. Nelson v. Sanford-Brown Ltd. In a welcome decision for government contractors, the court held that the FCA is "not the proper mechanism" for government enforcement of regulations. Instead, regulatory violations should be handled by the appropriate government agency — not the courts.

Under the implied false certification doctrine, an invoice submitted to the government impliedly certifies compliance with applicable laws, regulations and contract terms. A number of circuits, including the Fourth, Ninth, Tenth and D.C. Circuits, have adopted the implied false certification theory. In Sanford-Brown, however, the Seventh Circuit rejected the theory and more clearly differentiated a breach of contract from the submission of a false claim.

Qui tam relator Brent Nelson was the previous director of education at Sanford-Brown College, a for-profit educational institution in Wisconsin. He alleged that Sanford-Brown and its corporate parent defrauded the government by receiving federal subsidies even though it was violating the Higher Education Act and the program participation agreement it had signed with the U.S. secretary of education. The PPA, per federal law, conditioned the initial and continuing participation of Sanford-Brown's Title IV subsidies on compliance with statutory, regulatory and contractual requirements. Nelson claimed that the college's recruiting and retention practices had violated these conditions and, thus, resulted in the submission of thousands of false claims. As the FCA allows for trebled damages and a statutory penalty of up to $11,000 per violation, defendants were facing hundreds of millions of dollars in liability.

The United States declined to intervene in the case, and many of the relator's claims were dismissed due to the public disclosure bar or the first-to-file rule. Ultimately, the district court granted defendants' motion for summary judgment, rejecting the implied false certification theory. Nelson appealed to the Seventh Circuit, challenging, among other issues, the district court's rejection of implied false certification.

A party that "knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval" violates the FCA.[1] Nelson, therefore, needed to show: (1) a false or fraudulent claim; (2) that

defendants presented or caused to be present for payment; (3) with knowledge the claim was false.

The United States, though it had declined to intervene, filed an amicus brief supporting the relator and arguing that a violation of the program participation agreement caused Sanford-Brown to present false claims, because compliance with the agreement was a condition of payment. The Seventh Circuit found the relator and the government's position to be "untenable" and lacking a "discerning limiting principle:"

[W]e conclude that it would be … unreasonable for us to hold that an institution's continued compliance with the thousands of pages of federal statutes and regulations incorporated by reference into the PPA are conditions of payment for purposes of liability under the FCA …The FCA is simply not the proper mechanism for government to enforce violations of conditions of participation contained in — or incorporated by reference into — a PPA.

The court emphasized the distinction between a mere breach of contract, which is not cognizable under the FCA, and entering into the contract in bad faith from the outset. A promise of future performance does not become false due to subsequent noncompliance. The court declined to join the circuits that adopted the doctrine of implied false certification, and instead declared that it was joining the Fifth Circuit in rejecting the theory.

The Seventh Circuit cited the Fifth Circuit's decision in U.S. ex rel.Steury v. Cardinal Health Inc., which held that "a false certification of compliance, without more, does not give rise to a false claim for payment unless payment is conditioned on compliance."[2] Interestingly, in a follow-up decision, the Fifth Circuit distanced itself from this statement and proclaimed that this decision, cited by the Seventh Circuit, "did not reject the implied false certification theory of FCA liability."[3] Instead, the Fifth Circuit noted that while it has "not definitively ruled on the cognizability of implied false certification claims," it has accepted that certifications must be a prerequisite of payment. So, while the Fifth Circuit has not adopted the implied false certification theory, it has not clearly rejected it either (despite the Seventh Circuit's claims to the contrary).

The Seventh Circuit's ruling makes clear that it was the U.S. Department of Education's role to enforce the PPA through the administrative mechanisms provided by its regulations. Noncompliance with federal regulations, therefore, does not trigger FCA liability in the Seventh Circuit, unless there is proof that the original agreement was entered into fraudulently.

By deepening the circuit split on the theory of implied false certification, the Seventh Circuit introduced further complexity into FCA jurisprudence. Government contractors now have varying degrees of FCA exposure, depending on their location. As it currently stands, nine circuits have accepted implied false certification to some degree: the First, Second, Third, Fourth, Sixth, Eighth, Ninth, Tenth, Eleventh, and D.C. Circuit.[4] These circuits differ, however, on the breadth and scope of the theory. The Second Circuit, for instance, limits the theory's application to when the underlying statute or regulation expressly requires the defendant's compliance for payment.[5]

The Fourth Circuit, on the other hand, adopted a broad approach: A plaintiff "pleads a false claim when it alleges that the contractor, with the requisite scienter, made a request for payment under a contract and withheld information about its noncompliance with material contractual requirements.'"[6] The D.C. Circuit adopted a similarly unrestrained interpretation.[7] Remarkably, both circuits recognized that such an expansive implied false certification theory "is prone to abuse" by parties that may bring minor contractual violations as FCA actions. According to the Fourth Circuit, to avoid overzealous plaintiffs

from trying to “shoehorn” breach of contract claims into FCA lawsuits, the courts will have to ensure “strict enforcement of the Act’s materiality and scienter requirements.” This will provide little comfort for government contractors. Providing judicial enforcement of complex legal concepts will unlikely deter relators from bringing breach of contract claims as FCA suits. This is particularly true because applying a broad implied false certification theory, many unmeritorious FCA claims may be able to survive the motion to dismiss stage. Summary judgment may prove to be an effective gatekeeper. However, the costs and risks of defending a breach of contract claim under the guise of an FCA claim are not insignificant, and may push many contractors to settle, regardless of the merits.

Contractors in the Seventh Circuit now enjoy a narrowed scope of potential FCA liability. Regulatory compliance is to be evaluated and adjudicated by the appropriate agency and not by the courts. The Seventh Circuit’s ruling will protect contractors from opportunistic relators who may allege that mere breaches of implied certifications with respect to the myriad statutes and regulations affecting government contracts amount to false claims. In other circuits, however, contractors may face a limited implied false certification theory, such as in the Second Circuit, or an expansive doctrine only limited by judicial enforcement of scienter and materiality.

Particularly for contractors with a national presence, the circuit split creates varying levels of legal liability, depending on where lawsuits are brought. The Seventh Circuit’s decision runs against the tide of circuits adopting variations of the implied false certification theory. Its rejection may be enough to pique the U.S. Supreme Court’s interest in resolving the issue in a uniform manner nationwide. But, until then, contractors face uncertain liabilities for common conduct that are dependent on the jurisdiction in which suit is brought. Given the great risks involved in FCA litigation, this kind of jurisdiction dependent liability makes no sense.

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[1] 31 U.S.C. § 3729(a)(1)(A).

[2] 625 F.3d 262, 269 (5th Cir. 2010).

[3] United States ex rel. Steury v. Cardinal Health, Incorp., 735 F.3d 202, 206 (5th Cir. 2013).

[4] See, e.g., United States ex rel. Badr v. Triple Canopy Inc., 775 F.3d 628, 636 (4th Cir. 2015); United States ex rel. Vigil v. Nelnet Inc., 639 F.3d 791, 799-800 (8th Cir. 2011); United States ex rel. Hutcheson v. Blackstone Med., Inc., 647 F.3d 377, 387-88 (1st Cir. 2011); United States ex rel. Wilkins v. United Health Grp. Inc., 659 F.3d 295, 306 (3d Cir. 2011); Ebeid ex rel. United States v. Lungwitz, 616 F.3d 993, 996 (9th Cir. 2010); United States v. Sci. Applications Int'l Corp., 626 F.3d 1257, 1269 (D.C. Cir. 2010); United States ex rel. Conner v. Salina Reg'l Health Ctr. Inc., 543 F.3d 1211, 1217 (10th Cir. 2008); McNutt ex rel. United States v. Haleyville Med. Supplies Inc., 423 F.3d 1256, 1259 (11th Cir.2005); United States ex rel. Augustine v. Century Health Servs. Inc., 289 F.3d 409, 415 (6th Cir. 2002); Mikes v. Straus, 274 F.3d 687, 700 (2d Cir. 2001).

[5] Mikes v. Straus, 274 F.3d 687, 700 (2d Cir. 2001).

[6] United States ex rel. Badr v. Triple Canopy Inc., 775 F.3d 628, 636 (4th Cir. 2015).

[7] United States v. Sci. Applications Int'l Corp., 626 F.3d 1257, 1266 (D.C. Cir. 2010).