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SECOND CIRCUIT FALLS IN LINE FOR FCA PLEADING REQUIREMENTS

On September 7, 2017, the Second Circuit realigned its stance on false certifications under the False Claims Act ("FCA") in light of the Supreme Court's decisions in *Universal Health Services, Inc. v. United States ex rel. Escobar*, 136 S.Ct. 1989, 195 L.Ed.2d 348 (2016).

BACKGROUND

In the initial action, relators brought a *qui tam* action under the FCA against Wells Fargo alleging the company falsely certified its compliance with banking laws in order to borrow money at favorable rates from the Federal Reserve System.[1] In *Bishop v. Wells Fargo & Co.*, 823 F.3d 35 (2nd Cir. 2016), the Second Circuit relied on its previous holding in *Mikes v. Straus*, 274 F.3d 687 (2nd Cir. 2001) in upholding the district court's dismissal of the relator's complaint.[2] The court's rationale for dismissing the complaint rested on two separate points: (1) an implied false certification is appropriately applied only when the underlying statute or regulation relied upon by the relator expressly states the provider must comply in order to be paid; and (2) an expressly false claim is a claim that falsely certifies compliance with a particular statute.[3] The Supreme Court granted certiorari, vacated and remanded the matter back to the Second Circuit in light of its opinion in *Escobar*.[4]

ANALYSIS

The Supreme Court's holding in *Escobar* nullifies the Second Circuit's holding in *Mikes*. In *Escobar*, the Supreme Court held that "a statement that misleadingly omits critical facts is a misrepresentation irrespective of whether the other party has expressly signaled the importance of the qualifying information.[5] This directly contradicts the Second Circuit's holding that an express statement of compliance must be included in the underlying statute or regulation.

The Supreme Court also indicated that limitations on liability under the FCA must be grounded in the text of the FCA, including the well-settled meaning of common-law terms the FCA uses but does not expressly define.[6] In vacating the previous holding, the Second Circuit stated "we detect no textual support in the FCA for *Mikes's* particularity requirement."[7] The Second Circuit also acknowledged that the *Escobar* holding addressed *Mikes's* particularity requirement in other ways.[8] Specifically, *Escobar* states, "Instead of adopting a circumscribed view of what it means for a claim to be false or fraudulent, concerns about fair notice and open-ended liability can be effectively addressed through strict enforcement of the FCA's materiality and scienter requirements."[9]

The Supreme Court's holding in *Escobar* not only nullified the Second Circuit's holding in *Mikes*, it created a new standard.[10] The Supreme Court stated, "A misrepresentation about compliance with statutory, regulatory, or contractual requirement must be material to the Government's payment decision in order to be actionable under the FCA."[11] The Supreme Court further refined this standard stating, "materiality…cannot be found where noncompliance is minor or insubstantial."[12] Perhaps most significantly, the Supreme Court noted, "…if the Government pays a particular claim in full despite its actual knowledge that certain requirements were violated, that is very strong evidence that those requirements are not material."[13]

PRACTICAL TAKEAWAYS

The Supreme Court's new "materiality" standard in *Escobar* replaces the Second Circuit's previous holding in *Mikes*. The practical effect of *Escobar*'s holding requires that *qui tam* actions brought on the basis of a false certification, whether expressed or implied, must be material to the government's decision to pay a provider. However, if a provider can show that the government made a payment knowing that a provider was violating certain requirements, those requirements may not be considered material.

If you have any questions, please contact:

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[1] Bishop v. Wells Fargo & Co., 870 F.3d 104, 106 (2nd Cir. 2017).

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[2] *Id.*

[3] *Id.*

[4] *Id.*

[5] *Universal Health Services, Inc. v. United States ex rel. Escobar*, 136 S.Ct. 1989, 2001 (2016).

[6] *Id.* at 1999.

[7] *Wells Fargo & Co.*, 870 F.3d at 107.

[8] *Id.*

[9] *Escobar*, 136 S.Ct. at 2002.

[10] *Id.* at 2004.

[11] *Id.* at 2002.

[12] *Id.* at 2003.

[13] *Id.*

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