9th Circ. Adds to Growing Consensus on Escobar FCA Test

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The U.S. Supreme Court's 2016 decision in *Universal Health Services Inc. v. United States ex rel. Escobar*[1] settled the key question of whether there can be liability for implied false certifications under the False Claims Act – there can – but left some big, open questions in its wake. The court held that when "a defendant makes representations in submitting a claim but omits its violations of statutory, regulatory, or contractual requirements, those omissions can be a basis for liability if they render the defendant's representations misleading with respect to the goods or services provided."[2] But precisely when such omissions can be the basis for liability was not clearly resolved and has generated numerous conflicting opinions.

The Ninth Circuit's recent opinion in *United States ex rel. Rose v. Stephens Institute*[3] is the latest decision addressing this issue and solidifies the emerging view that the only way to prove implied false certification liability is by specifically showing the two prerequisites mentioned in *Escobar*: (1) specific representations about the goods or services provided and (2) failure to disclose noncompliance with material statutory, regulatory or contractual requirements that renders those specific representations misleading or false. The Supreme Court stated implied false certification liability can attach "at least where" these two conditions are met, but, because the allegations in *Escobar* included "specific representations," explicitly declined to address whether every claim implicitly represents that the claimant is in compliance with all applicable legal requirements. Since then, courts have split over whether establishing both conditions is necessary for a viable implied false certification claim.

Though Stephens Institute held that the two-part test laid out in *Escobar* is mandatory, the Ninth Circuit panel came to its ruling with some apprehension, signaling that whether the Supreme Court's opinion requires this result is anything but fully resolved in the circuit courts. However, the issue appears to be headed in the right direction.

The Ninth Circuit's Decision

In *Stephens Institute*, the relators alleged defendant Stephens Institute established enrollment goals for each admissions representative and adjusted salaries based on the representative's success or failure in enrolling that number of students. Stephens Institute receives federal funding under Title IV of the Higher Education Act, provided they comply with various statutory,

regulatory, and contractual requirements, including the incentive compensation ban. That ban prohibits schools from offering or paying incentive compensation for recruiting or enrolling a higher number of students.[4] At issue before the Ninth Circuit was the relators' contention that the Institute's failure to disclose its noncompliance with the ban was sufficient to render claims false under an implied false certification theory of FCA liability.

In the Aug. 24, 2018, *Stephens Institute* decision, the Ninth Circuit concluded the government or relator must satisfy the two-part test identified in *Escobar* for implied false certification liability to attach. In *Escobar*, the Supreme Court held this theory can be a basis for FCA 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."[5] Since *Escobar*, the question has been whether this means both conditions must be satisfied or whether an FCA claim based on implied false certification can proceed without a specific representation.

The Ninth Circuit came to its holding in *Stephens Institute* with great reluctance. Under pre-*Escobar* Ninth Circuit precedent, *Ebeid ex rel. U.S. v. Lungwitz*, a relator "could show falsity by pointing to noncompliance with a law, rule, or regulation that is necessarily implicated in a defendant's claim for payment."[6] In other words, no specific representation was necessary.

Though no panel had overruled *Ebeid*, the Ninth Circuit believed it was bound by two of their own post-*Escobar* cases that treated *Escobar*'s two conditions as mandatory. The first, *United States ex rel. Kelly v. Serco Inc.*,[7] analyzed falsity under *Escobar*'s two-part test only and did not consider the lower *Ebeid* standard. The second, *United States ex rel. Campie v. Gilead Sciences Inc.*,[8] stated that *Escobar*'s two conditions must be satisfied. While the *Stephens Institute* court "doubt[ed] that the Supreme Court's decision would require us to overrule *Ebeid*," it ultimately held that a plaintiff "must satisfy *Escobar*'s two conditions to prove falsity, unless and until our court, en banc, interprets *Escobar* differently."[9]

How *Stephens Institute* Stacks Up to Other Appellate Decisions

Through *Stephens Institute* and its other recent decisions, the Ninth Circuit joined the First and Seventh Circuits in holding that liability under an implied false certification theory requires satisfying *Escobar*'s two-part test. The Seventh Circuit, in *United States v. Sanford-Brown Ltd.*,[10] held that implied false certification liability requires specific representations. That circuit had affirmed summary judgment for the defendant on the relator's false presentment claim, but the Supreme Court remanded the case back to the circuit after issuing its decision in *Escobar*. The Seventh Circuit again affirmed after finding the relator failed to establish the defendant made any specific representations in connection with its claims for payment. Accordingly, the relator did not show that "the defendant's failure to disclose noncompliance with material statutory, regulatory, or contractual requirements ma[de] those representations misleading half-truths."[11] Since *Sanford-Brown*, district courts in the Seventh Circuit have followed suit in requiring both a specific representation and noncompliance that makes it a misleading half-truth.[12]

The First Circuit has not been as explicit on this issue, but the court in *United States ex rel. Nargol v. DePuy Orthopaedics Inc.*,[13] went out of its way to expressly discuss the existence of specific representations as a basis for potential FCA liability in an implied false certification context. The relators in that case alleged the defendant distributed a defectively manufactured product to health care providers, who then sought government reimbursement. The district court granted a motion to dismiss, and on appeal, the First Circuit specifically noted "[t]he district court observed that the complaint allege[d] no 'specific representations.'"[14] In vacating the district court's dismissal with respect to those alleged claims, the First Circuit found there was a "plain specific representation" that "the device was the Pinnacle MoM device, an FDA-approved product, rather than a defectively manufactured, nonconforming variant"[15] — thereby highlighting the importance of specific representations in implied false certification cases.

In contrast, the Fourth Circuit held in *United States ex rel. Badr v. Triple Canopy Inc.*[16] that a "misleading half-truth" consistent with that in *Escobar* could establish implied false certification liability even in the absence of a clear, specific representation. Even after *Escobar*, the Fourth Circuit concluded that its prior rulings that "the government pleads a false claim when it alleges a 'request for payment under a contract' where the contractor 'withheld information about its noncompliance with material contractual requirements'"[17] was still good law. Two D.C. district court cases similarly held that "the D.C. Circuit's broader statement of the implied certification theory remains good law after *Escobar*,"[18] but no other courts of appeals have joined the Fourth Circuit.

The Ninth Circuit's holding in *Stephens Institute* reflects momentum in favor of the two-part mandatory test. Yet, the *Stephens Institute* court came to its decision through fidelity to precedent, not through conviction that its interpretation of *Escobar* was correct. The court noted *Escobar* "did not state that its two conditions were the only way to establish liability under an implied false certification theory" and invited the full Ninth Circuit to evaluate *Escobar*'s falsity test anew.

Requiring Specific Representations Keeps This Theory Faithful to the Purposes of the FCA

This growing consensus that the two conditions outlined in *Escobar* are a minimum floor for liability under an implied false certification theory is consistent with the scope and purposes of the FCA. As the Supreme Court has cautioned, the FCA "is not an all-purpose antifraud statute, or a vehicle for punishing garden-variety breaches of contract or regulatory violations."[19] Requiring falsity be rooted in affirmative lies by a defendant helps keep FCA liability tethered to combating the submission of fraudulent claims. Indeed, the court pointed to the FCA's stringent materiality and scienter requirements as a means of addressing concerns about fair notice and open-ended liability, and limiting implied false certification liability to cases involving specific representations further helps to ensure this theory of liability does not impermissibly expand the scope of the FCA.

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

[2] Id. at 1999.

[3] *United States ex rel. Rose v. Stephens Institute* , --- F.3d ----, No. 17-15111 (9th Cir. Aug. 24, 2018).

[4] See 20 U.S.C. § 1094(a)(20); 34 C.F.R. § 668.14(b)(22).

[5] *Escobar*, 136 S. Ct. at 2001.

[6] *Ebeid ex rel. U.S. v. Lungwitz* , 616 F.3d 993, 998 (9th Cir. 2010).

[7] *United States ex rel. Kelly v. Serco Inc.* , 846 F.3d 325, 332 (9th Cir. 2017).

[8] *United States ex rel. Campie v. Gilead Sciences Inc.* , 862 F.3d 890, 901 (9th Cir. 2010).

[9] *Stephens Institute*, --- F.3d ----, No. 17-15111, at 12.

[10] *United States v. Sanford-Brown Ltd.* , 840 F.3d 445, 447 (7th Cir. 2016).

[11] Id.

[12] *U.S. ex rel. Lisitza v. Par Pharm. Cos., Inc.* , 276 F. Supp. 3d 779, 794 (N.D. Ill. 2017).

[13] *United States ex rel. Nargol v. DePuy Orthopaedics Inc.* , 865 F.3d 29 (1st Cir. 2017).

[14] Id. at 37.

[15] Id.

[16] *United States ex rel. Badr v. Triple Canopy Inc.* , 857 F.3d 174 (4th Cir. 2017).

[17] Id. at 178 n.3.

[18] *United States v. DynCorp Int'l LLC* , No. 16-1473, 2017 WL 2222911, at *100 (D.D.C. May 19, 2017); accord *United States ex rel. Landis v. Tailwind Sports Corp.* , No. 10-cv-00976, 2017 WL 573470 (D.D.C. Feb. 13, 2017).

[19] *Escobar*, 136 S. Ct. at 2003.

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