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THE PAST, PRESENT, AND FUTURE OF “MATERIALITY” UNDER THE FALSE CLAIMS ACT

JOHN T. BOESE*

“Words calculated to catch everyone may catch no one.”

—Adlai E. Stevenson II¹

“The United States is a nation of laws: badly written and randomly enforced.”

—Frank Zappa²

I. INTRODUCTION

One of the most important debates in the jurisprudence of the civil False Claims Act (“FCA”)³ has always been the question of materiality as a necessary element for liability under the FCA.⁴ The questions have traditionally revolved around:

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1. Adlai E. Stevenson, Welcome Address to the 1952 Democratic National Convention (July 21, 2952), in 4 *THE PAPERS OF ADLAI E. STEVENSON* 11, 13 (Walter Johnson et al. eds., 1974).

2. ANTONIO SANTI, *THE BOOK OF ITALIAN WISDOM* 168 (2003).

3. 31 U.S.C. §§ 3729-33 (2006).

4. See 31 U.S.C. § 3729(a)(1)-(2) (2006) (creating liability for “[a]ny person who—(1) knowingly presents, or causes to be presented, to an officer or employee of the United States Government . . . a false or fraudulent claim for payment or approval [or] (2) knowingly makes, uses, or cause to be made or used, a false record or statement to get a false or fraudulent claim paid or approved by the Government”). See also *United States v. Bourseau*, 531 F.3d 1159, 1170-71 (9th Cir. 2008), *cert. denied*, 129 S. Ct. 1524 (2009) (holding that FCA includes a materiality element); *United States ex rel. A+ Homecare, Inc. v. Medshares Mgmt.*

- Whether materiality was an essential element for FCA liability.
- If so, how “materiality” would be defined.
- However defined, how courts would apply this element.

The reason this question is so critical is that materiality is the difference between innocence and guilt under this quasi-criminal statute.⁵ Materiality is not an issue in the run-of-the-mill FCA case. A hospital that bills Medicare for a “phantom” patient it has never treated is liable under the FCA and materiality is never considered an issue.⁶ A doctor who treats a Medicare patient and then codes the treatment at a higher reimbursement level is liable under the FCA and materiality is either irrelevant or, more properly, assumed.⁷ The issue of materiality is never litigated in these cases because, under these facts, the violation is obvious—the defendant has billed the government for services that it has not provided. This is the essence of a “false claim.”

Materiality is a critical determination, however, for cases based on what some courts call “legally false” claims.⁸ (These courts refer to the situations described in the paragraph above as “factually false” claims.⁹) Other courts refer to these as “false certification” cases because some express or implied certification of compliance has been violated.¹⁰ In a case based on a “legally false” claim, or in a “false certification” case, the defendant has provided the goods or services to the government or government beneficiary for the agreed upon price.¹¹ For example, a hospital has provided medically necessary services to a Medicare eligible beneficiary and billed the government the proper amount; a defense contractor has provided a

Group, Inc., 400 F.3d 428, 441-42 (6th Cir. 2005) (concluding that false statements or conduct must be material to the claim in order to hold a violator liable under the FCA); *Mikes v. Straus*, 274 F.3d 687, 697 (2d Cir. 2001) (declining to address whether the FCA requires a materiality element); *United States ex rel. Berge v. Board of Tr. of Univ. of Ala.*, 104 F.3d 1453, 1459, 1460 (4th Cir. 1997), *cert. denied*, 118 S. Ct. 301 (1997) (stating whether FCA requires a materiality element is a question for the court); Megan L. Hoffman, Comment, *The Substantial Weight Test: A Proposal to Resolve the Circuits’ Disparate Interpretations of Materiality Under the False Claims Act*, 58 U. KAN. L. REV. 181, 190 (2009).

5. See *Medshares Mgmt.*, 400 F.3d at 443 (“[L]iability does not arise from merely making a false statement, but rather from making a false statement to conceal, avoid, or decrease an obligation owed to the Government. A false statement can only avoid or decrease an obligation if that statement is material to the money or property owed to the Government.”).

6. *United States ex rel. Conner v. Salina Reg’l Health Ctr. Inc.*, 543 F.3d 1211, 1217 (10th Cir. 2008); *Mikes*, 274 F.3d at 697.

7. *Conner*, 543 F.3d at 1217; *Mikes*, 274 F.3d at 697.

8. *Conner*, 543 F.3d at 1217; *Mikes*, 274 F.3d at 697.

9. *Conner*, 543 F.3d at 1217; *Mikes*, 274 F.3d at 697.

10. See *Conner*, 543 F.3d at 1217-18 (discussing express and implied false certification).

11. *Id.*

part that meets all specifications and billed the government for the contract price; a university has spent federal grant money for the purposes set forth in the grant.

But—and there is always a “but” in these cases—the hospital, contractor or grantee has violated some other regulation, statute, contract, or grant term in the course of delivering that service, producing that article, or performing the grant. In the case of the hospital, one or more conditions of participation may have been violated in the course of delivering the necessary services to the eligible beneficiary.¹² The contractor may have violated a discrimination law in hiring workers for its plant, which the contract prohibited. In the case of the grantee, an ancillary term of the grant may have required full compliance with environmental laws, and even though the grantee performed the work funded by the grant, it otherwise was not in full compliance with these laws.

In every FCA case of this nature, the question arises: Do these factually true claims become legally false because of the violation of ancillary legal requirements? Does the fact that an express (or implied) certification of legal compliance occurred make an otherwise true claim for money become false? The answer has, in most cases, depended on the application and definition of the requirement of materiality. More simply, are the ancillary violations material to the government’s decision to pay the claim? If the answer is yes, assuming the necessary knowledge or intent requirement has been met, the claim is false and the defendant is liable under the FCA. If no, the claim is not false and the defendant is not liable.

The history and development of materiality under the FCA is a fascinating case study in statutory construction. Academics and federal judges have waxed eloquent on whether materiality is required and what it means.¹³ To practicing lawyers and their clients, however, this is not an idle

12. *Id.* at 1220. *See also Mikes*, 274 F.3d at 697 (stating the most common form of a false claim is for goods or services not rendered or provided in violation of contract terms, specification, statute, or regulation).

13. *See United States v. Bourseau*, 531 F.3d 1159, 1170 (9th Cir. 2008) (discussing that while the FCA text does not contain a materiality requirement, legislative history indicates it was Congress’ intent for one to be incorporated); *United States ex rel. A+ Homecare, Inc. v. Medshares Mgmt. Group, Inc.*, 400 F.3d 428, 442-43 (6th Cir. 2005) (“[U]nder the rule that Congress intends to incorporate the well-settled meaning of the common-law terms it uses, we cannot infer from the absence of an express reference to materiality that Congress intended to drop that element from the fraud statutes” (quoting *Neder v. United States*, 527 U.S. 1, 23 (1999)); *Mikes*, 274 F.3d at 697 (discussing that a materiality requirement meant that only a portion of admittedly false claims would be subject to FCA liability); *United States ex rel. Berge v. Board of Tr. of Univ. of Ala.*, 104 F.3d 1453, 1459 (4th Cir. 1997) (“[W]e now make explicit that the current civil False Claims Act imposes a materiality requirement.”); *see also Hoffman*, *supra* note 4, at 190 (discussing that circuit courts have found materiality a

question for law professors and judges. Any provider, contractor, or grantee dealing with the federal government is subject to such an overwhelming regime of laws, rules, regulations, and guidelines that full compliance is impossible. For such entities, should they become the defendant in an FCA case, materiality is one of two key issues (the other being intent) that renders an otherwise innocent defendant liable under the FCA.¹⁴ Materiality is a theoretical concept with devastating real-world ramifications—treble damages and per-claim civil penalties under the FCA—even though the services or goods were delivered as promised.¹⁵

The stakes were raised on May 20, 2009, when the FCA was amended to make materiality an explicit requirement for liability and to establish a definition of the term,¹⁶ resolving a circuit split that had developed since the 1986 amendments.¹⁷ In every crucial liability provision, the term “material” was added.¹⁸ Thus, 31 U.S.C. § 3729(a)(1)(B) was amended to require that the knowingly false statement be “material to a false or fraudulent claim.”¹⁹ In addition, the reverse false claim provision was amended to require that the false record or statement be “material to an obligation to pay or transmit money or property to the Government.”²⁰ The term was then defined in the manner espoused by the Department of Justice (“DOJ”).²¹ New Section

requirement of 31 U.S.C. § 3729(a), even though Congress did not make it an express requirement under the statute).

14. *Medshares Mgmt.*, 400 F.3d at 443.

15. *Bourseau*, 531 F.3d at 1173.

16. The Fraud Enforcement and Recovery Act of 2009 (FERA), Pub. L. No. 111-21, § 4(a)(1), 123 Stat. 1617, 1623 (2009) (to be codified at 31 U.S.C. § 3729(a)(1)(B)).

17. See *Bourseau*, 531 F.3d at 1170-71 (discussing that the First, Fourth, Fifth, Sixth, Eighth and Ninth circuits hold that the FCA includes a materiality element, yet each is still split on how to measure materiality); *Medshares Mgmt.*, 400 F.3d at 445 (stating that the circuits that have addressed materiality are inconsistent on its standard to be applied); Hoffman, *supra* note 4, at 197-98 (discussing that the Fourth, Sixth, Ninth, and Tenth circuits have applied the natural tendency test, which states “that a false statement is material if it has ‘a natural tendency to influence, or is capable of influencing, the decision of the decisionmaking body to which it was addressed’” (quoting *Neder v. United States*, 527 U.S. 1, 16 (internal quotations omitted))), while the Second and Eighth circuits have applied the outcome determinate test, which “requires a showing that the alleged fraudulent actions had the purpose and effect of causing the United States to pay out money it is not obligated to pay, or those actions which intentionally deprive the United States of money it is lawfully due” (quoting *Medshares Mgmt. Group*, 400 F.3d at 446) (internal quotations and citations omitted)).

18. FERA § 4(a), 123 Stat. at 1621-23.

19. FERA § 4(a)(1), 123 Stat. at 1621.

20. FERA § 4(a)(1), 123 Stat. at 1622 (to be codified at 31 U.S.C. § 3729 (a)(1)(G)).

21. Brief for United States as Amicus Curiae Supporting Plaintiff at 10, *United States ex rel. Heath v. Dallas/Fort Worth Int’l Airport Bd.*, No. 3:99-CV-0100-M, 2004 WL 1197483 (N.D. Tex. May 28, 2004) [hereinafter *Heath Brief*] (arguing for the adoption of the “capable

3729(b)(4) provides that "the term 'material' means having a natural tendency to influence, or be capable of influencing, the payment or receipt of money or property."²²

Even though materiality is now clearly a requirement with a definition provided, what has really changed with the 2009 amendments? What do the phrases "having a natural tendency to influence" and "be capable of influencing" really mean? How much more vulnerable are FCA defendants under these amendments? The key to the future, as always, lies in the past. This history demonstrates how the warnings from the elegant Mr. Stevenson and the irrepressible Mr. Zappa, quoted above, can apply to FCA enforcement.

II. HISTORY OF MATERIALITY UNDER THE FALSE CLAIMS ACT

A. *Materiality Before the 1986 Amendments*

Prior to the 1986 amendments, although the concept of materiality existed under the FCA, there were few FCA cases expressly discussing it.²³ The concept of materiality has its roots in *United States v. McNinch*, where the Supreme Court stated that the FCA is "not designed to reach every kind of fraud practiced on the Government."²⁴ Prior to the expansion of *qui tam* enforcement in 1986,²⁵ most FCA cases brought by the government were factually false claims.²⁶ The concept that a claim could be false because of the violation of an ancillary law, regulation, contract, or grant term was not unknown, but FCA enforcement on this theory was quite rare.²⁷

In most pre-1986 amendment cases, the concept of materiality was more properly raised as a question of reliance or causation—terms commonly used interchangeably. For example, in *Woodbury v. United States*²⁸ and *United States v. Hibbs*,²⁹ the courts required the Government's

of influencing" test); JOHN T. BOESE, CIVIL FALSE CLAIMS AND QUI TAM ACTIONS 2-186 (3d ed. Supp. 2010-1).

22. FERA § 4(a)(2), 123 Stat. at 1623.

23. See, e.g., *United States v. McNinch*, 356 U.S. 595 (1958); *United States v. Thomas*, 709 F.2d 968, 972 (5th Cir. 1983); *United States v. Miller*, 645 F.2d. 473, 475 (5th Cir. 1981); *United States v. Hibbs*, 568 F.2d 347, 350 (3d Cir. 1977).

24. *McNinch*, 356 U.S. at 599.

25. False Claims Amendments Act of 1986, Pub. L. No. 99-562, § 3, 100 Stat. 3153, 3155-57 (codified at 31 U.S.C. § 3730(c)-(g) (2006)).

26. See *Hibbs*, 568 F.2d at 351 (discussing that defendant submitted false certifications to the FHA); *McNinch*, 356 U.S. at 597 (discussing government's claim that defendant caused a bank to submit false applications for insurance to the FHA); *Woodbury v. United States*, 232 F. Supp. 49, 52 (1964) (discussing government's claim that plaintiff's contracts and applications for payment were false).

27. *Woodbury*, 232 F. Supp. at 55-56.

28. *Id.* at 55.

reliance on the false statement or certification. In those cases (both involving FCA cases based on criminal convictions), the courts analyzed reliance and causation as an element of damages—the false certification had to cause the damages sought by the government.³⁰ This analysis can also be found in other pre-1986 cases, such as *United States v. Miller*,³¹ and *United States v. Thomas*.³² One of the most well-known false certification cases decided before 1986 was *United States ex rel. Weinberger v. Equifax, Inc.*³³ In *Weinberger*, a *qui tam* relator claimed that the defendant submitted false claims to the government because the defendant, while providing services to the government, had violated the Anti-Pinkerton Act.³⁴ The court first explained that the purpose of the FCA was primarily to deal with factually false claims:

The False Claims Act “was not designed to reach every kind of fraud practiced on the Government.” *United States v. McNinch*, 356 U.S. 595, 599, 78 S.Ct. 950, 2 L.Ed.2d 1001 (1958). The statute is primarily directed against government contractors’ billing for nonexistent or worthless goods or charging exorbitant prices for delivered goods. *Id.* Equifax plainly did not submit a false claim under this reading of the statute: no one has suggested that Equifax’s reporting activities for the government were not properly carried out. *Weinberger* has alleged no false claim in this sense.³⁵

The court went on to discuss what other courts would later describe as legally false claims or false certification cases:

The statute also interdicts material misrepresentations made to qualify for government privileges or services. See, e. g., *Alperstein v. United States*, 291 F.2d 455, 456 (5th Cir. 1961) (per curiam) (veteran violated False Claims Act when, to qualify for federal benefits, he falsely swore that he was financially unable to bear medical expenses); *United States v. Johnson*, 138 F.Supp. 525, 52728 (W.D.Okla.1956) (physician misrepresented competency and general qualifications to gain employment with Air Force). The principal thrust of *Weinberger*’s allegations fall into this category: that Equifax misrepresented its qualification for government employment and thus made a false claim. But to establish that Equifax committed fraud in this manner, *Weinberger* first must demonstrate that the government was misled by Equifax’s application for the reporting business. Unless the government made it clear that it would not employ detective agencies when it contracted for the work, Equifax’s application did not make a material

29. *Hibbs*, 568 F.2d at 350.

30. *Id.* at 350; *Woodbury*, 232 F. Supp. at 55.

31. *United States v. Miller*, 645 F.2d 473, 475 (5th Cir. 1981).

32. *United States v. Thomas*, 709 F.2d 968, 972 (5th Cir. 1983).

33. *United States ex rel. Weinberger v. Equifax, Inc.*, 557 F.2d 456 (5th Cir. 1977).

34. *Id.* at 458.

35. *Id.* at 460.

misrepresentation, did not mislead the government, and did not defraud the government within the meaning of the False Claims Act . . . In this case the False Claims Act is not an enforcement device for the AntiPinkerton Act. Weinberger has failed to allege a claim under the False Claims Act.³⁶

Post-1986 concepts of materiality can be traced directly to this decision.

B. "Materiality" After the 1986 Amendments

The rarity of legally false or false certification cases and the debate over materiality changed in 1986, when FCA enforcement was transferred from virtually exclusive control of the DOJ to a shared enforcement with private attorneys representing *qui tam* relators.³⁷ While the DOJ has the option to control all FCA cases, it intervenes and takes control in only about twenty percent of the cases (where over ninety-five percent of the recoveries occur).³⁸ The other eighty percent of FCA cases are uninvolved cases litigated by *qui tam* relators without DOJ control.³⁹ The materiality issue arose after 1986, mostly in these uninvolved cases.⁴⁰ These were the legally false cases, where the goods and necessary services were delivered to the government and eligible government beneficiaries at the prices agreed to, but some other ancillary violation allegedly occurred, and the *qui tam* relator alleged that the claim became false by reason of this violation.⁴¹

Why would these legally false or false certification cases rise so dramatically with the increase in *qui tam* enforcement? The answer lies in the different motivations for DOJ enforcement of the FCA and *qui tam* enforcement of the FCA. DOJ attorneys (along with those in the U.S. Attorneys' Offices) are primarily law enforcement officials. Their motivation is to root out fraud on the U.S. Treasury, and they have a broader policy goal.⁴² The DOJ and its client agencies must balance FCA enforcement with the government's responsibility for serving the citizens. As a result, DOJ's primary focus is on factually false cases: that is where the true fraud

36. *Id.* at 461.

37. False Claims Amendments Act of 1986, Pub. L. No. 99-562, § 3, 100 Stat. 3153, 3155 (codified at 31 U.S.C. § 3730(c)(3) (2006)).

38. See BOESE, *supra* note 21, at H-7 app (As of September 30, 2009, the U.S. has intervened in 1,266 cases out of a total 6,628 cases.).

39. *Id.*

40. *Id.* at 2-167.

41. United States *ex rel.* Thompson v. Columbia/HCA Healthcare Corp., 125 F.3d 899, 902 (5th Cir. 1997).

42. See generally BOESE, *supra* note 21, at 1-11 (discussing the ruling of United States v. Griswold, 24 F. 361 (D. OR. 1885), "that while the government might release a *qui tam* defendant from the damages owed it under the Act it could not release the defendant from damages due the informer," the U.S. Treasury).

occurs.⁴³ A *qui tam* lawyer, on the other hand, is primarily interested in the greatest financial recovery for his or her individual client. While *qui tam* lawyers prefer factually false *qui tam* cases because they are easier to prove, the private relator and counsel are interested in a recovery, and a legally false FCA case, which is far easier to allege, is better than no FCA case at all. For this reason, the *qui tam* relator counsel is much more likely to push the envelope on materiality issues than the DOJ attorney. They have nothing to lose.

In these unintervened cases, the question commonly arose: When does the ancillary violation make an otherwise true claim become false? In virtually all of these cases the DOJ did not intervene, but only appeared as an amicus, or friend of the court.⁴⁴

C. *The Initial DOJ Position: Materiality Is Not a Requirement for FCA Liability*

Despite the clear holding in *Weinberger*, the DOJ position in virtually every amicus brief after 1986 was that materiality was not a requirement for FCA liability.⁴⁵ While the DOJ agreed that there was “something” that differentiated inconsequential violations from important violations, the government consistently denied the requirement for materiality.⁴⁶ Perhaps the best discussion of the government position is in the panel decision in *United States v. Southland Management Corporation*.⁴⁷ The discussion by both the panel majority and the dissent (which is one of the best-written FCA

43. See Brief for United States as Amicus Curiae Supporting Defendants-Appellees at 1, *Mikes v. Straus*, 274 F.3d 687 (2d Cir. 2001) (No. 00-6269) (stating that knowingly billing the government for services not provided is a “garden-variety” FCA violation). See also BOESE, *supra* note 21, at 2-167 (“Prior to 1986, when the FCA was enforced almost entirely by the Justice Department, most FCA complaints relied on what may be referred to as ‘traditional’ fraud—claims for substandard products, claims based on timecard mischarging, claims in contracts procured by bribery, etc . . . After 1986, when FCA enforcement was significantly expanded to affirmatively encourage enforcement by private parties, *qui tam* relators (and to a lesser extent the now-expanded Justice Department) began pushing the application of the FCA beyond the more traditional areas of enforcement. In this new era, FCA cases began to be based on allegations that claims to the government contained ‘certifications’ (either express or implied) of compliance with other laws, regulations, guidelines, or standards.”).

44. Brief for United States as Amicus Curiae Supporting Plaintiffs-Appellants, *United States ex rel. Burlbaw v. Orenduff*, 548 F.3d 931 (10th Cir. 2008) (No. 60-2006, 05-2393); Heath Brief, *supra* note 21; Brief for United States as Amicus Curiae Supporting Plaintiff-Appellant, *United States ex rel. Thompson v. Columbia/HCA Healthcare Corp.*, 125 F.3d 899 (5th Cir. 1996) (No. 96-40868) [hereinafter *Thompson Brief*].

45. Heath Brief, *supra* note 21, at 3; *Thompson Brief*, *supra* note 44, at 10.

46. *United States v. Southland Mgmt. Corp.*, 288 F.3d 665, 677, 678 (5th Cir. 2002).

47. *Id.*

opinions ever) refers to the DOJ position on materiality as unsustainable.⁴⁸ The dissenting judge, Judge Edith Jones, stated that "the precise definition of materiality remains open to question in this court based on a government theory never before accepted by a federal court."⁴⁹ Judge Jones later stated that "the government's proffered test of 'claim materiality' is ingenious but wrong."⁵⁰

D. *The "Prerequisite for Payment" Test of Materiality*

According to the dissent in *Southland*, and a number of other federal courts, the issue was quite simple: Were the false certifications a prerequisite to government payment?⁵¹ Although some courts did not call this a test for materiality, it was a requirement for liability. The best example of this is *United States ex rel. Mikes v. Strauss*, where the court was faced with a claim by the *qui tam* relator (the DOJ declined to intervene) that a healthcare provider had submitted false claims under the theory that services provided to eligible beneficiaries were "false" because the device used was not properly calibrated.⁵² In its famous decision, the Second Circuit held:

We join the Fourth, Fifth, Ninth, and District of Columbia Circuits in ruling that a claim under the Act is legally false only where a party certifies compliance with a statute or regulation as a condition to governmental payment.⁵³

Essentially, these courts held that only certifications which actually affected payment could harm the treasury and, because the FCA was founded upon harm to the Federal Treasury, a false statement that did not harm the Federal Treasury could not constitute a violation of the FCA.

E. *The DOJ Acceptance and Redefinition of "Materiality"*

The decision in *Mikes* was a wake-up call for the DOJ. By continuing to argue that materiality was not a required element of the FCA, the DOJ was losing the ability to define what was required under the FCA. A few cases,

48. *Id.* at 678, 692.

49. *Id.* at 692. The *Southland* case became a virtual embarrassment for DOJ. After the panel decision in favor of the government was released, the defendants were granted reconsideration *en banc*. *United States v. Southland Mgmt. Corp.*, 307 F.3d 352 (5th Cir. 2002). In the decision that followed, the court of appeals unanimously (including the two panel judges who favored the government) reversed the panel decision and rejected liability. *United States v. Southland Mgmt Corp.*, 326 F.3d 669, 677 (5th Cir. 2003) (*en banc*).

50. *Southland*, 288 F.3d at 693.

51. *See, e.g., id.* at 694; *Mikes v. Straus*, 274 F.3d 687, 698 (2d Cir. 2001); *Luckey v. Baxter Healthcare Corp.*, 183 F.3d 730, 732-33 (7th Cir. 1999); *United States ex rel. Thompson v. Columbia/HCA Healthcare Corp.*, 125 F.3d 899, 902, 903 (5th Cir. 1997).

52. *Mikes*, 274 F.3d at 693.

53. *Id.* at 697.

most notably the Fourth Circuit's decision in *United States ex rel. Harrison v. Westinghouse Savannah River Co.*,⁵⁴ provided the DOJ with a possible answer. In *Harrison*, the court found that an organizational conflict of interest violation was material to the contract, but held that there were no damages where the government continued to fund the contract after learning about the conflict.⁵⁵ The court did, however, affirm the assessment of penalties, finding that penalties were the proper remedy when FCA violations had occurred but no damages were proven.⁵⁶

The DOJ response was to change its language, but not its position. In an amicus brief for *United States ex rel. Heath v. Dallas Fort Worth Airport Board*,⁵⁷ which followed shortly after the government's debacle in the *Southland* case, the DOJ stated that materiality was a requirement for FCA liability,⁵⁸ but it then defined materiality as simply a false certification that is "capable of influencing" or "has a natural tendency to influence" the government's decision to pay the claim.⁵⁹ The DOJ adopted the following position on materiality:

[T]he proper standard for determining whether the alleged false statements in the instant case were material is whether they had the potential or natural tendency to affect the Government's payment decision. This inquiry, in turn, requires the Court to examine the grant provisions with which the relator contends that the defendant misrepresented its compliance, to determine whether any of these provisions was a condition of payment. . . . If the defendant's false statements are determined to be related to a condition of payment—and the Government takes no position on this issue—those statements had a natural tendency to affect the Government's payment decision and were therefore material.⁶⁰

The DOJ's change in strategy was, for the most part, successful. Courts began to accept this capable of influencing standard. The Fourth Circuit, which previously adopted this standard,⁶¹ was joined by the Sixth Circuit in

54. *Harrison v. Westinghouse Savannah River Co.*, 352 F.3d 908 (4th Cir. 2003).

55. *Id.* at 917, 922-23.

56. *Id.* at 913 (noting that the district court ruled that even though plaintiff failed to prove actual damages, aggravating and mitigating circumstances allowed for a penalty against defendant).

57. *United States ex rel. Heath v. Dallas/Fort Worth Int'l Airport Bd.*, No. 3:99-CV-0100-M, 2004 WL 1197483 (N.D. Tex. May 28, 2004). (The reader should note that the author was one of the attorneys representing the defendant in this case.)

58. Heath Brief, *supra* note 21, at 3.

59. *Id.* at 4 (citing *Neder v. United States*, 527 U.S. 1, 16 (1999)).

60. Heath Brief, *supra* note 21, at 13.

61. See *Harrison v. Westinghouse Savannah River Co.*, 352 F.3d 908, 914 (4th Cir. 2003); *United States ex rel. Berge v. Board of Trs. of Univ. of Ala.*, 104 F.3d 1453, 1459 (4th Cir. 1997).

*United States ex rel. A+ Homecare, Inc. v. Medshares Management Group, Inc.*⁶² and a number of other courts.⁶³ Others, however, clung to the position that a false certification had to be a prerequisite to payment for FCA liability to result.⁶⁴

III. THE 2009 AMENDMENTS REQUIRE AND DEFINE "MATERIALITY"

When the opportunity presented itself, the DOJ used Congress's desire to amend the FCA to settle the dispute over materiality. In 2008, a number of amendments to the FCA were proposed primarily by *qui tam* relator groups lobbying for elimination of certain defenses adverse to *qui tam* relator lawsuits.⁶⁵ The DOJ opposed these amendments, primarily because the amendments would have allowed government employees, in certain circumstances, to bring *qui tam* cases for their own personal benefit.⁶⁶ The DOJ Comment Letter to the Senate Judiciary Committee (as well as a later letter to the House Judiciary Committee) expressed this opposition but stated that, if Congress wished to amend the FCA, the DOJ had a number of amendments in mind.⁶⁷ For the most part, these amendments were accepted and passed by the Judiciary Committees of both the Senate and the House, but the bills never reached the floor of either house of Congress before the session ended.⁶⁸

62. *United States ex rel. A+ Homecare, Inc. v. Medshares Mgmt. Group, Inc.*, 400 F.3d 428, 445 (6th Cir. 2005).

63. *See, e.g., United States v. Bourseau*, 531 F.3d 1159, 1171 (9th Cir. 2008); *United States v. Rogan*, 517 F.3d 449, 452 (7th Cir. 2008).

64. *See Mikes v. Straus*, 274 F.3d 687, 698 (2d Cir. 2001); *United States ex rel. Thompson v. Columbia/HCA Healthcare Corp.*, 125 F.3d 899, 902 (5th Cir. 1997); *United States ex rel. Hopper v. Anton*, 91 F.3d 1261, 1266 (9th Cir. 1996); *United States ex rel. Smart v. Christus Health*, 626 F. Supp. 2d 647, 656 (S.D. Tex. 2009); *United States ex rel. Graves v. ITT Educ. Servs., Inc.*, 284 F. Supp. 2d 487, 496 (S.D. Tex. 2003).

65. *See generally* False Claims Act Correction Act of 2008, S. 2041, 110th Cong. § 3 (2008); False Claims Act Correction Act of 2007, H.R. 4854, 110th Cong. (2007). *See also* S. REP. NO. 110-507, at 9 (2008) (Committee on the Judiciary's report outlining proposed amendments of S. 2041); John T. Boese & Michael J. Anstett, *Dramatic Changes to the False Claims Act are No Laughing Matter*, METRO. CORP. COUNSEL, Feb. 2009, at 14, 14, available at <http://www.metrocorpcounsel.com/pdf/2009/February/14.pdf>. (The reader should note that the author testified before the Senate Judiciary Committee in opposition to these amendments.)

66. U.S. DEP'T OF JUSTICE, *Comments on Managers' Substitute Amendment of S. 2041*, 1-2 (2008), available at <http://www.ffhsj.com/files/QTam/DOJ%20Comments%20on%20Sub.%20S.%202041.pdf>.

67. *Id.* at 2-3.

68. Chris Flynn et al., *The False Claims Act Correction Act: Key Provisions and Implications*, 12 PAYORS PLANS & MANAGED CARE, Jan. 2009, at 17, 17, available at <http://www.crowell.com/documents/The-False-Claims-Act-Correction-Act.pdf>.

The DOJ proposals, however, became the basis of the 2009 amendments to the FCA found in Section 4 of the Fraud Enforcement and Recovery Act of 2009 (“FERA”).⁶⁹ These amendments, in the main, did not address the concerns of the *qui tam* lobbyists, but they did address the DOJ issues. For the first time, these amendments also addressed the issue of materiality. As stated above, materiality was added as a specific requirement in both sections 3729(a)(1)(B) and (G).⁷⁰ Materiality was defined in new section 3729(b)(4) as the “capable of influencing” or “natural tendency to influence” standard, the same standard that the DOJ has espoused in its amicus briefs.⁷¹ That amendment, however, was not retroactive. It applies only to false claims submitted after May 20, 2009.⁷² At least one court, however, has used the adoption of the capable of influencing standard in FERA as a reason to adopt this standard in pre-2009 cases.⁷³ Other courts, even after the amendments, have continued to use the prerequisite for payment standard.⁷⁴

IV. THE FUTURE OF THE “MATERIALITY” STANDARD

One would think, in light of the active and vigorous debate over the proper definition and test for materiality, that decisions would hinge on whatever standard was adopted. In fact, for the most part, the opposite has been true. A few examples will demonstrate that.

Materiality is critical to one issue of great importance to hospitals—whether the violation of a condition of participation renders otherwise proper claims submitted by a hospital false under the FCA. Two leading cases have addressed that issue, and both concluded that a violation of a condition of participation would not, under the facts presented, be material to the government’s payment decision.⁷⁵ Both used the capable of

69. FERA, Pub. L. No. 111-21, § 4, 123 Stat. 1617, 1621-25 (2009).

70. FERA § 4(a)(1).

71. FERA § 4(a)(2); Heath Brief, *supra* note 21, at 4.

72. See FERA § 4(f); United States *ex rel.* Sanders v. Allison Engine Co., Inc., Nos. 1:95-cv-970, 1:99-cv-923, 2009 WL 3626773, at *4 (S.D. Ohio Oct. 27, 2009).

73. See United States *ex rel.* Longhi v. United States, 575 F.3d 458, 470 (5th Cir. 2009) (applying capable of influencing test to *qui tam* suit filed in 2002).

74. See, e.g., United States *ex rel.* Bauchwitz v. Holloman, No. 04-2892, 2009 WL 4362819, at *13 (E.D. Pa. Dec. 1, 2009); United States *ex rel.* Dillahunt v. Chromalloy Okla., No. CIV-08-944-L, 2009 WL 3837294, at *4 (W.D. Okla. Nov. 16, 2009).

75. See United States *ex rel.* Conner v. Salina Reg’l Health Ctr., Inc., 543 F.3d 1211, 1221 (10th Cir. 2008) (holding that perfect compliance is not a prerequisite to receiving Medicare payments); United States *ex rel.* Landers v. Baptist Mem’l Health Care Corp., 525 F. Supp. 2d 972, 979 (W.D. Tenn. 2007) (holding that “[c]onditions of [p]articipation do not condition payment on certifications of compliance”) (The reader should note that the author was one of the counsel for the defendant in this case.).

influencing standard. In *United States ex rel. Landers v. Baptist Memorial Health Care Corp.*, because the district court was in the Sixth Circuit, it was bound by the circuit's holding in *A+ Homecare* that materiality required only the capable of influencing standard.⁷⁶ The court carefully analyzed the decisions in *Harrison* and *A+ Homecare* to determine exactly what the natural tendency test meant.⁷⁷ Nevertheless, on a summary judgment motion in which the court assumed that a standard of participation had been violated, the court held:

In this case, Plaintiff has failed to satisfy the Sixth Circuit's materiality requirement for liability under the FCA. As discussed above, Conditions of Participation do not condition payment on certifications of compliance. Therefore, any alleged false certifications of compliance would not have a natural tendency to influence the Government's payment decisions.⁷⁸

A similar decision was issued shortly thereafter by the Tenth Circuit in *United States ex rel. Conner v. Salina Regional Health Center, Inc.*⁷⁹ Again, the *qui tam* relator argued that the defendant had submitted false claims to Medicare because the hospital was in violation of certain conditions of participation.⁸⁰ The relator relied upon the language in the cost report certifying that the hospital was in compliance with the various Medicare laws and regulations.⁸¹ This was rejected both by the district court and the Tenth Circuit.⁸² The Tenth Circuit first addressed the nature of this certification:

Although this certification represents compliance with underlying laws and regulations, it contains only general sweeping language and does not contain language stating that payment is conditioned on perfect compliance with any particular law or regulation. Nor does any underlying Medicare statute or regulation provide that payment is so conditioned. Thus, by arguing that the certification's language is adequate to create an express false certification claim, Conner fundamentally contends that *any* failure by SRHC to comply with *any* underlying Medicare statute or regulation during the provision of *any* Medicare-reimbursable service renders this certification false, and the resulting payments fraudulent.⁸³

The court then addressed the relationship between violations of conditions of participation and the FCA:

76. *Landers*, 525 F. Supp. 2d at 979.

77. *Id.*

78. *Id.*

79. *United States ex rel. Conner v. Salina Reg'l Health Ctr., Inc.*, 543 F.3d 1211 (10th Cir. 2008).

80. *Id.* at 1215-16.

81. *Id.* at 1218-19.

82. *Id.* at 1216, 1219.

83. *Id.* at 1219.

[L]iability [under the FCA] does not arise merely because a false statement is included within a claim, but rather the claim itself must be false or fraudulent." *United States ex rel. A+ Homecare, Inc. v. Medshares Mgm't Group, Inc.*, 400 F.3d 428, 443 (6th Cir. 2005). A false certification is therefore actionable under the FCA only if it leads the government to make a payment which it would not otherwise have made. *See, e.g., United States ex rel. Hopper v. Anton*, 91 F.3d 1261, 1266 (9th Cir. 1996). Or, put another way, the "false statement must be material to the government's decision to pay out moneys to the claimant."⁸⁴

The court then rejected the relator's theory of liability:

A brief review of the scheme for managing Medicare participation will demonstrate that the annual cost report certification does not condition the government's payment on perfect compliance with all underlying statutes and regulations, but rather seeks assurances that the provider continues to comply with the conditions of participation originally agreed upon. Reading the FCA otherwise would undermine the government's own administrative scheme for ensuring that hospitals remain in compliance and for bringing them back into compliance when they fall short of what the Medicare regulations and statutes require.⁸⁵

Another case that rejected FCA liability under the capable of influencing test is *United States ex rel. Lamers v. City of Green Bay*.⁸⁶ In that case, the Seventh Circuit was faced with facts that clearly indicated that the City of Green Bay had misled the federal government on various grant applications.⁸⁷ The court referred to the Fourth Circuit's materiality holdings, and yet it held that these misstatements by the City were irrelevant to the funding decision.⁸⁸ It is almost impossible to believe that those misstatements would not have been at least capable of influencing the DOT's decision to fund the grant, but the court of appeals had no problem rejecting the FCA claim.⁸⁹

84. *Id.* at 1219.

85. *Id.* at 1220.

86. *United States ex rel. Lamers v. City of Green Bay*, 168 F.3d 1013, 1019, 1020 (7th Cir. 1999).

87. *Id.* at 1015.

88. *Id.* at 1019.

89. *Id.* at 1020. In many cases that adopt the "capable of influencing" standard for materiality, the court, explicitly or implicitly, makes clear that the defendant would have been liable even under a more stringent standard. *See, e.g., United States ex rel. Longhi v. United States*, 575 F.3d 458, 472 (5th Cir. 2009). In *Longhi*, the Fifth Circuit Court of Appeals addressed the proper materiality standard for a pre-FERA FCA case. *Id.* at 468-69. Influenced by the new definition of materiality, the court decided to adopt the "capable of influencing" standard, despite previous Fifth Circuit law to the contrary. *Id.* at 470. Importantly, however, the court makes clear that the defendant would have been liable regardless of the definition utilized by stating that

If a violation of a condition of participation is not, as a matter of law, at least capable of influencing the decision by the government to pay a Medicare claim, what is? If lying on a grant application is not capable of influencing the funding decision, what is? What comes out of these and many other similar decisions is this: Most rational courts are not going to allow a miscarriage of justice. Most rational courts are also not going to allow a defendant to be bankrupted when it provides necessary services to eligible beneficiaries or when a contractor provides articles that met all the specifications, just because some ancillary law was broken. If these courts cannot grant a motion to dismiss or summary judgment, as in *Landers*,⁹⁰ *Conner*,⁹¹ and *Lamers*,⁹² they will limit the recovery to penalties, as in *Harrison*.⁹³ Where there is true fraud—a factually false claim—the court will find liability regardless of the standard (as in *A+ Homecare*⁹⁴ and *Longhi*⁹⁵).

The flaw in this approach, of course, is its very randomness. The avoidance of a true miscarriage of justice relies on judges, at both the district and appellate levels, creating definitions of “capable of influencing” and “natural tendency to influence” to avoid the financial disaster foreseen by the Tenth Circuit in *Conner*, where it recognized that a strict interpretation of materiality could “undermine the government’s own administrative scheme for ensuring that hospitals remain in compliance.”⁹⁶

Adding the definition of materiality in the 2009 amendments was intended by the DOJ to eliminate this issue. For the government’s own sake, one hopes it has not and will not. As the Supreme Court stated many years ago in *McNinch*, not every violation results in an FCA violation, and

[t]he Government has also successfully demonstrated [that] Lithium Power’s false statements were material. As we explained above, the test for determining whether a false statement is material is whether it has a ‘natural tendency to influence or is capable of influencing’ the government’s decision-making. We are convinced that Lithium Power’s false statements had the potential to influence the [Government’s] decisions to award Lithium Power the SBIR grants Moreover, in the instant case we also have the evidence that the false statements actually influenced the decision to award the Defendants the SBIR grants.

Id. at 471-72.

90. United States *ex rel.* *Landers v. Baptist Mem’l Health Care Corp.*, 525 F. Supp. 2d. 972, 980 (W.D. Tenn. 2007).

91. United States *ex rel.* *Conner v. Salina Reg’l Health Ctr.*, 543 F.3d. 1211, 1226 (10th Cir. 2008).

92. *Lamers*, 168 F.3d at 1020.

93. *Harrison v. Westinghouse Savannah River Co.*, 352 F.3d 908, 922-23 (4th Cir. 2003).

94. United States *ex rel.* *A+ Homecare, Inc., v. Medshares Mgmt. Group, Inc.*, 400 F.3d 428, 452 (6th Cir. 2005).

95. United States *ex rel.* *Longhi v. United States*, 575 F.3d 458, 472 (5th Cir. 2009).

96. *Conner*, 543 F.3d at 1220.

that remains the law.⁹⁷ Long before materiality was an issue, courts have been rejecting FCA claims if the false statement or false certification was not essential—not a prerequisite—to the government’s decision to pay the claim.⁹⁸ In earlier decisions it was based on reliance or causation.⁹⁹ In the *Mikes* case, the court specifically stated that it was not relying on materiality.¹⁰⁰ While, for many years, this materiality requirement was used to reject improper claims, if materiality is no longer available, courts will find another way to reach the same conclusion.

If courts do not, the FCA will no longer be a statute to remedy fraud upon the Federal Treasury. Without a direct and causal connection between the false certification and the false claim, without some type of prerequisite to payment requirement, the FCA is no longer remedial. It then becomes a criminal statute and is probably unconstitutional unless enforced with all the protections of a criminal prosecution.

If the purpose of FERA’s amendment was to effectively eliminate materiality as an element of FCA liability, one needs to keep in mind Mr. Stevenson’s warning: “Words calculated to catch everyone may catch no one.”¹⁰¹ Hopefully, courts will apply the new definition of materiality with this in mind.

97. *United States v. McNinch*, 356 U.S. 595, 599 (1957).

98. *See United States v. Thomas*, 709 F.2d 968, 971-72 (5th Cir. 1983); *United States v. Miller*, 645 F.2d 473, 475-76 (5th Cir. 1981); *United States ex rel. Weinberger v. Equifax, Inc.*, 557 F.2d 456, 460 (5th Cir. 1977).

99. *See Miller*, 645 F.2d at 475-76; *United States v. Hibbs*, 568 F.2d 347, 350 (3d Cir. 1977); *Woodbury v. United States*, 232 F. Supp. 49, 55 (D. Or. 1964).

100. *Mikes v. Straus*, 274 F.3d 687, 697 (2d Cir. 2001).

101. *Stevenson*, *supra* note 1, at 13.