

# The “Gumbo” of Civil Fraud Enforcement:

*The False Claims Act, FIRREA, and a New Era in Federal and State Governments’ Enforcement Against Fraud*

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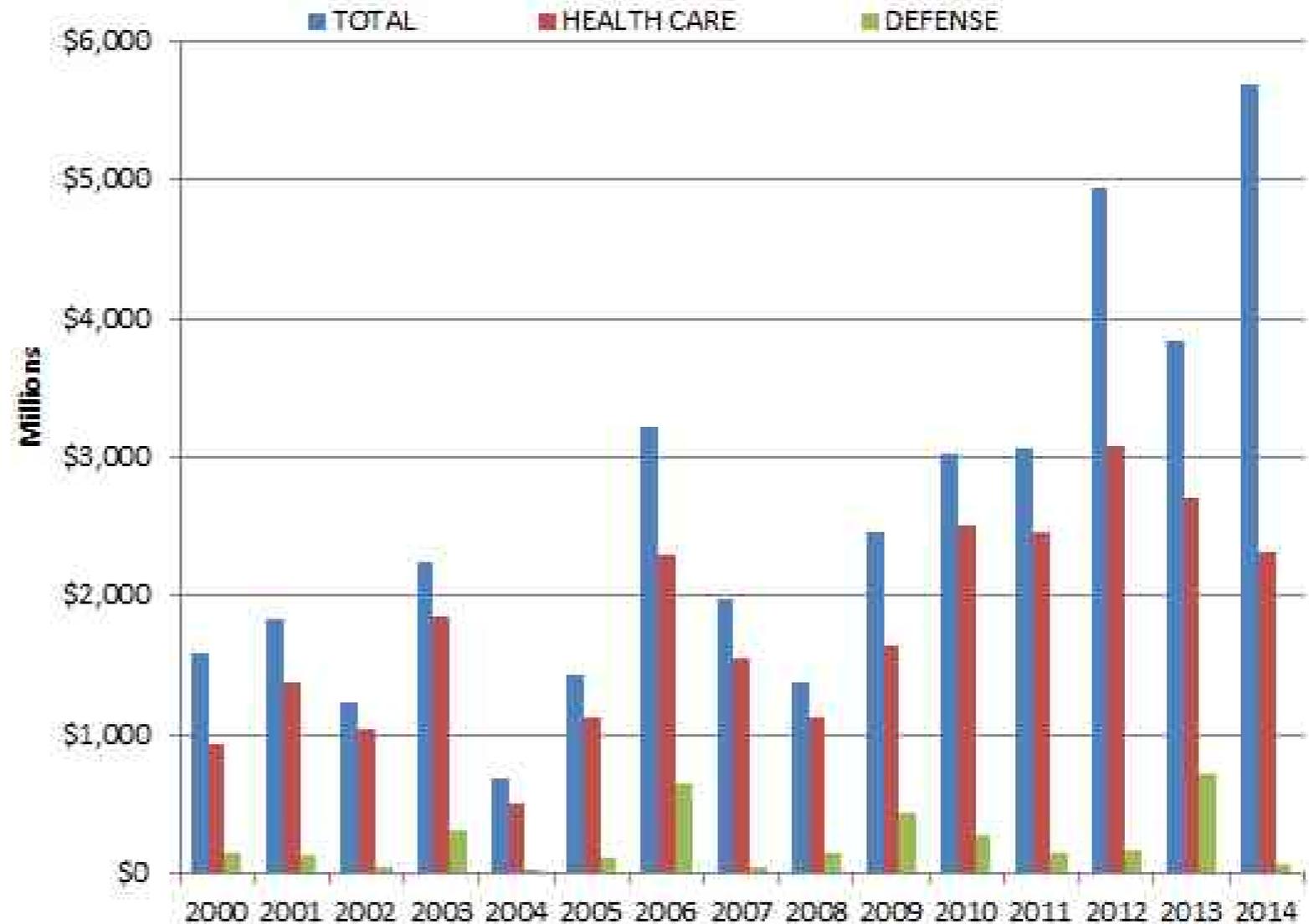
# Topics

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- **Why are the False Claims Act and FIRREA relevant?**
- **Whistleblower / Anti-Retaliation Issues**
- **Federal / State Investigations and Coordination**
- **Compliance and Best Practices**

# Civil Fraud Enforcement on the Rise – Total Recoveries

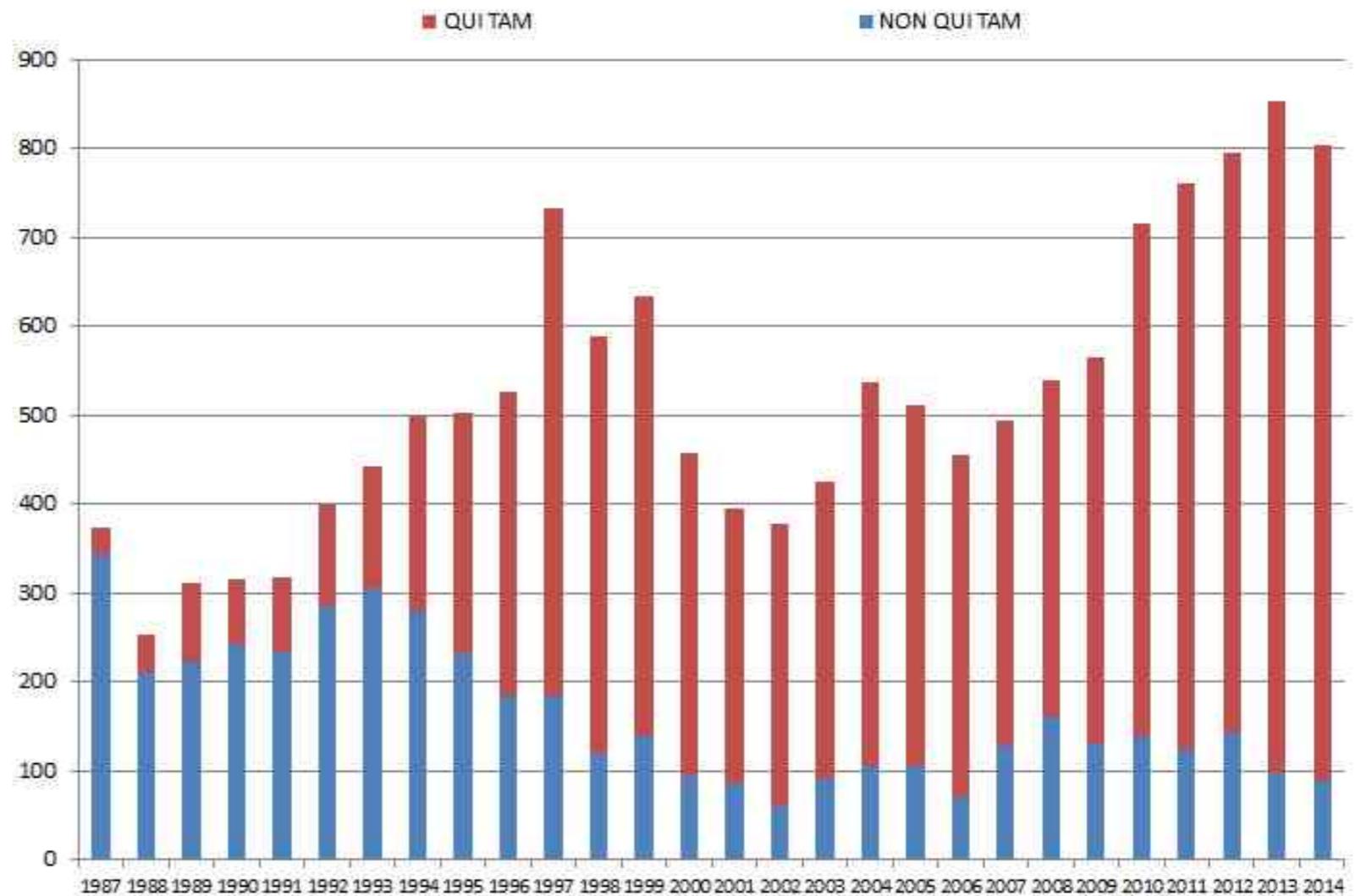
- \$5.69 billion in False Claims Act settlements in 2014
- Since January 2009, over \$23 billion in FCA recoveries – over half of total recoveries since Congress amended FCA 28 years ago to strengthen whistleblower lawsuits



Source: Gibson Dunn 2014 False Claims Act Year-End Update

# Civil Fraud Enforcement on the Rise – Qui Tam Lawsuits

- Whistleblowers initiated 713 of the 804 FCA cases filed in 2014
- Second highest number of qui tam complaints filed (754 in 2013)
- Qui tam complaints have, on average, doubled, since early 2000s



Source: Gibson Dunn 2014 False Claims Act Year-End Update

# Civil Fraud in DOJ Crosshairs

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- DOJ will “be stepping up [its] use of one tool [to combat crime]. . . [and] investigating and filing cases under the False Claims Act. Through our Fraud Section, we will be committing more resources to this vital area, so that we can move swiftly and effectively to combat major fraud involving government programs.” – Leslie Caldwell, DOJ Assistant Attorney General for the Criminal Division, September 2014.
- “In 2011, many of you were with us in the Great Hall at the Justice Department when we celebrated the twenty-fifth anniversary of the 1986 amendments to the False Claims Act. Those amendments have played a critical role in transforming the FCA into what it is today – the most powerful tool the American people have to protect the government from fraud.” – Stuart Delery, then-DOJ Assistant Attorney General for the Civil Division, June 2014.



# Industries in Focus

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- Health Care and Life Sciences
  - More than 60% of FCA cases
  - Pharma companies: off-label marketing
  - Hospital and medical providers: improper Medicare/Medicaid billing
- Banks and Financial Institutions
  - Focus on fallout from 2008 financial crisis
  - Misconduct related to residential mortgage-backed securities
- Defense and Government Contractors
  - Focus on inflated costs billed in connection with military efforts



# False Claims Act – Key Features

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- Liability for any person who (1) knowingly presents or causes to be presented a false or fraudulent claim for payment; (2) knowingly makes, uses, or causes to be made or used, a false record or statement material to a false or fraudulent claim; or (3) conspires to commit a violation.
- FCA liability can impose not only mandatory treble damages, but also a civil penalty of \$5,500 to \$11,000 imposed for each claim for payment that is found to be false or fraudulent.

# False Claims Act – General Prohibitions

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- Affirmative False Claims
  - Knowingly filing, or causing to be filed, a false or fraudulent claim
  - Knowing use of a false record or statement to get a false or fraudulent claim paid
  - Conspiring to defraud the government by getting a false or fraudulent claim paid

# False Claims Act – General Prohibitions

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- Reverse False Claims
  - Old language: Knowingly makes, uses, or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government
  - New language (amended in 2009 by Fraud Enforcement and Recovery Act): It is now also illegal to “knowingly conceal . . . or knowingly and improperly avoid . . . or decrease . . . an obligation to pay or transmit money or property to the Government”
  - Eliminates the need for a “false statement or record” – mere knowledge is now enough to create FCA liability

# False Claims Act – Sample Penalty Calculation

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- Defense Contractor
  - \$100,000 damages x 3 = \$300,000
  - 12 (# of claims) x \$11,000 = \$132,000
  - Total maximum liability = \$432,000
- Health Care Provider
  - \$100,000 damages x 3 = \$300,000
  - 2,000 (# of claims) x \$11,000 = \$22,000,000
  - Total maximum liability = \$22,300,000
- Treble damages in combination with statutory penalties held to be constitutional
- One district court held that even an 8 to 1 ratio of total judgment to single damages was not in violation of Excessive Fines Clause of 8<sup>th</sup> Amendment

# False Claims Act – Relator's Share

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- Relator (qui tam plaintiff) can proceed even if Government declines
- Can receive 15-25% of recovery if Government intervenes
- Can receive up to 30% of recovery if Government declines



# State AG Focus on False Claims Enforcement

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- **The rise of state law *qui tams*.** The 2005 Federal Deficit Reduction Act incentivized states to bolster *qui tam* provisions.
- **A focus on health care ... and more.** Medicaid has been the traditional focus of state enforcement, but now includes financial services and defense procurement.
- **Majority of states have false claims laws on the books.** 33 states and the District of Columbia, most of which apply to general false claims.

# California

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- California's False Claims Act — Enacted in 1987 (CA Gov. Code Section 12650, *et seq.*)
- Very similar to federal False Claims Act, with important California-specific differences — *e.g.*, inadvertent submissions, government dismissals, exhaustion, and recovery percentages.
- 2013 amendments to track the federal False Claims Act and receive a +10% recovery in Medicaid actions.



# What are the States Targeting?

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- Health Care - Medicaid and Pharma
- Financial Services — *e.g.*, *People v. McGraw-Hill* (Standard & Poor's)
- Government procurement

# FIRREA

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## *Financial Institutions Reform, Recovery, and Enforcement Act*

- **An old “new” tool for fraud enforcement.** FIRREA was enacted in 1989 after the savings-and-loan crisis.
- **Involves or affects a financial institution.** Authorizes suit based on violation one of 14 statutes — 9 relate to harm to banks (e.g., bank fraud, fraud in connection with SBA transactions) and 5 relate to fraud generally (with a nexus that it “affects” a financial institution).
- **Preponderance.** It’s a lower burden to prove the underlying criminal predicate.
- **Significant penalties.** \$1.1m per violation or more for continuing offenses (\$1.1m per day / \$5.5m per violation).



# FIRREA: *Notable Actions*

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- **Mortgage securitization.** Multiple settlement examples, including Standard & Poor's (\$1.2b), BOA (\$16b), Citigroup (\$7b), and J.P. Morgan Chase (\$13b).
- **Forex trading.** Misreps in connection with foreign-exchange trading by bank. *U.S. v. Bank of New York Mellon* (S.D.N.Y. 2011).
- **Future targets?** Industries, not individual actors.



# Whistleblower Protections – Anti-retaliation

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- FCA anti-retaliation provision – 31 USC 3730(h)(1)
  - Protects “any employee, contractor, or agent” against discrimination in the terms and conditions of employment because of lawful acts “in furtherance of an action under this section or other efforts to stop 1 or more violations of the FCA.”
  - Relief: employment reinstatement, 2 times backpay, compensation for special damages (e.g., litigation costs and attorney fees).
- Sarbanes-Oxley §1107 amends 18 U.S.C. §1513
  - Prohibits retaliation by any employer against any employee who provides “truthful” information to law enforcement relating to commission of any federal offense.
  - Need not be a violation of the Sarbanes-Oxley Act.
- Many other potentially applicable federal/state anti-retaliation laws

# Whistleblower Protections – Anti-retaliation

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- Employee engaged in a protected activity
- Employer took adverse employment action against the employee
- Adverse action was causally related to the protected activity



# Whistleblower Protections – KBR case

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- First enforcement action against a company for using restrictive language in confidentiality agreements that could stifle whistleblowing process.
- **Allegations:**
  - Global technology and engineering firm KBR violated the Dodd-Frank Act by requiring witnesses in internal investigations to sign confidentiality statement, that stated: “I understand that . . . I am prohibited from discussing any particulars regarding this interview and the subject matter discussed during the interview, without prior authorization of the Law Department. I understand that unauthorized disclosure . . . may be grounds for disciplinary action up to and including termination of employment.”
  - No known instance where employee was in fact stifled – merely the potential that an employee could be stifled.

# Whistleblower Protections – KBR case

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- **Settlement:** \$130,000. KBR also voluntarily amended confidentiality statement to add language clarifying that employees were free to report violations to the SEC and federal agencies without KBR approval.
- **SEC to Continue Enforcement:** “SEC rules prohibit employers from taking measures through confidentiality, employment, severance, or other type of agreements that may silence potential whistleblowers before they can reach out to the SEC. We will vigorously enforce this provision.” - Andrew J. Ceresney, Director of the SEC’s Division of Enforcement.
- Impact on *Upjohn* warnings?

# Federal/State Coordination

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- **Layers of regulators.** Feds (DOJ, FTC, CFPB) and state AGs, plus *qui tam* relators.
- **Force multiplier.** Increases litigation risk across jurisdictions in the United States.
- **Intelligence sharing.** Mutually strengthens cases — *e.g.*, Standard & Poor's.



# Corporate Compliance / Best Practices

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- **Update code of conduct and compliance policies**
  - Emphasize that employees are required to maintain culture of compliance by complying with standards themselves and reporting those who run afoul of the law/standards
- **Educate employees**
  - Mandatory training on policies/procedures
  - Familiarity with steps and timeline of reporting process – use hypotheticals
- **Robust internal reporting system**
  - Hotline; formalized complaint intake; training for supervisors
- **Prevent retaliation**
- **Review confidentiality agreements, exit interviews**
- **Consider incentive structure**





## Government & Internal Investigations ADVISORY ■

**SEPTEMBER 25, 2014**

### Criminal Division to Investigate All False Claims Act Qui Tam Claims

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The United States Department of Justice (DOJ) announced last week that its Criminal Division will review all future complaints filed under the *qui tam* provisions of the federal False Claims Act. Assistant Attorney General Leslie Caldwell introduced the new policy during a speech before the Taxpayers Against Fraud Education Fund.

The False Claims Act (FCA) is the government's primary civil remedy for redressing fraud against the government. Most FCA actions are filed by private citizens under the statute's whistleblower, or *qui tam*, provisions. Previous DOJ policy required only that federal civil prosecutors review *qui tam* complaints; review by criminal prosecutors has always been discretionary. Now, according to AAG Caldwell, "experienced prosecutors in the [Criminal Division's] Fraud Section are immediately reviewing the *qui tam* cases . . . to determine whether to open a parallel criminal investigation."

Although the Criminal Division will review all *qui tam* complaints, AAG Caldwell highlighted three industries that will face particular scrutiny: health care, defense procurement, and financial services. DOJ has devoted substantial resources to these industries in recent years: in 2013 alone, it recovered \$2.6 billion for health care fraud violations and charged 345 individuals with associated crimes. Since 2009, over 100 individuals have been charged for procurement fraud, while financial institutions and executives have faced criminal scrutiny for alleged mortgage fraud, Ponzi scheme involvement, and various other allegations of fraud and corruption.

These numbers will only increase under the Criminal Division's new *qui tam* policy. Some reasons are obvious—criminal prosecutors will have greater exposure to criminal activity. Other reasons might be less obvious—criminal prosecutors may notice potential criminal allegations in an otherwise civil complaint. For example, an FCA action brought under the civil Stark Law may result in a criminal investigation under the Anti-Kickback Statute. A contractor facing civil procurement fraud allegations might also be investigated under the Foreign Corrupt Practices Act.

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For these and other reasons, AAG Caldwell encouraged *qui tam* relators to consult with criminal authorities when filing *qui tam* complaints. Said Caldwell, “the earlier we begin our investigation, the more legal tools and investigative techniques we have available to us. . . . [W]e can bring more cases and hold more companies and individuals responsible for the crimes they commit.”

The new policy creates procedural and strategic challenges. Most investigations begin with the receipt of a subpoena or Civil Investigative Demand for documents (CID). Because of the mandatory sealing provisions under the FCA, companies often do not know at the outset whether a government inquiry is the result of a *qui tam* complaint or some other type of review. Given the significance of this new policy, companies or individuals facing these investigations should assume that an inquiry is related to a *qui tam* complaint *and* that the Criminal Division is also involved. Nothing in AAG Caldwell’s new policy announcement provides any guidance as to when a company or individual will be informed that the Criminal Division’s review is complete and that an inquiry is only civil.

Companies and individuals should adjust their strategy to account for increased Criminal Division presence. For example, a defendant should assume that criminal prosecutors will review materials that are produced in response to a CID. Fifth Amendment protection may be appropriate and necessary in certain circumstances. In order to mitigate the risk of prosecution, *qui tam* defendants should carefully consider these potential issues, including whether and when to communicate with the Criminal Division, in order to obtain certainty around whether the DOJ intends to open a parallel criminal investigation.

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