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Ideas for Reforming the False Claims Act

From the Experts

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Every company that receives federal funds in any form—whether by contract, as a subcontractor, through a federal subsidy program or as a grantee—or that has obligations to the federal government, has reason to focus on the False Claims Act (FCA). A statute originally designed to punish fraud in government contracting, the FCA has been amended in recent years to reach every form of federal assistance, including grants and loans, and indirect as well as direct recipients. And the FCA incentivizes whistleblowers by allowing them to sue in the name of the federal government. As a result, litigation and liability under the FCA are skyrocketing. Nearly a thousand new suits were filed last year, most by self-proclaimed "whistleblowers" seeking a share of the government's recoveries—which over the past five years have totaled nearly $15 billion.

The FCA's after-the-fact punishment-through-litigation approach to reducing fraud in government programs is both inefficient and frequently unfair, too often pressuring companies to settle for vast amounts to resolve what are at most minor regulatory defaults and incentivizing the filing of meritless suits. The authors helped design amendments to the FCA, recently proposed by the U.S. Chamber of Commerce Institute for Legal Reform (ILR), that would change the paradigm by aligning corporate interests in conforming to the law with the government's interest in fraud-free federal programs. Compliance, not after-the-fact jackpot recoveries, should be the first line of defense against fraud in government programs.

This article describes key elements of compliance best practices and outlines the ILR's proposed reforms designed to fight fraud by incentivizing state-of-the-art in-house compliance efforts.

Calibration of Multiplier

A company that violates the FCA is generally liable for three times the amount of damages sustained by the government, regardless of the company's degree of culpability. Thus, a defendant that acts with intent to defraud the government is subject to the same damages multiplier as the defendant who lacks such intent but is later found to have been reckless about the truth or falsity of some material aspect of a claim. (The FCA provides for a reduction to double damages if the defendant has made a disclosure to the government of the misconduct, has fully cooperated with the government and had no knowledge of a government investigation at the time of the disclosure. But courts have relied on this provision only rarely.)

ILR proposes that for companies with certified compliance programs, the multiplier structure should differentiate between companies that have acted with intent to defraud (treble damages), entities that have made good-faith attempts to ensure compliance but whose employees have engaged in misconduct (double damages), and entities that

promptly disclose any wrongdoing to the government (1.5 times damages).

Certified compliance programs reduce fraud and thus save the government money. Self-reports also save the government significant time and money, by reducing the cost of investigation and prosecution and ensuring that violations are detected. Without concrete incentives—such as assurances that lower damages will be imposed—companies may be hesitant to come forward with reports of possible misconduct.

Jurisdictional Bar on *Qui Tam* Actions

Under the current FCA, a *qui tam* plaintiff who files suit after the defendant has already disclosed the same conduct to an agency inspector general is entitled to proceed with the suit and receive a full bounty. This possibility exists even though the disclosure has been made to the government authority responsible for investigating fraud, and even though the party making the disclosure is typically required to cooperate fully in the investigation. When a corporation has made a disclosure of fraud to an agency IG or other investigative office, qui tam actions based on the same allegations of fraud should be foreclosed.

The self-disclosure provision advocated by ILR would not foreclose actions filed by whistleblowers who provide the government with information about fraud before a corporation makes a self-disclosure.

Incentives for Potential Relators to Report Internally

The FCA currently provides no incentive for employees to report concerns about potential fraud to their employers. To the contrary, the FCA contains a structural disincentive to internal reporting in the form of the "first-to-file" provision, which specifies that only the first relator who files suit is eligible for a bounty. This provision creates a "race to the courthouse," with the problematic effect that a potential relator has no incentive to take the extra step of reporting internally first since doing so might reveal information to other employees, one of whom might beat the initial discoverer of the problem to court.

The FCA's disincentives for prompt internal reporting are out of sync with modern statutory and regulatory mechanisms that encourage internal reporting and more robust corporate compliance programs. If an employee of a company with a certified compliance program (or any other individual with a contractual or legal obligation to make reports to the company) fails to report the alleged misconduct internally at least 180 days before filing a qui tam suit, the ILR proposes that the court would be required to dismiss the action. The 180-day window would afford the employer sufficient time to investigate the allegations and make a determination whether to self-disclose a violation to the government and/or take corrective action. In order to ensure that a person who uses the internal reporting mechanism is not disadvantaged, the reforms would also provide that a person who reports internally and triggers a prompt disclosure by the company to the government would still be eligible for up to 10 percent of any government recovery that results from the company's disclosure. If the whistleblower reports internally, but the company does not promptly self-disclose and the whistleblower proceeds with a qui tam action, then the whistleblower will be deemed to have filed an action for purposes of the FCA's "first-to-file" bar dating back to the time of the internal report.

No Mandatory or Permissive Exclusion or Debarment

For government contractors, the threat of suspension or debarment based on FCA violations has become a tool for pressuring companies into substantial settlements. In 2011 alone, over 3,300 federal contractors were suspended or debarred as a result of increased contract monitoring by federal agencies. Health care and pharmaceutical companies in particular have faced this dilemma, with the threat of exclusion from federal healthcare programs, including Medicare and Medicaid. The U.S. Department of Health and Human Services has dramatically expanded the reach of the exclusion threat by making entities that are indirectly reimbursed for products prescribed to program beneficiaries subject to exclusion.

Exclusion or debarment may be necessary to protect federal programs from entities or individuals who present a particularly high risk of recidivism. But when a company has implemented a certified compliance program, the rationale for exclusion or debarment no longer applies. ILR has proposed eliminating the threat of exclusion for such companies. Doing so would create a powerful incentive for companies to adopt state-of-the-art compliance programs while also affording such companies the meaningful ability, where appropriate, to seek the guidance and protection of the courts.

Conclusion

The False Claims Act is an essential tool for fighting fraud in government programs—a goal that is all the more urgent at a time of enormous federal deficits. But the FCA as currently drafted and enforced is much less effective at preventing—and thus reducing—fraud than it could be, while it imposes unfair and unnecessary costs on businesses that are trying to do the right thing. Common-sense reforms of the sort described here can and should make the FCA both fairer and more effective.

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