Analyzing FCA Materiality Defense Outcomes Under Escobar

By **Brenna Jenny, Matthew Bergs and Paul Kalb** (December 13, 2021)

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The U.S. Supreme Court's 2016 decision in Universal Health Services Inc. v. U.S., generally known as the Escobar case,[1] put a spotlight on the government's continued payment in False Claims Act cases, establishing that the government's continued payment despite actual knowledge of a violation is a strong defense against the element of materiality.

To assess the current effectiveness of this defense, we analyzed all published opinions in FCA cases issued from July 1, 2019, to the present that substantively addressed the relevance of the government's continued payment to the materiality inquiry.[2]

Our analysis revealed that Escobar's continued-payment defense is often a winning argument for defendants, although the success rate can vary significantly based on factors such as the stage of litigation, the defendant's industry and the political affiliation of the administration that appointed each judge.

However, these trends may shift if Congress passes a recently proposed amendment to the FCA's materiality standard.

In Escobar, the Supreme Court unanimously held that the implied false certification theory is a valid basis for FCA liability in some circumstances, provided that the requirement at issue was material to the government's payment decision.[3]

The Supreme Court's approval of the implied false certification theory was a victory for whistleblowers and the U.S. Department of Justice, but far from a complete one.

The court rejected the DOJ's position that a violation is material so long as the defendant knew the government would be entitled to refuse payment if it had been aware of the violation, holding that the FCA's materiality requirement is demanding and rigorous, and must be strictly enforced.[4]

The court noted, in particular, that where 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."[5]

At the same time, the court went out of its way specifically to "reject [the] assertion that materiality is too fact intensive for courts to dismiss False Claims Act cases on a motion to dismiss or at summary judgment."[6]

Escobar's continued-payment defense has posed a particular threat to the DOJ's FCA enforcement in the health care industry because the Centers for Medicare & Medicaid Services rarely halt payment despite knowledge of alleged misconduct.

As a result, over the past few years, the DOJ has frequently attempted to clarify two

aspects of the continued-payment defense: which government actors need knowledge, and what knowledge they need.

For example, in statements of interest filed in the wake of Escobar,[7] the DOJ argued that it is not enough for defendants to point to law enforcement's knowledge of violations of law; instead, the relevant government payor, such as CMS, must have that knowledge.

Second, the DOJ argued that the type of knowledge the government payor must have is actual knowledge of misconduct, rather than mere awareness of allegations.

The DOJ has also emphasized that the government's continued payment is but one of many factors relevant to the materiality inquiry — despite the Supreme Court's characterization of such payment history as very strong evidence of a lack of materiality.

Earlier this year, in another statement of interest, the DOJ adopted an even more extreme position on what it views as the general irrelevance of the government's continued payment under Escobar.[8]

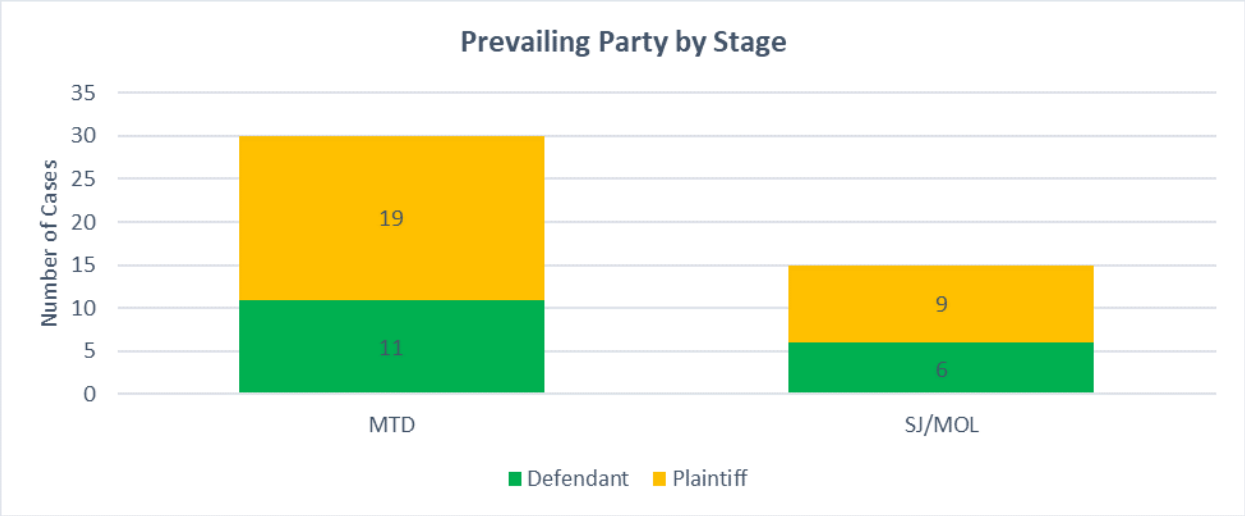
According to the DOJ, the government's continued payment is only relevant to the materiality inquiry if the government had "actual knowledge of specific false claims," rather than actual knowledge of a fraudulent course of conduct.

Even where alleged fraud has "been brought to the attention of the federal agency responsible for making the payment," unless the agency "knew of specific claims that were false and paid those claims notwithstanding such actual knowledge," the DOJ's position is that the continued payment cannot serve as meaningful evidence of a lack of materiality.[9]

The DOJ's campaign to chip away at Escobar's continued-payment defense has generated mixed results.

We identified 45 cases issued from July 1, 2019, to the present that substantively assessed the government's continued payment as part of an inquiry into materiality. In 30 of those 45 cases, the court was deciding a motion to dismiss, or MTD. In the remaining 15 cases, the court was deciding a motion for summary judgment or motion for judgment as a matter of law — SJ or JMOL, respectively.

The government's continued payment is often a winning argument for defendants, both at the MTD stage and the SJ/JMOL stages. Defendants defeated materiality using this defense in 37%, or 11 of 30, of the MTD cases, and 40%, or 6 of 15, of the SJ/JMOL cases.

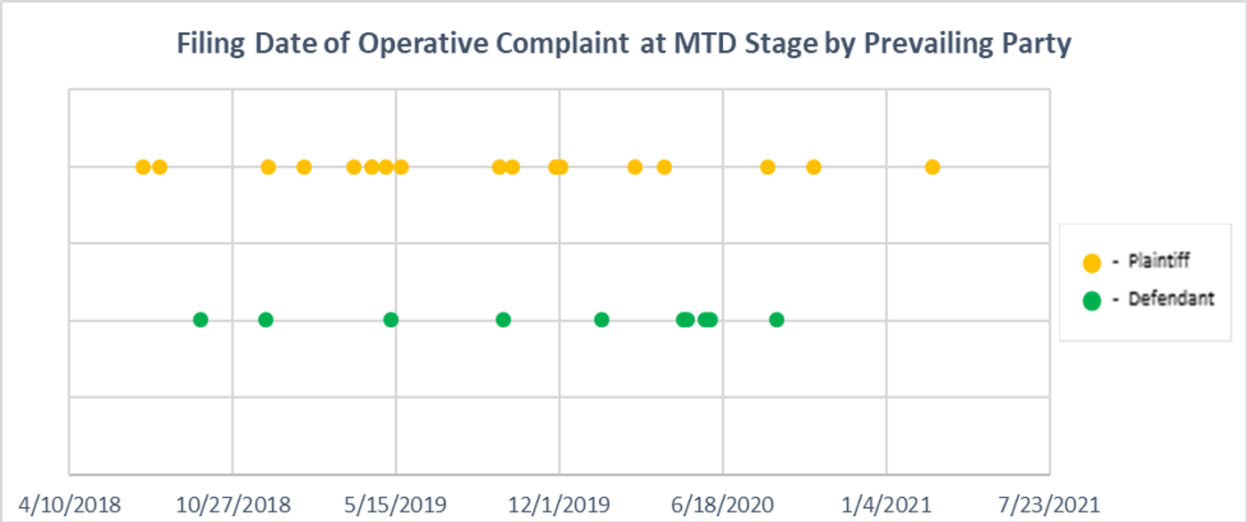


Courts siding with defendants on materiality at the MTD stage have generally relied on concessions in the pleadings about the government's continued payment, concluding that the complaint pleads its way out of materiality based on the plain meaning of Escobar's guidance.

We further explored the MTD stage data to determine whether there were any identifiable trends based on the filing date of the operative complaints underlying the MTD decisions.[10]

While one may have anticipated that post-Escobar, plaintiffs would be less likely to plead their way out of materiality based on the government's continued payment, there was in fact no correlation between whether the plaintiff or defendant prevailed and how long ago the operative complaint was filed.

There was also no correlation when we arrayed the decisions by the filing date of the original complaint.



Where courts sided with the relator or the government on materiality 63% of the time, or in

19 of 30 rulings, at the MTD stage, courts uniformly found that the continued-payment defense raised issues of fact not properly considered at the MTD stage. They did so despite the Supreme Court's specific admonition in Escobar that materiality may be decided as a matter of law.

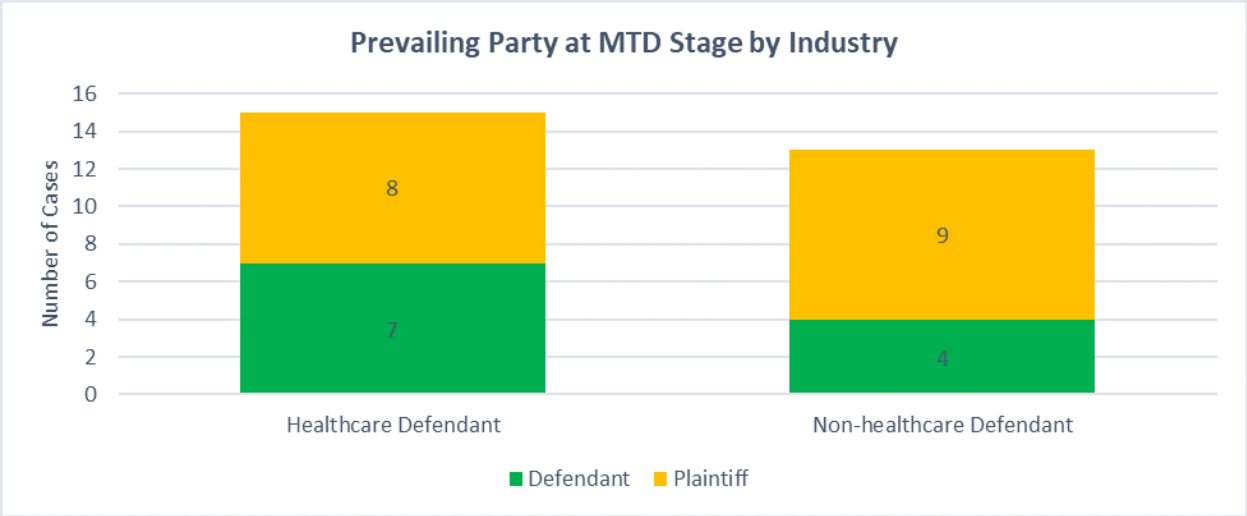
To further understand the MTD decisions, we analyzed the outcomes by the defendants' industries.

One might have expected that health care defendants employing the continued-payment defense at the MTD stage would fare worse than defendants in other industries due to the factual complexity of the health care industry and the fact that government payors might be particularly hesitant to deny payment for medically necessary services.

However, defendants in other industries actually fared somewhat worse than defendants in the health care industry at the MTD stage.

Furthermore, once cases involving a court's analysis of the materiality of alleged kickbacks are removed — allegations that uniformly were deemed adequate to plead materiality — the difference is even more significant. Defendants in the health care industry prevailed in 47% of the remaining motions to dismiss, or in 7 of 15 cases, and defendants in other industries prevailed in 30%, or 4 of 13, cases.

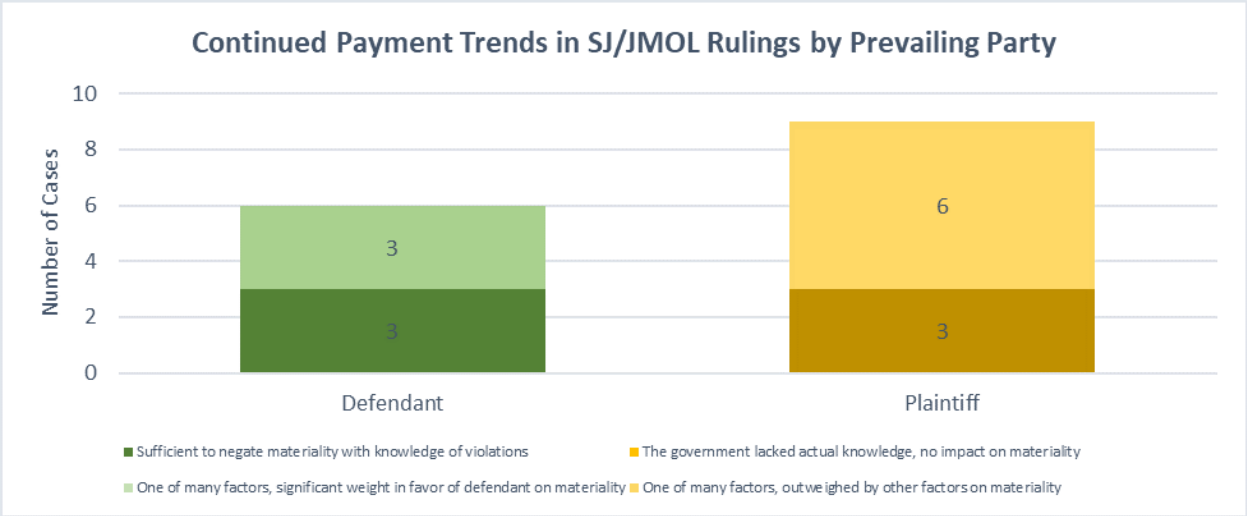
These outcomes could reflect how the hyper-regulated nature of the health care industry results in participants more frequently running afoul of one of the many nonmaterial requirements applicable to the industry.



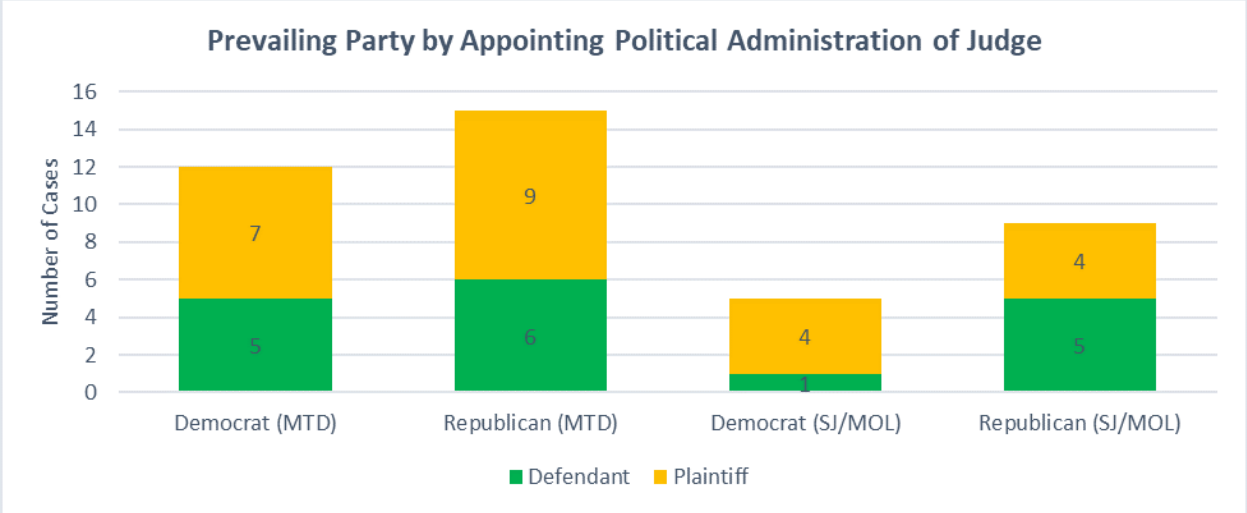
At the SJ/JMOL stages, courts ruling in favor of defendants on materiality commonly found either that: (1) while continued payment is one of many relevant materiality factors, consistent with Escobar, it bears significant weight in favor of defendants, or (2) continued payment during and after the DOJ's investigation with knowledge of violations is sufficient to negate materiality.

Courts ruling in favor of the relator or the government on materiality at the SJ/JMOL stages typically took one of two approaches, concluding either that: (1) continued payment is one of many materiality factors, but it was outweighed by other relevant factors, or (2) the continued-payment defense was undermined by the fact that the government lacked actual

knowledge of wrongdoing, as opposed to awareness of allegations, so its continued payment did not negate materiality.



Our review of the continued payment cases at the SJ/JMOL stages also revealed that judges appointed by Republican administrations appear more likely than judges appointed by Democratic administrations to find in favor of defendants. This pattern was not present in decisions at the MTD stage.[11]



These patterns demonstrate that courts have largely been faithful to Escobar's admonition that the materiality standard is a demanding one. But these patterns may shift in the future if Congress passes a set of amendments to the FCA proposed by Sen. Charles Grassley, R-Iowa, this past summer.[12]

As currently structured, the amendments would, among other things, add a new provision titled "Proving Materiality," which states:

> In determining materiality, the decision of the Government to forego a refund or to pay a claim despite actual knowledge of fraud or falsity shall not be considered

> dispositive if other reasons exist for the decision of the Government with respect to such refund or payment.[13]

This provision appears to have been designed specifically to undercut the Supreme Court's position in Escobar regarding the import of the government's continued payment.

Grassley has a long track record of proposing amendments to the FCA that are favorable to relators and the government. He claims primary responsibility for the 1986 amendments to the FCA, which ushered in the modern era of vigorous FCA enforcement,[14] and he has blamed courts for watering down the FCA post-Escobar.

For example, in opening remarks at the Federal Bar Association's 2021 Qui Tam Conference, Grassley criticized lower courts for interpreting Escobar in a way that "read[s] into the law a more stringent materiality standard than the text of the" FCA provides, and stressed the need to "come down with a sledgehammer" on those who commit fraud.[15]

If the proving-materiality amendment is passed, it has the potential to disrupt the relatively pro-defendant gains of the post-Escobar period.

In particular, the amendment seems calculated to eliminate the continued-payment defense at the MTD stage, when it may be easy to assert other — possibly even hypothetical — reasons for the government's continued payment.

The amendment may also create challenges for defendants at the SJ stage, where there may be disputes about whether the other reasons for continued payment proffered by the relators and/or the government truly caused the government's action or are instead merely hypothetical.

Regardless of whether the standard for proving materiality under the FCA is changed, courts will no doubt continue to exhibit a diverse range of approaches to assessing materiality.

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

[2] United States ex rel. Prose v. Molina Healthcare of Ill., Inc., 10 F.4th 765 (7th Cir. 2021); United States ex rel. Cimino v. Int'l Bus. Machines Corp., 3 F.4th 412 (D.C. Cir. 2021); United States ex rel. Sheoran v. Wal-Mart Stores E., LP, 858 F. App'x 876 (6th Cir. 2021); United States ex rel. Bibby v. Mortg. Invs. Corp., 987 F.3d 1340 (11th Cir. 2021); United States ex rel. Janssen v. Lawrence Mem'l Hosp., 949 F.3d 533 (10th Cir. 2020); United States ex rel. Patel v. Cath. Health Initiatives, 792 F. App'x 296 (5th Cir.

2019); United States ex rel. Kartozia v. Freedom Mortg. Corp., No. 18-cv-194-CDL, 2021 WL 4721066 (M.D. Ga. Oct. 8, 2021); United States ex rel. UPPI, LLC v. Cardinal Health, Inc., No. 17-cv-378-RMP, 2021 WL 4484552 (E.D. Wash. Sept. 29, 2021);United States ex rel. Lee v. N. Metro. Found. for Healthcare, Inc., No. 13-cv-4933-EK-RER, 2021 WL 3774185 (E.D.N.Y. Aug. 25, 2021);United States ex rel. Marsteller v. Tilton, No. 13-cv-830-AKK, 2021 WL 3726605 (N.D. Ala. Aug. 23, 2021);United States ex rel. Hamilton v. Yavapai Cmty. Coll. Dist., No. 12-cv-8193-PCT-GMS, 2021 WL 3709811 (D. Ariz. Aug. 20, 2021);United States ex rel. Sanders v. USAA Fed. Sav. Bank, No. 5:19-cv-00004, 2021 WL 3513663 (W.D. Va. Aug. 10, 2021);United States ex rel. Menoher v. FPoliSolutions, LLC, No. 19-cv-855, 2021 WL 3513860 (W.D. Pa. Aug. 10, 2021);United States ex rel. Aldridge v. Corp. Mgmt., Inc., No. 16-cv-369-HTW-LGI, 2021 WL 2518221 (S.D. Miss. June 18, 2021);United States ex rel. Lewis v. California Inst. of Tech., No. 18-cv-5964-CAS-RAO, 2021 WL 1600488 (C.D. Cal. Apr. 19, 2021);United States ex rel. Howard v. Caddell Constr. Co., Inc., No. 11-cv-270-FL, 2021 WL 1206584 (E.D.N.C. Mar. 30, 2021);United States ex rel. Conyers v. Halliburton Co., No. 06-cv-4024, 2021 WL 1140944 (S.D. Tex. Mar. 25, 2021);Hawaii ex rel. Torricer v. Liberty Dialysis-Hawaii, LLC, 512 F. Supp. 3d 1096 (D. Haw. 2021);United States ex rel. McIver v. ACT for Health, Inc., No. 18-cv-792-RBJ, 2021 WL 50879 (D. Colo. Jan. 6, 2021);United States ex rel. Savage v. CH2M Hill Plateau Remediation, Co., No. 14-cv-05002-SMJ, 2020 WL 8678016 (E.D. Wash. Dec. 30, 2020);United States ex rel. Armstrong v. Andover Subacute & Rehab Ctr. Servs. One, Inc., No. 12-cv-3319-SDW-MAH, 2020 WL 7640535 (D.N.J. Dec. 22, 2020);United States ex rel. Montcrieff v. Peripheral Vascular Assocs., PA, 507 F. Supp. 3d 734 (W.D. Tex. 2020);United States ex rel. Silbersher v. Allergan Inc., 506 F. Supp. 3d 772 (N.D. Cal. 2020);United States v. Honeywell Int'l Inc., 502 F. Supp. 3d 427 (D.D.C. 2020);United States ex rel. Parker v. Sea-Mar Cmty. Health Ctr., No. 18-cv-5395-RBL, 2020 WL 4698813 (W.D. Wash. Aug. 13, 2020);United States v. Ellis, No. 19-cv-107-CAR, 2020 WL 4642837 (M.D. Ga. Aug. 11, 2020);United States ex rel. Wallace v. Exactech, Inc., No. 18-cv-1010-LSC, 2020 WL 4500493 (N.D. Ala. Aug. 5, 2020);United States ex rel. Gohil v. Sanofi U.S. Servs. Inc., No. 02-cv-2964, 2020 WL 4260797 (E.D. Pa. July 24, 2020);United States ex rel. Fzco v. Supreme Foodservice GmbH, No. 17-cv-1290-RDA-JFA, 2020 WL 4579458 (E.D. Va. July 8, 2020);United States ex rel. Garrett v. Kootenai Hosp. Dist., No. 17-cv-314-CWD, 2020 WL 3268277 (D. Idaho June 17, 2020);United States ex rel. Johnson v. Golden Gate Nat'l Senior Care, LLC, No. 08-cv-1194-DWF-HB, 2020 WL 1915612 (D. Minn. Apr. 20, 2020);United States ex rel. Foreman v. AECOM, 454 F. Supp. 3d 254 (S.D.N.Y. 2020);United States ex rel. Holzner v. DaVita Inc., No. 18-cv-1250-JLS-DFM, 2020 WL 3064771 (C.D. Cal.Apr. 10, 2020);United States ex rel. Zissa v. Santa Barbara Cty.Alcohol, Drug and Mental Health Servs., No. 14-cv-6891-DMG-AGR, 2020 WL 4369629 (C.D. Cal. Mar. 25, 2020);United States ex rel. Scott v. Pac. Architects & Eng'rs, Inc., No. 13-cv-1844-CKK, 2020 WL 224504 (D.D.C. Jan. 15, 2020);United States ex rel. Campbell v. KIC Dev., LLC, No. 18-cv-193-KC, 2019 WL 6884485 (W.D. Tex. Dec. 10, 2019);United States ex rel. Polansky v. Exec. Health Res., Inc., 422 F. Supp. 3d 916 (E.D. Pa. 2019);United States ex rel. Lewis v. Cal. Inst. of Tech., No. 18-cv-5964-CAS, 2019 WL 5595046 (C.D. Cal. Oct. 28, 2019);United States ex rel. Bonzani v. United Techs. Corp., No. 16-cv-1730-JCH, 2019 WL 5394577 (D. Conn. Oct. 22, 2019);United States ex rel. Marsteller v. Tilton, No. 13-cv-830-AKK, 2019 WL 4749986 (N.D. Ala. Sept. 30, 2019);United States ex rel. Longo v. Wheeling Hosp., Inc., No. 19-cv-192, 2019 WL 4478843 (N.D.W. Va. Sept. 18, 2019);United States ex rel. Raffington v. Bon Secours Health Sys., Inc., 405 F. Supp. 3d 549 (S.D.N.Y. 2019);United States ex rel. MacDowell v. Synnex Corp., No. 19-cv-173-WHA, 2019 WL 4345951 (N.D. Cal. Sept. 12, 2019);United States ex rel. Tra v. Fesen, 403 F. Supp. 3d 949 (D. Kan. 2019);United States ex rel. Ling v. City of Los Angeles, 389 F. Supp. 3d 744 (C.D. Cal. 2019).

[3] Id. at 1999-2000.

[4] Id. at 2002-03.

[5] Id. at 2003.

[6] Id. at 2004 n.6.

[7] See, e.g., Statement of Interest of the United States in Connection with Relator's Rule 59(e) Motion to Alter Judgment, United States ex rel. Kolchinsky v. Moody's Corp., No. 12-cv-01399-WHP (S.D.N.Y. May 8, 2017).

[8] United States' Statement of Interest Regarding Defendants' Motion to Dismiss at 2, United States ex rel. JKJ Partnership 2011 v. Sanofi-Aventis U.S. LLC, No. 11-cv-06476-FLW-TJB (D.N.J. Apr. 2, 2021).

[9] Id. at 2-3.

[10] Three outlier cases were excluded from this analysis.

[11] Cases decided by magistrate judges were excluded from this analysis.

[12] False Claims Act Amendments Act of 2021, S. 2428, 117th Cong. (2021).

[13] Id. (manager's amendment approved by the Senate Judiciary Committee on October 28, 2021).

[14] Press Release, Chuck Grassley, Senator, Prepared Statement of Senator Chuck Grassley at False Claims Act Hearing (Feb. 27, 2008), https://www.grassley.senate.gov/news/news-releases/prepared-statement-senator-chuck-grassley-false-claims-act-hearing.

[15] Jaime L.M. Jones, Brenna Jenny & Meredith Greene, "Come Down with a Sledgehammer": Sen. Grassley and Acting Civil Division Head Boynton Discuss FCA Priorities, Sidley Austin False Claims Act Blog (Feb. 18, 2021), https://fcablog.sidley.com/come-down-with-a-sledgehammer-sen-grassley-and-acting-civil-division-head-boynton-discuss-fca-priorities/.