Beware the False Claims Act, Whistleblowers, and the Importance of Internal Investigations

By Craig Denney and Greg Brower

Companies that do business with the federal government must be cognizant of potential liability under the False Claims Act. Civil litigation may be inevitable at times as a result of occasional business disputes with suppliers, customers, former employees, or competitors. Companies, however, should be particularly cautious about litigation with the United States as the adverse party. The reasons may be obvious since the federal government has unlimited resources for litigation. The financial consequences under the FCA can be devastating to business operations. As such, companies should be familiar with the FCA, have internal controls and policies, and be prepared to promptly investigate allegations of wrongdoing when they arise. This is simply the cost of doing business with the federal government.

FCA investigations and enforcement actions are frequent and have wide reach in most industries, including defense, energy, transportation, healthcare, and gaming. Any business with a government contract or that is receiving government funds as part of a project can have exposure under the FCA if wrongdoing occurs. For example, the Patient Protection and Affordable Care Act (colloquially known as "ObamaCare") will result in the creation of health insurance exchanges that will offer insurance options and receive subsidies from the federal government for payment of premiums. Congress has ensured that the FCA will apply to fraud involving federal payments to such exchanges.

Overview of the False Claims Act

The FCA was created during the Civil War because Congress was concerned that suppliers of goods to the Union Army were committing fraud on the military. The FCA provides that anyone who knowingly submits false claims to the government is liable for treble the government's damages plus a penalty of $5,000 to $10,000 for each false claim.

Under this statute, there is liability for any person who knowingly submits a false claim to the federal government, causes another to submit a false claim, or knowingly makes a false statement to induce payment of a false claim by the government. A person does not violate the FCA by merely submitting a false claim to the government (i.e. negligence). A person must have submitted, or caused the submission of, the false claim (or statement) with knowledge of the falsity. Knowledge of false information is defined as:

(1) actual knowledge,

(2) deliberate ignorance of the truth or falsity of the information, or

(3) reckless disregard of the truth or falsity of the information.

A claim under the FCA is a demand for money or property made directly to the federal government or to a contractor, grantee, or other recipient if the money is to be spent on the government's behalf and if the government provides any of the money demanded or if it will reimburse the contractor or grantee.

The FCA allows private persons (known as "relators") to file suit for violations on behalf of the government. Lawsuits filed by individuals in this manner are known as "qui tam" actions. Such lawsuits are filed in court under seal, and are served on the U.S. Attorney in the district where the action was filed and also on the U.S. Attorney General. The federal government must then investigate the allegations in the complaint, and then notify the court that it is proceeding with the action (generally referred to as "intervening" in the action) or declining to take over the action, in which case the relator can proceed with the action on its own.

If the government intervenes in the qui tam action, it has the primary responsibility for prosecuting the action. When this occurs, the relator now has the proverbial 900-pound gorilla on its side of the litigation. Companies obviously do not want to be the defendant on the wrong side of FCA litigation due to the potential financial exposure.

Whistleblower Financial Incentives

Central to the FCA is the financial incentive for private persons to report wrongdoing (or alleged wrongdoing). Often, the purported whistleblower is a former employee of the company. If the government intervenes in the qui tam action, the relator is entitled to receive between 15 to 25 percent of the amount recovered by the government.

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If the government declines to intervene in the action, the relator's share is increased to 25 to 30 percent. If DOJ intervenes and a financial settlement is negotiated, the relator stands to receive significant compensation and payment of its attorney's fees. Under certain circumstances, the relator's share may be reduced to no more than 10 percent.

If the relator planned and initiated the fraud, the court may reduce the award. However, in one recent, highly publicized DOJ investigation of UBS Bank for tax evasion of offshore accounts in Switzerland, the purported whistleblower, Bradley Birkenfeld, actually participated in the wrongdoing, was prosecuted criminally, went to prison, and still received over $100 million from the government's recovery for his report of the UBS false claims. The relator's share is paid by the government out of the payment received by the government from the defendant. If a qui tam action is successful, the relator is also entitled to be reimbursed by the defendant for legal fees and other expenses of the action.

CIVIL INVESTIGATIVE DEMANDS

When the Fraud Division of the Department of Justice (along with the U.S. Attorney's Office in the district where the action is filed) conducts the investigation of the FCA allegations, DOJ may issue civil investigative demands for testimony and documents. This allows DOJ to conduct, in essence, a hybrid of civil discovery and criminal investigation of the false claims. Unlike a traditional deposition in civil litigation, however, CIDs do not allow the defendant to be present to cross-examine the purported whistleblower or other witnesses that DOJ interviews and examines under oath.

INTERNAL INVESTIGATIONS

A company under an FCA investigation should strongly consider conducting its own internal investigation of the allegations rather than simply wait and see what DOJ determines. Due to the fact that a company is not entitled to be present for CID oral examinations of witnesses, it may be beneficial for the company to gather all the facts and interview witnesses with the aid of outside counsel. This will enable the company to be objective in gathering facts and proactive in efforts to negotiate with DOJ on the allegations and merits of the alleged false claims. The FCA investigation and litigation may last as long as three to five years before settlement or trial. If wrongdoing is uncovered in the investigation, the company may opt to disclose the results of the internal investigation to the federal government with the hope of persuading DOJ not to intervene in the relator's FCA complaint and also to avoid the imposition of treble damageWWs.

Companies that conduct business with the federal government should understand the FCA and have a program in place to respond to and investigate whistleblower complaints when they arise. ●