Government Contracts Advisory

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New District Court Decision Contributes to Uncertainty Regarding Use of Implied Certification Theory in False Claims Act Cases

Introduction

On February 8, 2011, the U.S. District Court for the Eastern District of Texas issued an opinion in *United States v. Kellogg Brown & Root*, No. 1:04-CV-2 (E.D. Tex. Feb. 8, 2011) ("*KBR*"). This opinion addresses, among other things, False Claims Act ("FCA") and Anti-Kickback Act ("AKA") issues of significance to government contractors. With respect to the FCA, the court held that, to state a valid FCA claim against a contractor based upon the alleged acceptance of kickbacks by one of the contractor's employees in violation of the AKA, the government was required to allege: (1) that the contractor expressly certified compliance with the AKA and that certified compliance was a condition of payment; and (2) that the employee in question was acting for the benefit of the corporation when accepting the purported kickbacks. Similarly, the court held that corporate liability under the AKA itself was limited to the amount of the alleged kickback unless the government could plead and show that the employee accepting the alleged kickbacks was "acting for the corporation's benefit."

Discussion

False Claims Act

Alleged FCA Violation Based Upon Non-Compliance With Statute
The government argued that KBR's continued billing of the government at the same time KBR had, allegedly in violation of the AKA, accepted kickbacks in connection with subcontracts issued under its prime contract, necessarily gave rise to an FCA claim. The court rejected this *per se* approach to FCA liability, however, and by the court's rationale, this rejection arguably would apply to any attempt by the government or a *qui tam* relator to base FCA liability on mere non-compliance with a statute, regulation, or contract provision. In this regard, the court found that "a false claim is stated when it involves a knowingly false ***certification of compliance*** with a statute or regulation and that certification is a prerequisite to payment of the asserted claim." *KBR*, slip op. at 15 (emphasis added). The court went on to find that the government, in its complaint, had not alleged: (1) that KBR had made any certification of compliance with the AKA; or (2) that compliance with the AKA was a condition of payment under KBR's contract with the government. *Id.* at 15-16. Moreover, the court found that the government's complaint was deficient because it failed to allege any facts indicating that KBR actually passed along the costs associated with the alleged kickbacks to the government. *Id.* at 16. As a result of these identified infirmities, the court dismissed the government's complaint, although allowing the government the opportunity to refile to correct

them.

Vicarious Liability

The FCA requires that a defendant *knowingly* make false claims for payment to the government. *See* 31 U.S.C. § 3729(a). KBR moved to dismiss the government's FCA claim for failing to adequately plead this element of the FCA, but the government argued that the knowledge of KBR's employees regarding the alleged kickbacks could be imputed to the corporation, thus giving rise to vicarious liability for the corporation.

The court found the government's allegations to be insufficient, noting that the complaint did not allege facts indicating that KBR employees knew the cost of the kickbacks were included in KBR's invoices to the government or that KBR knowingly submitted inflated claims to the government. Furthermore, the complaint did not allege that KBR employees were acting for the benefit of the corporation when accepting the purported kickbacks or that the corporation even benefitted from the kickbacks. The court noted that while KBR may have violated the terms of the contract by failing to ensure its employees complied with relevant statutes, "contractual non-compliance does not suffice to state an FCA claim." *Id*. at 19 (citing *United States v. Southland Mgmt. Corp.,* 326 F.3d 669 (5th Cir. 2003)). The court granted KBR's motion to dismiss the FCA claim on this basis as well.

Anti-Kickback Act

The government argued that KBR knowingly violated the AKA under 41 U.S.C. § 55(a)(1)--thus giving rise to the potential of a civil penalty of twice the amount of each kickback plus not more than $10,000 for each occurrence of the prohibited conduct--because KBR employees were directly involved in the alleged fraud and their knowledge may be imputed to the corporation. KBR argued that the complaint was improperly pled because, under § 55(a)(1), a prime contractor cannot be held liable for a knowing violation based solely on the acts of its employees, without more. The court found that the plain language of § 55(a) indicates that vicarious liability of a corporation, based solely upon the acts of its employees and not its own knowledge, is subject only to the limited penalty contemplated in § 55(a)(2), and not the more significant penalties set forth in § 55(a)(1). *Id.* at 23. Similar to the discussion of vicarious liability under the FCA, the court dismissed the AKA claim, finding the government insufficiently alleged that the KBR employees at issue were acting for the corporation's benefit. Thus, imputation of knowledge from the employees to the corporation was inappropriate.

Implications and Predictions

This decision comes on the heels of the U.S. Court of Appeals for the District of Columbia Circuit's December 3, 2010 decision in *United States v. Science Applications Int'l Corp*, (Slip. Op. No. 09-5385) ("*SAIC*"). As discussed in our **previous alert** on that case, the *SAIC* decision was significant because the court embraced a relatively broad implied certification theory of civil FCA liability, rejecting the argument that compliance with the contract provision at issue had to have been an "express condition" of payment in order for non-compliance with that provision to serve as the basis for FCA liability. In addition, and more positively for contractors, the *SAIC* court held that a corporate entity may not be found to possess the requisite knowledge for an FCA violation on the basis of a "collective knowledge" theory that pools the knowledge of all of the corporate entity's employees.

The *KBR* court's ruling regarding the need for an express certification

of compliance to state a valid FCA claim is at odds with the ruling in *SAIC*, which found that liability could attach absent any such certification. Thus, the *KBR* decision contributes to the "unsettled" state of the law regarding implied certification, noted by the D.C. Circuit in *SAIC*. And, as we pointed out in our client alert, the uncertainty in this area could increase the likelihood that the Supreme Court will grant *certiorari* in a case presenting the implied certification issue. It also could prompt calls for legislative action, although such action remains unlikely at this time.

Despite their differences on the need for express certification, the *SAIC* and *KBR* cases both show the courts' willingness to impose strict requirements on the government and *qui tam* relators with respect to demonstrating knowledge by corporate defendants under the FCA. Both cases rejected broad theories to show the requisite knowledge. Indeed, the *KBR* case may go even further in this regard than *SAIC*. In *SAIC*, the issue was whether the knowledge of a number of employees could be combined to satisfy the FCA knowledge requirement. In *KBR*, however, the court suggests that, even if a single employee has all of the requisite knowledge, that would not be enough if he is not acting for the benefit of the corporation.