IN THE

# United States Court of Appeals

**FOR THE SECOND CIRCUIT**

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PAUL BISHOP, ROBERT KRAUS, UNITED STATES OF AMERICA,
EX REL PAUL BISHOP, EX REL ROBERT KRAUS,

*Plaintiffs-Appellants,*

STATE OF NEW YORK, EX REL PAUL BISHOP, EX REL ROBERT KRAUS, STATE OF DELAWARE, EX REL PAUL BISHOP, EX REL ROBERT KRAUS, DISTRICT OF COLUMBIA, EX REL PAUL BISHOP, EX REL ROBERT KRAUS, STATE OF FLORIDA,

(*Caption continued on inside cover*)

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ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NEW YORK

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**BRIEF OF TAXPAYERS AGAINST FRAUD EDUCATION FUND AS *AMICUS CURIAE* IN SUPPORT OF APPELLANTS**

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*Plaintiffs,*

—against—

WELLS FARGO & COMPANY, WELLS FARGO BANK, N.A.,

*Defendants-Appellees.*

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**TO THE HONORABLE UNITED STATES COURT OF APPEALS:**

Pursuant to Fed. R. App. P. 29, Taxpayers Against Fraud Education Fund respectfully submits this brief as *Amicus Curiae* in support of the Appellants Paul Bishop and Robert Kraus.[1] A Motion for Leave to File has been submitted contemporaneously herewith, and this brief is subject to that Motion. Taxpayers Against Fraud Education Fund supports Appellants for the reasons set forth below.

## I. STATEMENT OF INTEREST

### A. Taxpayers Against Fraud Education Fund

Taxpayers Against Fraud Education Fund ("TAFEF") is a nonprofit, public interest organization dedicated to combating fraud against the government and protecting public resources through public-private partnerships. TAFEF is committed to preserving effective anti-fraud legislation at the federal and state levels. The organization has worked to publicize the *qui tam* provisions of the False Claims Act ("FCA"), has participated in litigation as a *qui tam* relator and as an *amicus curiae*, and has provided testimony to Congress about ways to improve the False Claims Act. TAFEF has a strong interest in ensuring proper interpretation and application of the False Claims Act. TAFEF is supported by

[1] Pursuant to Federal Rule of Appellate Procedure 29(c), Taxpayers Against Fraud Education Fund ("TAFEF") states that it is a corporation organized under § 501(c)(3) of the Internal Revenue Code. It has no parent corporation and no stock owned by a publicly owned company. TAFEF represents no parties in this matter and has no pecuniary interest in its outcome. Counsel for TAFEF authored this brief in its entirety. TAFEF has an institutional interest in the effectiveness and correct interpretation of the federal False Claims Act.

whistleblowers and their counsel, by membership dues and fees, and by private donations. TAFEF is the 501(c)(3) arm of Taxpayers Against Fraud, which was founded in 1986.

### B. The Importance of the Outcome of this Litigation

The FCA imposes liability on any person who (A) "knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval;" or (B) "knowingly makes, uses, or causes to be made or used, a false record or statement *material to a false or fraudulent claim*."[2] The FCA reaches "all fraudulent attempts to cause the Government to pay [out] sums of money or to deliver property or services."[3] The FCA was written "expansively, meaning 'to reach all types of fraud, without qualification, that might result in financial loss to the government.'"[4]

This Circuit has expressed concern with how to cabin liability in cases where the program terms at issue are tangential or possibly irrelevant to payment, and in doing so began to limit the availability of the "implied certification" theory of FCA liability to those cases where the underlying contract, statute, or regulation

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[2] 31 U.S.C. § 3729(a)(1)(A)-(B)(emphasis added).
[3] S. Rep. No. 99-345, at 9 (1986), reprinted in 1986 U.S.C.C.A.N. 5266, 5274.
[4] *United States ex rel. Hutcheson v. Blackstone Medical, Inc.*, 647 F.3d 377, 392 (1st Cir. 2011), *cert. denied*, 132 S. Ct. 815 (2011) (*quoting Cook Cnty. v. United States ex rel. Chandler*, 538 U.S. 119, 129 (2003) and *United States v. Neifert-White Co.*, 390 U.S. 228, 232 (1968)).

expressly stated that compliance was a prerequisite to payment.[5] However, other circuit court opinions have addressed how courts should analyze liability for false or fraudulent claims under the FCA, and have rejected judicially-constructed approaches that may inappropriately cabin the types of conduct the statute was designed to reach.[6] These opinions make clear that the existing precepts of the FCA – knowledge and materiality – provide the appropriate means to limit the scope of liability under the statute, and that courts should not substitute artificial categories or "magic word" tests to determine whether a claim is false.[7] However, just as the evolution of categories such as "false certification" and "legal falsity" became an artificial means to limit FCA liability, the categories of "conditions of payment" and "conditions of participation" are equally unavailing and merely offer new artificial boxes around FCA liability. The use and application of these forced classifications impacts the FCA's effectiveness in addressing rampant fraud.

The sole purpose of TAFEF's brief as *amicus curiae* is to address the proper legal analysis to determine falsity and materiality under the FCA. TAFEF leaves any other disputed issues to the parties.

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[5] *United States ex rel. Mikes v. Straus*, 274 F.3d 687, 700 (2d Cir. 2001); *see also United States ex rel. Kirk v. Schindler Elevator Corp*., 601 F.3d 94, 114, n.15 (2nd Cir. Apr. 6, 2010), *rev. & remanded on other grounds sub nom. Schindler Elevator Corp. v. United States ex rel. Kirk*, 131 S. Ct. 1885 (2011).

[6] *United States ex rel. Hutcheson*, 647 F.3d 377; *New York v. Amgen*, 652 F.3d 103, 109-110 (1st Cir. 2011); see also *United States ex rel. Jones v. Brigham & Women's Hosp.*, 678 F.3d 72, 85-86 (1st Cir. 2012).

[7] *See e.g., Hutcheson*, 647 F.3d at 388.

### C. Nature of the Action

Plaintiffs-Appellants have alleged that beginning in 2001, executives at Wachovia Bank used sham accounting practices to hide low-grade, toxic assets and obscure the fact that the bank was severely undercapitalized.[8] Wachovia's protocols were allegedly undetectable to outsiders evaluating the bank's finances and management practices.[9]

Wachovia allegedly appeared on paper to be sufficiently capitalized and financially healthy, and Wachovia was turning a profit. As alleged, Wachovia was actually severely undercapitalized and on the verge of collapse.[10] During the financial crisis that began in 2007-2008, many of the nation's largest financial institutions could not obtain short-term funding, which was frequently used by banks to finance their day-to-day operations. The United States government stepped in and bailed them out, using taxpayer dollars.[11]

Wachovia was a recipient of the government financial assistance and received billions of dollars in short-term funding from the Federal Reserve.[12] Wachovia allegedly falsely certified that it was in compliance with the relevant banking laws and regulations and was financially secure in order to borrow money

[8] *U.S. ex rel. Kraus v. Wells Fargo & Co.*, No. 11 CIV. 5457 BMC, 2015 WL 4509036, at *1-2 (E.D.N.Y. July 24, 2015).
[9] *Id.*
[10] *Id.*
[11] *Id.* at *2.
[12] *Id.*

at a highly subsidized interest rate from the Federal Reserve -- putting taxpayer funds at risk.[13] In reality, the Appellants alleged, Wachovia's actions violated numerous banking laws and regulations, and as a result of Wachovia submitting fraudulent balance sheets that did not disclose the bank's financial instability, the amount that Wachovia was required to repay to the Federal Reserve was significantly less than the bank would have been required to pay if the Federal Reserve had known the truth about Wachovia's financial state.[14]

According to the Appellants, each time Wachovia borrowed funds from the Federal Reserve based on false statements regarding its true financial condition, the bank certified that it was not violating any laws or regulations that could adversely affect its ability to perform the terms of the bank's lending agreement with the Federal Reserve, and that no document submitted to the Federal Reserve in connection with the lending agreement contained misstatements. As alleged, these statements were material to the Federal Reserve's decision to permit Wachovia to borrow funds.[15]

## II. ARGUMENT

The District Court below granted the Motion to Dismiss Relator's Third Amended Complaint, finding that Wachovia could not be held liable under the

[13] *Id.* at *1-2.
[14] *Id.*
[15] *Id.* at *6

FCA for falsely certifying its compliance with the regulations at issue because those regulations were too "tenuous" to the payment of monies by federal entities.[16]

The District Court rejected the Appellants' argument that when a defendant falsely certifies compliance with the rules and regulations of a program, it is disqualified from submitting the very claims that form the basis for payment. As the District Court noted in its opinion:

> In the most basic sense, this claim is most appropriate where the statute or regulation of which the defendant is alleged to be in violation is the same statute that governs eligibility for the benefit that is the basis for the FCA claim. That is not what is alleged here. In a case like this one, it is not the Lending Agreement that would have to condition payment on compliance with laws and regulation to give rise to FCA liability; it is the laws and regulations themselves. By way of illustration: If, for example, relators were alleging that defendants' underlying "control fraud" was among other things a violation of the Sarbanes–Oxley Act (as they do allege), *and* it was the case (or alleged) that the Sarbanes–Oxley Act *itself* governed eligibility for the Federal Reserve's primary credit program (and of course it does no such thing), only then would knowing violation of Sarbanes–Oxley be an implied false certification at the discount window.
>
> Here, there quite simply is no allegation (nor could there be) that any of the many alleged violations of laws and regulations that took place

[16] *But see id.*, at *3 (finding that there were claims made and payments received consistent with the FCA, and stating "[a]s a threshold matter, relators allege that defendants 'received payments from the Federal Entities [including the Federal Reserve and FHLBs] by drawing advances and/or obtaining guarantees in connection with one or more of the Federal Programs,' and *defendants do not appear to dispute that this allegation is sufficient* to satisfy the requirement that in each instance defendants "made a claim" and were "seeking payment" for purposes of FCA liability." (emphasis added).

> at the defendant banks was ever a violation of a statute that governed eligibility for the primary credit program. For that reason, an implied legally false certification claim is misplaced on the facts alleged in this case.[17]

Applying this distinction, the District Court determined that the language of the regulations did not identify the requirements at issue as a "condition of payment" and, as such, FCA liability was precluded. "[I]t cannot be said that there has been a misrepresentation made *to* the agency *in connection with* the payment."[18]

*Amicus* TAFEF disagrees with this approach; it is not necessary to distinguish between conditions of payment versus conditions of participation to determine whether a claim is materially false within the meaning of the FCA. Rather, TAFEF asserts that courts properly evaluate liability under the FCA by looking to whether the defendant has knowingly violated conditions that are material to the payment of the claim. This Court has recently held as such:

> Under the Act as currently in force, "the term 'material' means having a natural tendency to influence, or be capable of influencing, the payment or receipt of money or property." *Id.* § 3729(b)(4); *see also Neder v. United States*, 527 U.S. 1, 16, 119 S.Ct. 1827, 144 L.Ed.2d 35 (1999) ("In *87 general, a false statement is material if it has a natural tendency to influence, or [is] capable of influencing, the decision of the decision making body to which it was addressed." (brackets in original; internal quotation marks omitted) (criminal fraud case)).[19]

This evaluation is not dependent on express statements in an underlying

[17] *Id.* at *6.
[18] *Id.* at *8.
[19] *U.S. ex rel. Feldman v. van Gorp*, 697 F.3d 78, 86-87 (2d Cir. 2012).

contract, statute, or regulation. Rather, the analysis should center on whether the requirement at issue has a material nexus to payment, in the context of all the extrinsic evidence (not just the express words of the statute, contract, or regulation).[20] In essence, the contextual evidence must establish a failure to comply with a requirement that would be capable of affecting the Government's decision to pay the claim.[21]

### A. Other Circuit Courts Have Already Rejected Artificial Categories

#### 1. Express and Implied Certification

The First Circuit in *Hutcheson* found that categorical limitations on falsity, such as express or implied certification, improperly restrict the scope of the FCA and "obscure and distort" the FCA's requirements, stating:

> Courts have created these categories in an effort to clarify how different behaviors can give rise to a false or fraudulent claim. Judicially-created categories sometimes can help carry out a statute's requirements, but they can also create artificial barriers that obscure and distort those requirements. The text of the FCA does not refer to "factually false" or "legally false" claims, nor does it refer to "express certification" or "implied certification." Indeed, it does not refer to "certification" at all. In light of this, and our view that these categories may do more to obscure than clarify the issues before us, we do not employ them here.[22]

Following the plain text of the FCA, that court correctly concluded that "[t]he text of the FCA and our case law make clear that liability cannot arise under the FCA

[20] *Hutcheson*, 647 F.3d at 387-88; *Amgen*, 652 F.3d at 110-11.
[21] *Hutcheson*, 647 F.3d at 393-94; *Jones*, 678 F.3d at 94-95.
[22] 647 F.3d at 385-86.

unless a defendant acted knowingly and the claim's defect is material."[23]

The First Circuit closely followed the analysis of the D.C. Circuit in *United States v. Science Applications International Corporation*, holding that non-compliance with contract terms may give rise to FCA liability, even if the contract does not specify that compliance with the contract term is a condition of payment.[24] In *SAIC*, the court rejected the defendant's argument that legal preconditions of payment must be expressly designated, holding that "nothing in the statute's language specifically requires such a rule," and that adopting one "would foreclose FCA liability in situations that Congress intended to fall within the Act's scope."[25] Rather, the D.C. Circuit specified, the statute's reach is limited through "the Act's materiality and scienter requirements."[26]

Similarly, in *Amgen*, the First Circuit made clear that it had rejected conceptual divisions between (1) legal and factual falsity and (2) express and implied certification; and more specifically, had rejected the notion that "a claim can only be impliedly false or fraudulent for non-compliance with a legal condition of payment if that condition is expressly stated in a statute or regulation."[27] Instead, the court confirmed the FCA's materiality and scienter requirements

[23] *Id.* at 388.
[24] 626 F.3d 1257, 1269 (D.C. Cir. 2010).
[25] *Id.* at 1268.
[26] *Id.* at 1270.
[27] 652 F.3d at 110.

appropriately "cabin the breadth of the phrase 'false or fraudulent.'"[28] These opinions demonstrate that the framework announced in *Hutcheson* is both growing in acceptance and is more consistent with the plain-text intended scope of the FCA.

Thus, FCA liability is not anchored to whether the drafter of a contract, statute, or regulation used talismanic words to denominate "conditions of payment," but rather whether the condition at issue is material to the payment decision based on the contextual evidence.

### 2. "Conditions of Payment" and "Conditions of Participation"

Where FCA liability is premised on the violation of a statute, regulation, or contract provision, FCA liability attaches where a failure to comply has the potential to affect entitlement to payment. Thus, the inquiry is whether an appropriate nexus is established between compliance with that statute, regulation, or contract provision, and defendant's claim for payment.

Efforts to articulate this nexus has led to a long line of authority that swings between cases that essentially evaluate the materiality of the relationship between the underlying violation in the context of the affected program and cases that require an express statement. Whether called "certification," "condition of payment," materiality, or something else, *Amicus* TAFEF submits that an express

[28] *See id*. *See also Jones*, 687 F.3d at 387-88 ("FCA liability continues to be circumscribed by 'strict enforcement of the Act's materiality and scienter requirements,'" *quoting SAIC*, 626 F.3d at 1280).

statement requirement under any rubric is incorrect. The statute contains no such requirement and a "one size fits all" standard is simply ill-fit for analyzing misrepresentations and fraud – conduct which, by its nature, is context-specific and often involves looking for a loophole. The courts are well-suited to review the extrinsic evidence in the context of a government program and determine whether a program requirement is material to payment of a claim.

**a. From Certification to Condition of Payment**

Many courts, including this one, established the nexus to payment using the theory of "false certification." This construct required an affirmative false certification of compliance with government program terms in order to render a defendant liable under the FCA. The theory evolved to include so-called "implied certification," which referred to claims that reflected violations of core program terms, but where there was no express statement of compliance; rather, the claims "represented an implied certification . . . of [defendant's] continuing adherence to the requirements for participation in the . . . program."[29]

Concerned with how to cabin liability in cases where the program terms are tangential or irrelevant to payment, some courts, including this Circuit, began to limit the availability of "implied certification" to those cases where the underlying

[29] *Ab-Tech Constr., Inc. v. United States*, 31 Fed. Cl. 429, 434 (Fed. Cl. 1994); *see also United States ex rel. Lemmon v. Envirocare of Utah, Inc.*, 614 F.3d 1163, 1169 (10th Cir. 2010).

contract, statute, or regulation expressly stated that compliance was a prerequisite to payment.[30]

Following the narrowing demanded by *Mikes* and its progeny, and Congress's amendment of the FCA itself to clarify that false certification of a material requirement was always the key to analysis of whether FCA liability attached, the pendulum swung again, and this type of talismanic, or "magic word," requirement has now been rejected by other circuits.[31] As made clear by those decisions, imposing an express words requirement inappropriately narrows FCA liability such that it would not reach situations plainly contemplated by the statute and instead would "create artificial barriers" that obscure the FCA's requirements.[32]

As the jurisprudence on this topic has grown, the nexus between compliance with a contract, statute, or regulation and the claim is no longer described narrowly as "certification" but instead as "condition of payment." This is consistent with the long line of authority holding that knowing submission of claims resulting from

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[30] *United States ex rel. Mikes v. Straus*, 274 F.3d 687, 700 (2d Cir. 2001); *see also United States ex rel. Kirk v. Schindler Elevator Corp*., 601 F.3d 94, 114, n.15 (2nd Cir. Apr. 6, 2010), *rev. & remanded on other grounds sub nom. Schindler Elevator Corp. v. United States ex rel. Kirk*, 131 S. Ct. 1885 (2011).
[31] *E.g.*, *Hutcheson*, 647 F.3d at 386-88; *SAIC*, 626 F.3d at 1269; *United States ex rel. Hendow v. Univ. of Phoenix*, 461 F. 3d 1166, 1176 (9th Cir. 2006).
[32] *Hutcheson*, 647 F.3d at 385-86.

violation of a material condition of payment creates FCA liability.[33]

However, faced with concerns about how to determine liability in cases where program terms are voluminous and, in some cases, contain terms that are tangential to payment, some courts have created a distinction between "conditions of payment" and "conditions of participation." While this phraseology may be helpful to differentiate between terms of an underlying statute or regulation that are too tangential to payment to render the claim false, it can also operate to obscure and distort the scope of FCA liability. Indeed, because government regulations may not expressly use the term "condition of payment," rejecting liability simply because a regulation did not use the magic words of materiality would limit the FCA's reach such that it did not address situations that Congress plainly intended it to cover.

Courts have correctly recognized that whether a requirement is a condition of payment or participation is often "a distinction without a difference."[34] In many

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[33] *E.g.*, *Hutcheson*, 647 F.3d at 379; *United States v. Rogan*, 459 F. Supp. 2d 692, 714-17 (N.D. Ill. 2006), *aff'd* 517 F.3d 449 (7th Cir. 2008); *McNutt ex rel. United States v. Haleyville Medical Supplies, Inc.*, 423 F.3d 1256, 1259 (11th Cir. 2005).

[34] *Hendow*, 461 F.3d at 1176; *see also Conner*, 543 F.3d at 1222[34] (*quoting Hendow* and explaining that "some regulations or statutes may be so integral to the government's payment decision as to make any divide between conditions of participation and conditions of payment a 'distinction without a difference'"); *United States ex rel. Tyson v. Amerigroup Ill., Inc.*, 488 F. Supp. 2d 719, 726 (N.D. Ill. 2007) (*quoting Hendow* and declaring that "'[I]f we held that conditions of participation were not conditions of payment, there would be no conditions of payment at all'").

cases, it defies logic that conditions of participation are relegated to an artificial box separated from conditions of payment, when establishing eligibility to participate in a government-funded program is necessarily the first condition that must be met before a claim for payment under that program can be paid.

The discussion of the delineation between these two categories has led to the pendulum swinging back again to an express words requirement. Rather than using the phraseology "condition of payment" or "condition of participation" to evaluate the relationship between the underlying program term and the government's payment decision, some courts have moved to examining regulations for the use of the words "condition of payment" when describing a requirement.[35] Therefore, the risk that the violation of *any* law – no matter how disconnected to payment – could serve as a basis for FCA liability is misplaced and should not function as a rationale for imposition of artificial constrictions on the statute. Courts, as noted above, are more than capable of determining materiality to payment, so the fears of a "slippery slope" are unfounded.

*Amicus* TAFEF suggests that this return to an express-words analysis that

[35] *E.g., Virginia ex rel. Hunter Labs. v. Quest Diagnostics, Inc.*, No. 1:13–CV–1129, 2014 WL 1928211, at *10 (E.D. Va. May 13, 2014) ("The name of the Agreement alone—the Virginia Medicaid Independent Laboratory Participation Agreement … does not suggest that the Commonwealth would have withheld payment for work already performed"); *United States ex rel. Hobbs v. MedQuest Assoc., Inc.*, 711 F.3d 707, 715 (6th Cir. 2013) (finding supervising-physician regulations are not conditions of payment).

looks to determine whether the requirement is characterized as a "condition of payment" or a "condition of participation" is a move back to relying upon artificial categories. The inappropriate narrowing it effectuates is plain: government agencies have written contracts and program requirements for decades without judicial constructs in mind, and the fact that certain words are not used makes core program requirements no less related to payment. An express words rubric would render many such requirements unenforceable under the FCA, creating an enormous loophole for fraud to go unchecked.[36]

As described more fully below, *Amicus* TAFEF asserts that analysis of FCA liability is more appropriately constrained by the principles of knowledge and materiality, not more artificial boxes.

**b. Materiality and Condition of Payment**

While this Court has not yet specifically rejected the distinction between a "condition of payment" and a "condition of participation" for the purpose of evaluating liability under the FCA, other circuits have made clear that the analysis of whether a requirement is a "condition of payment" is not limited to an

[36] *See SAIC*, 626 F.3d at 1268-69 ("[N]othing in the statute's language specifically requires such a rule, and we fear that adopting one would foreclose FCA liability in situations that Congress intended to fall within the Act's scope (internal citation omitted) . . . We decline to create such a counterintuitive gap in the FCA by imposing a legal requirement found nowhere in the statute's language").

evaluation of the express words of the statute or regulation.[37] Rather, the determination of whether "the claims at issue misrepresented compliance with a material precondition of payment" is a "fact-intensive and context-specific inquiry."[38] Moreover, while express language may certainly "'constitute dispositive evidence of materiality,' materiality may be established in other ways, 'such as through testimony demonstrating that both parties to the contract understood that payment was conditional on compliance with the requirement at issue.'"[39]

The District Court suggests that the materiality analysis is separate from whether a condition of payment exists. Indeed, it is the gap between those two concepts that appears to force a hyper-technical examination of the express words of the regulation for "condition of payment" language. TAFEF submits that the District Court's reading of the law is erroneous, and too limiting of the true breadth of the FCA as intended by Congress. While the other Circuits have, at times, employed a two-step analysis of first, whether there was a misrepresentation of compliance with a condition of payment, and second, whether the misrepresentation was material; they did not consistently employ an explicit two step analysis in all cases, or advocate that the identification of the initial

[37] *Hutcheson*, 647 F.3d at 388.
[38] *Amgen*, 652 F.3d at 110-11.
[39] *Hutcheson*, 647 F.3d at 394, *quoting SAIC*, 626 F.3d at 1269.

misrepresentation incorporated an express words analysis.[40] In the First Circuit in *Amgen*, for example, the court fluidly examined whether there was a misrepresentation of compliance with a material precondition of payment in various state Medicaid programs using a "fact-intensive and context-specific" analysis of the statutes, regulations, manuals, and provider agreements in each state.[41] There is no suggestion in prior cases that establishing that an underlying contractual, statutory, or regulatory term which was violated was "a condition of payment," and required meeting a stricter threshold than is necessary to establish that such a violation was material under the FCA. While an underlying condition, term, or requirement must be identified, there is no suggestion that a contract, statute, or regulation containing that condition must use specific words to denominate the requirement as "material" in order to support the existence of FCA liability.

Assessing whether the condition, term, or requirement at issue is a condition of payment is part of the analysis of whether the violation of a contractual, statutory, or regulatory provision is material to the government's payment decision. This Circuit has made clear that knowledge and materiality are the means by which the FCA limits the scope of liability for "false claims."[42] In order

[40] *E.g.*, *Amgen*, 652 F.3d at 111-16; *Jones*, 678 F.3d at 85-95.
[41] 652 F.3d at 11-116.
[42] See *Feldman*, supra at 92-93 regarding this Circuit's impression of the

to determine whether there has been a violation of a condition that is material to payment, it is incongruous to require that the determination be artificially truncated in two-steps with two different standards. Perforce, if courts require the express words "condition of payment" in order to support FCA liability, then the question of whether the violation was material to payment would be rendered superfluous in nearly all cases.

This is precisely in line with the analyses employed by numerous courts. The inquiry into whether the underlying condition or term (whether of a contract, statute, or regulation) is a condition of payment is a materiality analysis, *i.e.*, whether the requirement relates to "core terms" or "core eligibility" of the program,[43] the government's benefit of the bargain,[44] or "entitlement" to payment.[45]

Thus, a materiality analysis provides the dividing line between those requirements that are so integral to the program that a violation is capable of influencing the payment decision, and those where "noncompliance would not

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importance of materiality.

[43] *Ab-Tech*, 31 Fed. Cl. at 434 (referring to the concealment of "a fact vital to the integrity of the program" and "information critical to the decision to pay"); *United States v. Wells Fargo Bank, N.A.*, 972 F. Supp. 2d 593 (S.D.N.Y. 2013) (referring to "core eligibility requirements"); *United States v. TDC Mgmt. Corp.*, 288 F.3d 421, 426 (D.C. Cir. 2002) (referring to "core terms" of the contract).

[44] *E.g., SAIC*, 626 F.3d at 1271 ("Payment requests by a contractor who has violated minor contractual provisions that are merely ancillary to the parties' bargain are neither false nor fraudulent").

[45] *United States v. Bourseau*, 531 F.3d 1159, 1168 (9th Cir. 2008).

have influenced the government's decision to pay the claim" or were "tangential."[46] This definition of materiality has long been adopted by several circuit courts, and has been incorporated into the FCA itself.[47] It should be noted that materiality under the FCA is an objective standard and does not require a showing of actual reliance by the government.[48]

This is also consistent with the fact that not all frauds involve factual falsity *or* underlying contract or statutory terms. Some of the oldest cases interpreting false or fraudulent claims under the FCA "do not speak in terms of these newly created categories, which are not in the text of the FCA."[49] Rather:

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[46] *Mikes*, 274 F.3d at 697; *United States ex rel. Winkler v. BAE Sys.*, 957 F. Supp. 2d 856, 867 (E.D. Mich. 2013).

[47] 31 U.S.C. 3729(b)(4). *Hutcheson*, 647 F.3d at 394, *citing United States ex rel. Loughren v. Unum Group*, 613 F.3d 300, 307 (1st Cir. 2010); S. Rep. No. 111-10, at 10 ("material" means "having a natural tendency to influence, or being capable of influencing," the decision to pay).

[48] *See United States ex rel. Loughren v. Unum Group*, 613 F.3d 300, 309 (1st Cir. 2010) (confirming that a false statement is material where it "could have influenced" government's payment decision). There is an important distinction between having a "natural tendency to influence" and actually influencing a payment decision. The proper focus in evaluating materiality is on the "potential effect of the false statement when it is made, not on the actual effect of the false statement when it is discovered." *United States ex rel. Harrison v. Westinghouse Savannah River Co.*,352 F.3d 908, 916-17 (4th Cir. 2003). *See also United States ex rel. Feldman v. Van Gorp.*, 697 F.3d 78, 96 (2d Cir. 2012) (stating that materiality under the FCA "does not require evidence that a program officer relied upon the specific falsehoods proven"); *United States v. Rogan*, 517 F.3d 449, 552 (7th Cir. 2008) (rejecting the argument that the government must show it would actually have taken enforcement action if it had been aware of the falsity); *Longhi v. Lithium Power Techs.*, 575 F.3d 458, 470 (5th Cir. 2008).

[49] *Hutcheson* at 390.

> While *Bornstein*, *Rivera*, and *Scolnick* arguably involve misrepresentations of a strictly factual nature, *Hess* and *Murray & Sorenson* involve misrepresentations related to a legal status. As we held in *Murray & Sorenson*, "in *Hess* there was an implied false representation that the bids were competitive, and in this case there was an implied false representation that the bids were at a figure which the corporate defendant would have submitted in competition instead of at a somewhat higher figure" due to the tip. *Murray & Sorenson, 207 F.2d at 124*. These claims did not misstate a fact; they implied that the defendants had not engaged in certain illicit behaviors that would disqualify them from payment. Neither decision identified a statute, regulation, or certification as the basis of the legal precondition of payment the respective defendants had failed to meet.[50]

Categorical rules such as espoused by *Mikes* are at odds with the holdings of controlling decisions of other Circuits and the Supreme Court.[51] Additionally, this Circuit's holding in *Feldman* clearly demonstrates that fraudulent inducement cases, where a defendant has submitted a false statement to obtain a contract or benefit it was not entitled to, are alive and well.[52]

To force district courts to conduct a *Mikes* analysis after they've already determined that the falsity and materiality elements have been satisfied would

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[50] *Id.* at 390-391, *citing United States ex rel. Marcus v. Hess*, 317 U.S. 537 (1943) and *Murray & Sorenson v. United States*, 207 F.2d 119 (1st Cir. 1953) (other citations omitted).

[51] *Id.*

[52] *U.S. ex rel. Feldman v. van Gorp*, 697 F.3d 78, 91 (2d Cir. 2012) ("If the government made payment based on a false statement, then that is enough for liability in an FCA case, regardless of whether that false statement comes at the beginning of a contractual relationship or later. The only difference would be that liability begins when the false statement is made and relied upon, rather than at the beginning of the contractual relationship, as it would be in a fraudulent inducement case.")

waste judicial resources and would disregard the fact that the FCA now specifically defines "materiality."[53] Congress enacted the Fraud Enforcement and Recovery Act of 2009, Pub.L. 111–21, to clarify the materiality element, and to address the machinations courts were imposing to apply that element in an overly-restrictive manner.[54] By adopting a new standard, this Circuit can achieve harmony with the First and Ninth Circuits – the only two of its sister circuits that have addressed the FCA's materiality requirement post-FERA.

The lack of categorical rules remains true to the statute's purpose, "to reach all types of fraud, without qualification, that might result in financial loss to the government."[55] The principles of knowledge and materiality permit courts to engage in a fulsome inquiry regarding whether claims are false or fraudulent under the FCA, thereby properly balancing any stretches of the law to within the limits of material falsehoods, but without creating hyper-technical gaps in the statute's reach.[56]

Here, TAFEF respectfully suggests that any artificial distinctions created by

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[53] 31 U.S.C. 3729(b)(4)

[54] *See* S. Rep. No. 111-10 (2009), at 10 ("the new term 'material' is defined later in the section to mean 'having a natural tendency to influence, or being capable of influencing, the payment or receipt of money or property.' This definition is consistent with the Supreme Court definition, as well as other courts interpreting the term as applied to the FCA").

[55] *Hutcheson,* at 392, *quoting Cook Cnty.*, 538 U.S. at 129.

[56] See Monica P. Navarro, *Materiality: A Needed Return to Basics in False Claims Act Liability*. 43 U. Mem. L. Rev. 105,134 (2012).

a requirement that express words of "condition of payment" exist or must be clearly inferred by the judicial branch should be rejected. Rather, the analysis of whether there is a misrepresentation of compliance with a material precondition of payment should be a fluid one, allowing the court to employ a fact-specific and contextual inquiry of all the extrinsic evidence, in order to determine whether failure to comply with the requirement at issue was capable of influencing the government's decision to pay the claim. Rather than limit this inquiry to whether the express words of the contract, statute, or regulation identify a requirement as a "condition of payment," courts appropriately look to the relevant language and other extrinsic evidence to examine the nexus between the requirement and the entitlement to payment.

## III. CONCLUSION

For the foregoing reasons, the judgment below should be vacated.

Respectfully submitted,

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## CERTIFICATE OF COMPLIANCE WITH FRAP 29(c)(5)

The undersigned, counsel for Taxpayers Against Fraud Education Fund, *Amicus Curiae*, hereby certifies pursuant to Federal Rule of Appellate Procedure 29 that no party's counsel authored this brief in whole or in part; no party or party's counsel contributed money that was intended to fund preparing or submitting this brief; and no person other than Taxpayers Against Fraud Education Fund, *Amicus Curiae*, its members, or its counsel contributed money that was intended to fund preparing or submitting this brief.

Dated: September 30, 2015 /s/ Timothy J. McInnis

**CERTIFICATE OF COMPLIANCE WITH FRAP 29(d) AND FRAP 32(a)**

The undersigned, counsel for Taxpayers Against Fraud Education Fund, *Amicus Curiae*, hereby certifies that this brief complies with the type-volume limitation of Fed. R. App. P. 29(d) and 32(a)(7)(B) because it contains ***5076*** words as reported by the word count function of Microsoft Word, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). This brief also complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because it has been prepared in a proportionally spaced typeface using Microsoft Word in Times New Roman font, 14-point type for both text and footnotes.

Dated: September 30, 2105 /s/ Timothy J. McInnis

## CERTIFICATE OF SERVICE

I hereby certify that on this 30th day of September, 2015, I caused a corrected copy of the foregoing brief to be filed electronically with the Court's CM/ECF system, and that all counsel will be served by the CM/ECF system.

/s/ Timothy J. McInnis