TAF

Vol. 19
July 2000

TAXPAYERS AGAINST FRAUD

False Claims Act and *Qui Tam* Quarterly Review

INSIDE...

The *False Claims Act and Qui Tam Quarterly Review* is published by Taxpayers Against Fraud, The False Claims Act Legal Center (TAF). This publication provides an overview of major False Claims Act and *qui tam* developments including case decisions, DOJ interventions, and settlements.

TAF is a nonprofit public interest organization dedicated to combating fraud against the Federal Government through the promotion and use of the *qui tam* provisions of the False Claims Act (FCA). TAF's mission is both activist and educational. Established in 1986, TAF serves to: (1) collect and evaluate evidence of fraud against the Federal Government and facilitate the filing of meritorious FCA *qui tam* suits; (2) work in partnership with *qui tam* plaintiffs, private attorneys, and the Government to effectively prosecute *qui tam* suits; (3) inform and educate the general public, the legal community, and other interested groups about the FCA and its *qui tam* provisions; and (4) advance public, legislative, and government support for *qui tam*.

TAF is based in Washington, D.C., where it maintains a comprehensive FCA library for public use and a staff of lawyers and other professionals who are available to assist anyone interested in the False Claims Act and *qui tam*.

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Constitutionality/Article III Standing/State *Qui Tam* Liability

Vermont Agency of Natural Resources v. U.S. ex rel. Stevens, 120 S.Ct. 1858 (May 22, 2000)

In a highly anticipated decision, the Supreme Court unanimously held that private individuals who bring suit pursuant to the *qui tam* provisions of the False Claims Act satisfy the Constitution's Article III standing requirements. In an opinion written by Justice Scalia, the Court ruled that *qui tam* relators have standing as partial assignees of the Government's damages claim to remedy the injury suffered by the United States. In a 7-2 vote to reverse the 2nd Circuit, however, the Court also ruled that states and state agencies are not "persons" subject to *qui tam* liability under § 3729 of the statute. Holding that the FCA as originally enacted in 1863 did not include states as persons, the Court found no Congressional intent to broaden the meaning of the term person in subsequent amendments to the Act. The Court found support for its holding in the current statutory scheme, as well as in accepted canons of statutory construction, including the requirement that Congress make its intent to alter the usual constitutional balance between states and the Federal Government "unmistakably clear" in the language of the statute. According to the Court, Congress did not manifest such an intent in the FCA.

This *qui tam* action was initiated in 1995 when Jonathan Stevens, a former employee of the Vermont Agency of Natural Resources (Vermont), alleged that Vermont submitted false claims to the Environmental Protection Agency in connection with various federal grant programs administered by the EPA. Specifically, Stevens alleged that Vermont had overstated the amount of time spent by its employees on the federally funded projects, thus inducing the Government to disburse more grant money than Vermont was entitled to receive.

After the United States declined to intervene in the action, Vermont moved to dismiss the suit, arguing that neither a state nor a state agency is a "person" subject to liability under the FCA and that a *qui tam* action in federal court against a State is barred by the 11th Amendment. Vermont appealed the district court's denial of its motion to the 2nd Circuit, which by divided panel affirmed the lower court's ruling in favor of Stevens.

Court Finds Historical Support for Relator Standing

Before reaching the statutory and 11th Amendment issues squarely presented by the case before it, the Court addressed whether Stevens had standing under Article III of the Constitution. The Court unanimously ruled that Stevens met Article III's standing requirements.

The Court began by reviewing the three requirements that are the "irreducible constitutional minimum" of Article III standing. According to current doctrine, to have standing a plaintiff must establish: (1) an injury-in-fact – one that is "concrete" and "actual or imminent, not conjectural or hypothetical"; (2) causation – a "fairly … trace[able]" connection between the alleged injury-in-fact and the alleged conduct of the defendant; and, (3) redressability – a "substantial likelihood" that the requested relief will remedy the alleged injury-in-fact.

Stevens argued that his *qui tam* action served to remedy an injury suffered by the United States. The Court found that Stevens' com-

plaint properly alleged such an injury — both the injury to United States sovereignty arising from the violation of its laws and the proprietary injury resulting from the alleged fraud. The Court also found that the portion of the Government's recovery Stevens could receive upon prevailing constituted a concrete private interest in the outcome of the suit. Stating, however, that "[t]he interest must consist of obtaining compensation for, or preventing, the violation of a legally protected right," the Court stressed that the concrete interest must be related to the injury-in-fact. As Stevens' right to his share of the Government's recovery could not fully materialize until the litigation was over, this interest would be merely a "byproduct" of the suit and would not serve to obtain compensation for or prevent a violation to a legally protected right.

Instead, the Court found an adequate basis for Stevens' suit in an assignment theory of relator standing. The Court applied to *qui tam* relators the doctrine which grants an assignee of a claim the right to assert the injury suffered by the assignor. The Court held: "The FCA can reasonably be regarded as effecting a partial assignment of the Government's damages claim."

In reaching its holding, the Court heavily relied upon the *qui tam* concept's grounding in English and American legal history. The Court stated:

> [H]istory is particularly relevant to the constitutional standing inquiry since … Article III's restriction of the judicial power to "Cases" and "Controversies" is properly understood to mean "cases and controversies of the sort traditionally amenable to, and resolved by, the judicial process."

The Court observed that *qui tam* actions in various forms have been a part of English legal tradition since the end of the 13th century, when private individuals sued to vindicate royal interests as well as their own. The Court also recognized the *qui tam* tradition in the American legal system, noting particularly its use immediately before and after the framing of the Constitution. Referring to *qui tam*'s historical roots, the Court concluded its analysis of this issue by stating: "When combined with the theoretical justification for relator standing discussed earlier, it leaves no room for doubt that a *qui tam* relator under the FCA has Article III standing."

No Congressional Intent to Include States as Persons

Turning to the state sovereignty issues of the case before it, the Court addressed Vermont's contentions that: (1) a state or state agency is not a "person" subject to *qui tam* liability under § 3729 of the FCA; and (2) even if it were, the 11th Amendment bars such a suit. Ruling that the word "person" as it is used in § 3729 does not include states, the Court never reached the 11th Amendment issue.

Section § 3729(a) subjects to liability "[a]ny person who," *inter alia*, "knowingly presents or causes to be presented, to an officer or employee of the United States Government … a false or fraudulent claim for payment or approval." Applying its longstanding presumption that the term person does not include the sovereign, the Court found no affirmative showing of congressional intent to the contrary in the FCA. The Court stated: "The presumption is particularly applicable where it is claimed that Congress subjected the States to liability to which they had not been subject before." According to the Court, the FCA as originally enacted in 1863 "bore no indication that States were subject to its penalties" and none of the subsequent amendments to the statute, including the 1986 amendments, suggested a broadening of the term person.

The Court found support for its ruling in three aspects of the the current statutory scheme. First, § 3733 of the statute, which enables the Attorney General to issue civil investigative demands to "any person" possessing information relevant to a false claims law investigation, defines person to include states while the Act's liability provisions contain no such definition. Second, the Court stated that the current version of the FCA imposes damages that are "essentially punitive in nature," thus running contrary to the "presumption against imposition of punitive damages on governmental entities." Third, the Program Fraud Civil Remedies Act of 1986, a sister scheme creating administrative remedies for false claims which was enacted just before the 1986 amendments, contains a definition of person that does not include states. According to the Court, it would be "most peculiar" to subject states to the damages and penalties provisions of the False Claims Act while exempting them from the smaller damages imposed under the PFCRA.

The Court found further support for its holding in two doctrines of statutory construction. The Court applied the ordinary rule of statutory construction known as the clear statement rule, which holds that "if Congress intends to alter the usual constitutional balance between States and the Federal Government, it must make its intention to do so unmistakably clear in the language of the statute." Reiterating its finding that Congress did not manifest such an intent in the FCA, the Court moved on to the second doctrine, which holds that "statutes should be construed so as to avoid difficult constitutional questions." Of this the Court stated: "We of course express no view on the question whether an action in federal court by a *qui tam* relator against a State would run afoul of the Eleventh Amendment, but we note that there is 'serious doubt' on that score." The Court therefore reversed the judgment of the 2nd Circuit.

Majority Opinion Leaves Open Question About United States as Plaintiff

While the majority opinion did not directly address the issue, in a concurring opinion Justice Ginsburg observed that "the clear statement rule applied to private suits against a State has not been applied when the United States is the plaintiff." She therefore stated: "I read the Court's decision to leave open the question whether the word 'person' encompasses States when the United States itself sues under the False Claims Act."

No Ruling on Article II Issue

Noting that the validity of *qui tam* suits under other constitutional provisions is not a question to be resolved here, the majority stated in a footnote that it expressed no view on whether *qui tam* suits violate the Appointments Clause or the Take Care Clause of Article II of the Constitution. In a separate footnote, the majority left as an open question whether states can be persons for purposes of commencing a *qui tam* action.

Dissenting Justices Assert that False Claims Act is "All-Embracing in Scope"

Justices Stevens and Souter dissented strongly from the majority opinion on state liability, stating that "[t]he False Claims Act is … all-embracing in scope, national in its purpose, and as capable of being violated by state as by individual action." While acknowledging that statutory references to persons are not normally construed to apply to the enacting sovereign, the Justices stressed that "when Congress uses that word in federal statutes enforceable by the Federal Government or by a federal agency, it applies to States and state agencies as well as to private individuals and corporations." The Justices asserted further that both legislative history and the current text of the statute support their dissenting viewpoint, and utilized the same elements of the statutory scheme relied upon by the

majority to defend their opposing view. They concluded their dissent by asserting that the historical support for *qui tam* evidenced in the majority opinion also would be sufficient to find that the statute is constitutional under Article II.

Editor's Note: For an in-depth analysis of the impact of Stevens, see Spotlight section, page 15.

FCA Liability/Implied False Certification/Knowledge

U.S. ex rel. Shaw v. AAA Engineering & Drafting, Inc. et al., 213 F.3d 519 (10th Cir. May 18, 2000)

The 10th Circuit affirmed a jury's finding that falsely inflated work orders, while not actually claims for payment, could form the basis for a False Claims Act suit where the orders influenced the Government's payment decisions under the contract. In addition, the circuit court affirmed a finding of FCA liability on implied false certification grounds where the defendant failed to comply with environmental regulations in the performance of the contract. Finally, the circuit court ruled that government knowledge did not serve as a defense to the contractor's knowing submission of false records in support of its claims for payment.

Debra Shaw was a photographer employed by AAA Engineering & Drafting, Inc., a company that contracted with Tinker Air Force Base in Oklahoma to provide photography services. In 1993, Shaw brought a *qui tam* suit against AAA alleging that the company submitted false and inflated work orders to the Government in support of its requests for compensation. The suit also alleged that, in its photography operations, AAA failed to conduct a contractually required process known as silver recovery. At trial, judgment was entered against the company for $14,700 plus $15,000 in civil penalties.

Inflated Work Orders Were False Records

AAA's contract with the Government required it to prepare a work order for each customer describing all of the photography services that would be performed. The work orders were used to track work performed and could be used as the basis for any equitable adjustment under the contract. On appeal, the company argued that because the work orders were submitted merely as a record of work requested and performed, and not specifically for the purpose of receiving payment, they could not form the basis for Shaw's FCA claim. The court rejected this argument, noting that AAA had used the falsely inflated work orders to support its request for an upward equitable adjustment. While the work orders themselves were not claims for payment, the court ruled there was sufficient evidence to support a finding by the jury that the work orders were false records submitted in order to get claims paid.

Government Paid for Environmental Compliance

AAA's contract also required it to comply with Environmental Protection Agency regulations for the disposal of film processing solution. According to EPA guidelines, AAA was required to use the proper equipment to remove all traces of silver from the film processing solution prior to its disposal. Shaw's suit alleged that AAA failed to perform silver recovery but continued to invoice for and receive full payment under the contract.

As any equitable adjustments to the contract payments were negotiated separately, AAA's monthly invoices billed for the fixed price of the contract. AAA therefore argued that the monthly invoices could not be fraudulent because they billed only for the fixed price and did not contain any factual misrepresentations. The court found, however, that AAA had impliedly certified with each monthly invoice that it complied with the silver recovery provi-

sions of its contract with the Government. The court reasoned that because the contract required AAA to practice silver recovery in its laboratory, AAA was being paid not only for photography services but also for environmental compliance. The court therefore affirmed the defendant's liability on implied false certification grounds.

The court stated that permitting FCA liability based on a false certification of compliance, whether express or implied, is consistent with the legislative history of the 1986 amendments to the Act. The court cited to a statement by the Senate Judiciary Committee at the time of the amendments:

> [A false claim under the FCA] may take many forms, the most common being a claim for goods and services not provided, or provided in violation of contract terms, specification, statute, or regulation.

S.Rep. No. 99-345 at 9 (1986), *reprinted in* 1986 U.S.C.C.A.N. at 5274. In addition, the court found that the language of § 3729(a)(1) supports the theory of implied false certification. Whereas § 3729(a)(2) premises liability on the presentation of a "false record or statement to get a false or fraudulent claim paid or approved," liability under the language of § 3720(a)(1) does not require evidence of a "false record or statement." Thus, according to the court, FCA liability may arise even absent an affirmative or express false statement by the government contractor. Although the court admitted to a mixed judicial acceptance of the false certification theory, it suggested that any negative precedent could be easily distinguished from the facts of this case. In this instance, the court found that there was sufficient evidence that AAA submitted invoices for full payment while knowing that it had failed to comply with the contractual requirement to perform silver recovery in accordance with EPA rules.

Government Knowledge Does Not Mitigate Knowing Falsity

The court also dismissed the defendant's contention that, because the Government had access to the work orders during the contract period and knew about the failure to practice proper silver recovery, AAA could not have had the requisite intent to violate the FCA. The court stated that the 1986 Amendments had removed language that made the Government knowledge of a contractor's wrongdoing an automatic defense to a FCA action. While acknowledging that there still may be occasions when the Government's knowledge of such wrongdoing is so extensive that the contractor could not, as a matter of law, possess the requisite state of mind to be liable under the FCA, the court concluded that such extensive government knowledge was not present in the case before it. Thus, the court held that the Government's alleged knowledge of the defendant's actions did not negate the evidence that the defendant knowingly submitted false records in support of its claims for payment.

U.S. ex rel. Siewick v. Jamieson Science and Engineering, Inc. et al., 214 F.3d 1372 (D.C.Cir. June 30, 2000)

The relator's implied false certification theory fails where the Government did not condition its payment upon compliance with the "revolving door" statute at issue, ruled the D.C. Circuit. Moreover, the alleged violation did not void the government contract. Finding that the contract was at most voidable at the Government's election, the appellate court rejected the relator's argument that the defendant knowingly submitted claims for payment pursuant to an invalid agreement.

Beginning in 1987, Jamieson Science and Engineering, Inc. (JSE) contracted with the Navy's Strategic Defense Initiative Organization

(SDIO) to provide assessment of infrared sensors and related technology. JSE hired Vincent O'Connor, who until 1987 had been an SDIO employee, just a few months after he left his government employment. Dr. Joseph Siewick, a physicist formerly employed by JSE, brought a *qui tam* action alleging that by hiring O'Connor, JSE violated 18 U.S.C. § 207, a criminal statute aimed at fighting "revolving door" abuses by former government employees. According to Siewick, by submitting claims for payment under its government contract, JSE had impliedly and expressly certified to be in compliance with all applicable laws. Siewick also asserted that any violation of the "revolving door statute" rendered the government contract void and unenforceable, and thus all claims under the contract false. The circuit court addressed these issues on Siewick's appeal of a summary judgment entered in favor of the defendants.

Payment Not Conditioned on Compliance

Finding that the Government did not condition its payment on compliance with § 207, the court ruled that Siewick failed on his implied certification theory even if JSE had violated that statute. The court stated:

> Siewick's first theory – that the vouchers made an "implicit certification" of non-violation of § 207 — is a non-starter. It is doomed by the rule, adopted by all courts of appeals to have addressed the matter, that a false certification of compliance with a statute or regulation cannot serve as the basis for a *qui tam* action under the FCA unless payment is conditioned on that certification.

Siewick offered no evidence to support his view that JSE was required to certify compliance with § 207 in order to be payed under the contract.

Contract Voidable But Not Void

The court rejected further Siewick's assertion that a violation of the revolving door statute could, by itself, have voided the contract, thus making all claims under the contract false or fraudulent. At best, the contract would be voidable at the Government's option. The court analogized the case at hand to the Supreme Court's treatment of 18 U.S.C. § 208, which criminalizes certain conflicts of interest. In U.S. v. Mississippi Valley Generating Co., 364 U.S. 520 (1961), the Supreme Court held that such a violation simply would give the Government the right to "disaffirm a contact which is infected by an illegal conflict of interest."

The circuit court then addressed whether JSE knowingly misrepresented the validity of the contract. According to the court, if the contract were voidable, it would have become invalid only on a contingency: the Government's exercising its right to disclaim its obligations. Moreover, even if the defendants had reason to believe that § 207 had been violated, thus rendering the contract voidable, there was no evidence that the defendants knew such violation was material to the terms of the contract. Finally, the court reasoned that finding such a contract invalid in a *qui tam* action not joined by the Government would unilaterally divest the Government of its discretion to retain the contract as fully effective. The circuit court therefore affirmed the lower court's ruling in favor of JSE.

Collection Procedures/Sovereign Immunity

Shaw v. United States et al., 213 F.3d 545 (10th Cir. May 18, 2000)

The 10th Circuit ruled that the FCA contains no express or implied waiver of the United

States' sovereign immunity with respect to the collection of fees and expenses awarded under the Act. The appellate court therefore quashed a writ of garnishment served by the relator on a federal agency believed to owe money to the *qui tam* defendant pursuant to various government contracts. The court further ruled that the *qui tam* relator was not acting as "counsel to the United States" as that is defined in the Federal Debt Collection Procedures Act, nor could the relator invoke the collection procedures available to the United States pursuant to that statute.

In June 1997, the district court entered a judgment in favor of plaintiff Shaw in her *qui tam* suit and wrongful termination action. In October 1997, the United States applied to the district court for a writ of garnishment for the *qui tam* portion of the judgment, including the portion of the judgment to which Shaw was entitled. The garnishee was the National Imagery and Mapping Agency of the Defense Finance and Accounting Service (DFAS), which was believed to owe money to the *qui tam* defendant pursuant to various government contracts. Shaw twice applied for the same writ of garnishment against DFAS. The United States, arguing that the court lacked subject matter jurisdiction by reason of sovereign immunity, moved to quash Shaw's writ and dismiss the garnishment proceeding. The district court granted the Government's motion.

No Waiver of Sovereign Immunity in the FCA

The appellate court resolutely stated that no garnishment may be brought against the United States absent an express waiver of sovereign immunity. Relying on United States v. Nordic Village, 503 U.S. 20 (1992), the court emphasized that any waiver of the United States' sovereign immunity must be express in the statutory text, and ruled that no such express waiver exists in the FCA. The court summarily dismissed Shaw's contention that the FCA provisions awarding fees and expenses to a prevailing relator constitute an implied waiver of sovereign immunity.

Relators Are Not Counsel for the United States

The circuit court further ruled that, in seeking to collect statutory attorneys' fees or a relator's share of a judgment, *qui tam* relators do not have standing to invoke the powers afforded to the Federal Government under the Federal Debt Collection Procedures Act (FDCPA). The FDCPA delineates the procedures for the United States to recover a judgment on a debt. Shaw argued that, as a relator, she fell under the FDCPA definition for "counsel to the United States," thus enjoying the same powers as the United States to collect the debt owed by the defendant. The court disagreed with Shaw on two grounds. First, the FDCPA does not empower any plaintiff to collect his own debts. The FDCPA defines debt as "an amount owing to the United States." In this instance, the debt owed by the defendants was not to the United States, but to Shaw for her fees and expenses. Second, according to the court, Shaw fell outside of the FDCPA's statutory definition of counsel for the United States. While this definition does apply to private attorneys authorized by contract to conduct litigation on behalf of the United States, it cannot logically be extended to include *qui tam* plaintiffs seeking to collect attorneys' fees owed to them as individuals. The court therefore ruled that the relator does not acquire the Government's standing to assert the FDCPA and affirmed the district court's order quashing Shaw's writ of garnishment.

Section 3730(h) Retaliation Claims/Attorneys' Fees

Norbeck v. Basin Electric Power Cooperative, 215 F.3d 848 (8th Cir. June 15, 2000)

Joining the D.C. Circuit, the 8th Circuit affirmed a lower court's decision to allow a dual motive defense for an employer sued under the § 3730(h) retaliation provision of the False Claims Act. Relying on legislative history, the appellate court interpreted § 3730(h) as exonerating the employer where the employer could prove that retaliation was not the sole cause of the plaintiff's firing. Based on the jury's finding that the employer would have fired the plaintiff regardless of his protected activity, the court reversed the lower court's award of attorneys' fees to the plaintiff.

In January 1995, Robert Norbeck filed a *qui tam* suit against Basin Electric Power Cooperative (Basin) alleging fraudulent billing of costs under a Basin contract with the Western Area Power Administration. The Western Area Power Administration is a unit of the United States Department of Energy. The Government intervened and was awarded judgment against Basin in the amount of $43 million. The relator's share was 30 percent. Norbeck also filed a § 3730(h) retaliation claim against Basin. On the retaliation claim, the jury found that Basin would have fired Norbeck even if he had not engaged in protected whistleblowing activities. The jury did not award Norbeck damages, yet the court did award him $46,000 in attorneys' fees for his retaliation case. Norbeck appealed, arguing that the court erred in giving the jury a dual motive instruction. Basin cross-appealed, asserting that the district court erred in awarding Norbeck attorneys' fees because he did not prevail on his retaliation claim.

No Damages Awarded in Dual Motive Firing

The jury found that Norbeck had engaged in protected activity under the Act, that Basin knew he was engaged in such activity, and that Basin's decision to terminate him was motivated at least in part by retaliatory animus. As instructed by the district court, however, the jury also considered whether Basin would have fired Norbeck even if he had not engaged in protected activity. Finding in the affirmative on this issue, the jury awarded Norbeck no damages in his retaliation claim. Yet, the district court granted Norbeck's request for attorneys' fees because he had proven that an impermissible factor played some part in his firing.

On appeal, Norbeck argued that the district court committed reversible error by issuing the jury instruction that Basin should prevail if it could prove that Norbeck would have been fired regardless of engaging in activity protected under the FCA. The appellate court noted, however, that every court to have addressed the question of whether a dual motive affirmative defense is available to an employer has concluded that it is. The court acknowledged that § 3730(h) of the statute does not say whether a plaintiff must prove that retaliation was the only cause of his discharge in order to recover, nor does the statute mention an affirmative defense for an employer. However, citing to legislative history as support, the court found congressional intent to provide for a dual motive affirmative defense. Reasoning that such legislative history had been persuasive to other courts considering the issue, the court concluded that the district court did not err in giving a dual motive instruction to the jury.

The court rejected Norbeck's arguments that the jury should have been required to find that Basin's non-retaliatory reasons for firing him were legal. The court stated that Norbeck failed to raise this issue in the district court and failed

to show that the absence of such an instruction prejudiced substantial rights or resulted in a miscarriage of justice.

Award of Attorneys' Fees Reversed

Basin asserted in a cross-appeal that, because Norbeck did not prevail in his retaliation claim, the jury erred in awarding him attorneys' fees. The court agreed, holding that a finding of dual motive for the termination of a whistleblower plaintiff's employment exonerates the employer. The court found persuasive the reasoning in Mount Healthy School District Board of Education v. Doyle, 429 U.S. 274 (1977), which granted a dual motive defense to an employer in an employment action raising First Amendment claims. Focusing on the fundamental unfairness of a rule of causation that denies a dual motive defense to employers, the court reversed the award of attorneys' fees.

FCA Liability/Vicarious Liability of Employer

U.S. v. Southern Maryland Home Health Services, Inc. et al., 95 F.Supp.2d 465 (D.Md. May 9, 2000)

A Maryland district court held that an otherwise innocent employer cannot be held vicariously liable under the False Claims Act for actions committed by its employee. Although the court acknowledged that its holding is inconsistent with the majority of cases addressing this issue, it reasoned that a recent Supreme Court decision limiting the application of vicarious liability in the context of punitive damages supported its conclusion.

Southern Maryland Hospital (SMH) hired Diane Canon to serve as a physical therapist, apparently unaware that she was using false credentials and was not in fact a licensed therapist. During Canon's tenure as an SMH employee and contractor, SMH submitted nearly $60,000 in claims to Medicare for physical therapy services she provided. Upon discovering her subterfuge, the Government brought criminal and civil charges against Canon, and also filed a separate action against SMH alleging that the hospital was liable under the False Claims Act for at least $1 million in damages and penalties. The Government moved for summary judgment against SMH, arguing that SMH was vicariously liable for Canon's actions under the theory of *respondeat superior*, and citing to authority from a variety of circuits holding that employers can be liable under the FCA for their employees' actions even if those actions are undertaken without their knowledge or consent.

No Vicarious Liability Where Damages Imposed Are Punitive

The court acknowledged those decisions imputing an employee's FCA liability to an otherwise innocent employer based upon a "strict liability" theory or upon the determination that the employee's acts benefited the employer even if he was unaware of them. Nevertheless, the court cited to U.S. v. Ridglea State Bank, 375 F.2d 495 (5th Cir. 1996), in which the 5th Circuit refused to apply FCA liability to an innocent employer based on the misdeeds of an employee. The Ridglea Court distinguished vicarious liability for compensatory versus criminal liability and reasoned that the FCA is similar to a criminal statute because its damages and penalties provisions are punitive in nature. In Ridglea, the 5th Circuit concluded it would be inappropriate to hold an employer vicariously liable under a statute requiring knowledge or guilty intent.

Here, the district court expressly rejected the strict liability and the "benefit to the employer" analysis that might result in the application of vicarious liability under the FCA. Instead, the court held that, at least when the recovery

sought by the Government is substantially higher than the actual losses to the Government, an employer is not liable under the FCA for an employee's acts unless the employer knew of the acts, ratified them, or was reckless in hiring or supervising the employee.

The court reached its conclusion by applying general principles of agency law in the context of punitive damages. Noting that in this case the Government had paid about $60,000 in false claims but was seeking $1 million in damages and penalties, the court concluded that the Government was seeking FCA damages that were punitive in nature. Advocating the minority view, the court relied upon the Restatement (Second) of Agency and Torts, which generally does not impute an agent's liability to a principal unless the principal was aware of those actions, ratified them or if, in some cases, the agent was a high-level employee. The court also relied upon Kolstad v. American Dental Association, 119 S.Ct. 2118 (1999), in which the Supreme Court generally adopted the Restatement position and required some degree of culpability on the part of the employer in order to have the employee's acts imputed to it for punitive damages liability. The court observed that the Kolstad decision represents a major shift in agency law, therefore throwing into doubt many of the cases cited by the Government in support of its vicarious liability argument. Finding that SMH did not authorize Canon's actions or act recklessly in hiring or supervising her, the court concluded that it could not hold SMH liable under the FCA for her actions.

Settlement/Rule 9(b)/Standing

U.S. ex rel. Walsh v. Eastman Kodak Company et al., 98 F.Supp.2d 141 (D.Mass. May 31, 2000)

A Massachusetts district court dismissed a relator's attempt to relitigate claims against the defendants which had been resolved by settlement. Finding that the United States, and not the relator, was charged with asserting lack of compliance with the settlement, the court disregarded the relator's dissatisfaction with audits performed pursuant to the settlement agreement. Moreover, finding that the relator – the former Chief Financial Officer of the defendant hospital – only alleged theories of fraud and could not identify one specific false claim, the court ruled that the relator had failed to show even "bare bones" compliance with Rule 9(b). In addition, the court held that the relator did not have standing to assert the Government's common law claims.

In 1997, the Government intervened in a *qui tam* suit alleging that Daughters of Charity National Health System and Carney Hospital (collectively DCNHS) failed to include in cost reports submitted to Medicare the discounts and rebates received from vendor Eastman Kodak. Eastman Kodak provided x-ray films and other supplies to the hospital. Timothy Walsh, a former Chief Financial Officer of Carney, initially filed the *qui tam* suit in November 1995. In August 1998, DCNHS agreed to pay the United States $586,075 as an initial settlement amount to resolve false claims liability stemming from an audit of the Kodak discount program. The relator received $129,500 of the initial settlement amount.

The agreement also provided that DCNHS would pay double the total losses to Medicare, which would be calculated based on the results of a further audit of other vendor programs. Relator Walsh would then receive 22 percent of the Government's recovery. The agreement required the follow-up audit to be conducted by Catholic Healthcare Networks (CHAN), utilizing the same methodology as that used to audit the Kodak discounts. Walsh, however, contended that CHAN's audit of the other vendor programs failed to account for non-cash remuneration, such as credits and equipment leases, issued under the programs. Unhappy with perceived deficiencies of

the audit, Walsh filed an amended complaint, setting forth virtually the same allegations against DCNHS as were contained in the original *qui tam* complaint, adding common law claims of fraud, payment under mistake of fact, and unjust enrichment. In addition to the DCNHS hospitals, Walsh alleged the same FCA violations by ten classes of hospitals, which included every hospital in the United States that entered into similar contracts with the vendor defendants.

Relator Released Claims Pursuant to Terms of Settlement

The court granted the defendant's motion for summary judgment as to Walsh's attempt to relitigate his original cause of action against DCNHS. The court rejected the relator's arguments that DCNHS did not perform its obligations to the relator under the settlement agreement. Finding the language of the settlement unambiguous on the issue, the court ruled that the relator relinquished his claims against DCNHS upon the Government's receipt of the initial settlement amount. Furthermore, the United States, not the relator, was charged with ensuring that the follow-up audit was performed correctly. According to the agreement, the United States would not release its claims against DCNHS until the total Medicare loss was determined and final settlement amount tendered. However, the relator released his claims upon receiving the initial settlement amount.

Failure to Comply with Rule 9(b)

Walsh further alleged that by failing to ensure that its discount program met the statutory discount exception to the Anti-Kickback Act, Kodak in turn violated the FCA. The court dismissed Walsh's claim on Fed. Rule Civ. Proc. 9(b) grounds, finding that the relator had failed to properly plead with specificity that the defendant had the requisite knowledge or intent to violate either statute.

With respect to the additional vendor defendants, the court ruled that the relator failed to comply with 9(b)'s requirement for pleading allegations of fraud with sufficient particularity. Although Walsh had delineated the alleged methods by which the vendor defendants might have submitted false invoices, the court noted that, within his amended complaint, Walsh failed to cite a single specific false claim arising from a supposedly false invoice. The court emphasized that Walsh could not uncover any false cost reports despite having served as Chief Financial Officer of Carney Hospital, one of the vendor defendants. In light of this lack of detail, the Court dismissed the amended complaint with prejudice.

Relator Lacks Standing to Assert Government's Common Law Claims

Walsh additionally asserted three common law claims — fraud, payment under mistake of fact, and unjust enrichment — against DCNHS and the hospital classes. The court easily concluded that the language of the settlement agreement barred the relator from bringing claims arising from any of the allegations in the civil action. Furthermore, the express language of the FCA does not allow a relator to assert common law claims on behalf of the United States. Observing that the relator did not claim to have suffered any injury-in-fact from the conduct of the defendants, the court held that Walsh did not have standing to assert any of the Government's common law claims.

U.S. ex rel. Morris v. Crist et al. (SD OH No. C-2-97-1395)

On March 29, 2000, an Ohio district court ruled that under Medicare's Prospective Payment System (PPS), the inclusion of nonreimbursable services on a Medicare claim form may constitute fraud under the FCA even where the Government does not sustain actual damages. Under Medicare's PPS, each inpatient is assigned a diagnosis-related group (DRG) based on that patient's diagnosis. The hospital is reimbursed a flat fee based upon the DRG assigned to the patient, regardless of the number or type of services provided. In his *qui tam* suit, Morris alleged that Bethesda Hospital included nonreimbursable research costs incurred as a result of for-profit drug studies in the "allowable charges" column of the bills submitted to Medicare. Bethesda asserted, however, that as long as it assigned the proper DRG code to each patient that the claims submitted could not be false.

The court ruled that, even though the amount paid by the Government would be unaltered, the hospital's failure to offset the charges on the bill could constitute a false claim. Finding that the each bill represented a claim against the Government whether or not it was for a flat fee, the court rejected Bethesda's assertion that it could "pick and choose what can be false on a bill submitted to Medicare" so long as the DRG code was correct.

The court also ruled that actual damage to the Government is not necessary to establish a violation of the FCA. Furthermore, the Government may have suffered damages because the bills submitted by Bethesda could result in false inflation of the predetermined DRG payments in the future.

In re: Columbia/HCA Healthcare Corporation (MD TN No. 3-98-MDL-1227)

In April 2000, a Tennessee district court ruled that Columbia/HCA Healthcare Corp. waived both the attorney-client privilege and the attorney work-product exception as to documents it produced to the Government during an investigation of Columbia for improper billing practices. The documents at issue were created during special audits of Columbia's Medicare coding practices commissioned by its own in-house counsel. Prior to producing the documents to DOJ, however, both Columbia and the Government executed an agreement stating that the production did not constitute a waiver of either the attorney-client privilege or the work-product exception. In a subsequent, separate action in the Middle District of Tennessee, an unidentified plaintiff moved to compel the production of these documents, contending that Columbia's previous disclosure of the documents did indeed constitute a waiver. The district court agreed, rejecting the "selective waiver doctrine," which provides that when an entity voluntarily reveals communications to the Government during a Government investigation the waiver applies as to the Government, but not as to all other adversaries. The court entered an order requiring Columbia to produce to the plaintiff those audit documents that previously had been provided to the Government.

Hoefer v. Fluor Daniel, Inc. et al. (CD CA No. SACV98447GLTKY)

In April 2000, a California district court ruled that the Federal False Claims Act does not preempt a state wrongful discharge action for retaliation against a federal whistleblower. Earlier, the court had issued an order stating that the FCA was intended to occupy the entire

field of federal false claims and thus preempted the state suit. On reconsideration, however, the court withdrew this opinion, persuaded by a recent New Jersey district court decision evaluating this issue. *See* Paladino v. VNA of Southern New Jersey, 68 F.Supp.2d 455 (D.NJ 1999). The court concluded, without analysis, that the FCA does not preempt the state wrongful discharge action and did not dismiss the state claim. The court further held that the California False Claims Act does not provide retaliation protection for federal whistleblowers and that, as a matter of law under the intracorporate conspiracy doctrine, a corporation cannot conspire with its own employees or agents to retaliate against an employee whistleblower. The claims were brought by Patrick Hoefer, who was terminated from Fluor Daniel after bringing two *qui tam* actions against the company pursuant to the Federal Act. Before the court were Hoefer's California False Claims Act retaliation claim, a wrongful discharge claim brought pursuant to the corporate conspiracy doctrine, and a FCA retaliation claim.

U.S. ex rel. Kozhukh v. Constellation Technology Corp. (MD FL No. 8:98-CV-521-T-17E)

In June 2000, a Florida district court ruled that the provisions in the FCA which permit a relator to proceed when the Government does not intervene do not violate the Constitution. The court denied the defendant's motion to dismiss a FCA suit on the grounds that such provisions violate the separation of powers doctrine and the Take Care Clause of Article II of the United States Constitution. Citing to Nixon v. Administrator of Gen. Services, 433 U.S. 425 (1977), the court stated that the appropriate inquiry for determining whether an act violates the separation of powers doctrine is a "focus on the extent to which it prevents the Executive Branch from accomplishing its constitutionally assigned functions." Citing numerous court decisions holding that the FCA provides the Executive Branch with sufficient control over the litigation, the court concluded that the FCA does not violate the separation of powers doctrine. The court further noted that, in arguing that the *qui tam* provisions of the FCA are unconstitutional, the defendant's motion solely relied upon U.S. ex rel. Riley v. St. Luke's Episcopal Hospital, 982 F.Supp. 1261 (S.D.Tex. 1997), 12 TAF QR 1 (Jan. 1998), persuasive but nonbinding authority that was later vacated.

U.S. ex rel. Mikes v. Straus et al. (SD NY No. 92CIV2754)

In June 2000, a New York district court granted in part and denied in part the defendants' petition for attorneys' fees pursuant to § 3730(d)(4) of the FCA. Section 3730(d)(4) awards attorneys' fees and expenses to a prevailing defendant if "the court finds that the claim … was clearly frivolous, clearly vexatious, or brought primarily for purposes of harassment." The petition stemmed from an unsuccessful *qui tam* suit brought against the defendant physicians by Patricia Mikes, a former member of the practice, alleging that the defendants had billed Medicare for substandard care as well as for unnecessary testing. Mikes alleged that the physicians had failed to properly calibrate a spirometer, which measures the lung function in pulmonary patients, yet billed Medicare for testing with this device. In addition, Mikes contended that the defendants conducted unnecessary Magnetic Resonance Imaging (MRI) tests on Medicare patients. The defendants' motion for attorneys' fees followed seven years of litigation, which concluded in the court's dismissing Mikes' underlying *qui tam* action.

Acknowledging that the law of substandard quality-of-care claims under the FCA was unsettled at the time Mikes filed her suit, the court could not conclude that Mikes' FCA claim was so lacking in legal merit as to be frivolous. The court did find frivolous, however, Mikes unnecessary testing claims, as the only patient alleged by Mikes to have undergone unnecessary testing was not a Medicare beneficiary. The court likewise found frivolous Mikes' claim that the physicians engaged in fraudulent and unnecessary MRI referrals, as Mikes had been forced to withdraw the claim due to lack of sufficient evidence. Next required by § 3730(d)(4) to address whether Mikes' suit was vexatious or brought with primary intent to harass, the court ruled that the MRI referral claim was vexatious due to the complete absence of evidentiary support. Noting that the award of fees was still not mandatory, however, the court used its discretion to award only two-thirds of any attorneys' fees attributable to the MRI claims. In reaching this holding, the court took into account what it believed to be false testimony by one of the defendants.

The following is the first of a two-part series examining the impact of the Supreme Court's decision in Vermont Agency of Natural Resources v. U.S. ex rel. Stevens.

Qui Tam Suits Against Public Entities after Stevens

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The Supreme Court's recent decision in Vermont Agency of Natural Resources v. United States ex rel. Stevens, 120 S. Ct. 1858 (2000), will no doubt be best remembered for its ruling upholding the constitutionality of the *qui tam* provisions of the False Claims Act (FCA), 31 U.S.C. §§ 3729 et seq., under Article III of the federal Constitution. But the Stevens Court also resolved an important statutory construction issue by ruling that, in a pure *qui tam* action brought under the FCA — that is, an action brought by a private party and pursued without the Government's intervention — a State is not a "person" subject to suit within the meaning the Act. See 31 U.S.C. § 3729(a) (subjecting to suit "[a]ny person" who presents a false claim to the United States Government, and making any such "person" "liable to the United States Government" for treble damages and penalties. Id.)

The Court's ruling on that point has prompted, not only States, but many other public entity defendants, to move to dismiss pending FCA actions. The Stevens Court however, resolved only the issue of whether States themselves can be sued as "persons," and the Court did so only in the context of FCA suits neither initiated by nor joined by the Government.

Stevens, then, left unresolved a series of other questions, including four that we believe to be particularly important: (i) whether municipalities, municipal agencies, counties, and other local government entities (collectively referred to in this Article as "municipalities" for ease of exposition) can be sued as "persons" under the Act in pure *qui tam* actions; (ii) whether State or local "proprietary" or "independent" entities (as opposed to ordinary government agencies funded through tax revenues) can be sued as "per-

sons" in such actions; (iii) whether State and other government employees can be sued as "persons" in their individual capacities in such actions; and (iv) whether even States themselves can be sued when the United States either initiates or joins an FCA action.

This Article addresses the first three questions just outlined.[1] The conclusion we have reached is that all three classes of defendants identified above — municipalities, State and local proprietary/independent entities, and individuals sued in their individual capacities — are "persons" under § 3729(a), and that defendants in all of these classes may therefore be sued in pure *qui tam* actions.

Our reasoning, in capsule form, is that all three classes of defendants plainly were "persons" under the version of § 3729(a) in place prior to the 1986 Amendments to the False Claims Act; that nothing in the text, the overall structure, or the legislative history of the current, 1986 version of the FCA indicates that Congress intended to narrow the universe of defendants who could be sued as persons; that, to the contrary, the text, the structure, and the 1986 legislative history all demonstrate an intent to preserve the historic understanding that these categories of defendants are § 3729(a) "persons"; and that Stevens, in ruling that the original pre-1986 understanding of "person" carried over into the new Act, fully supports the proposition that all three classes of defendants we have identified remain "persons" who can be subject to suit.

In developing our points, we begin, in Part I, with a brief synopsis of the Stevens decision. That synopsis will provide an analysis of Stevens that is central to the arguments made in the subsequent parts. Part II examines the status of municipalities as "persons." Part III examines the status of proprietary/independent public entities as "persons." And, finally, Part IV examines the status of individual State (or other government) employees as "persons."

I. THE STEVENS DECISION

Aside from the Article III constitutionality question — which is outside the scope of this Article — the Court in Stevens granted certiorari to decide two questions: (1) whether a State is a "person" subject to suit in a *qui tam* action within the meaning of § 3729(a) of the FCA; and (2) whether, if a State is a "person," a State nevertheless is immune from *qui tam* suits by reason of the Eleventh Amendment to the federal Constitution and the principles of sovereign immunity underlying that Amendment. The Court never reached the second question, because the Court answered the first question — the question of whether a State is a "person" — in the negative.

In facing that question, the Court, in an opinion by Justice Scalia, began with the "long-standing interpretive presumption that 'person' does not include the sovereign." 120 S.

Ct. at 1866-67. As the Court explained, the presumption excluding States is not a "hard and fast rule," but is one that may be "disregarded only upon some affirmative showing to the contrary." Id. (quotations and citations omitted).

In determining whether there was any indication to the contrary in the case of § 3729(a), the Court notably began by examining the FCA, not as amended in 1986, but as it existed in its original, 1863 form. Id. at 1867. The Court explained that it was using the 1863 Act as its point of departure because "the term 'person' has remained in the statute unchanged since 1863." Id. at 1868 n.12.[2] After examining the text of the 1863 Act, id. at 1867, and the legislative history of the 1863 Act, id. at 1868 n.12, the Court found no basis for departing from the presumption that a sovereign is not a "person." Id. at 1867-68.

Having found that, in 1863, Congress had not intended the term "person" to apply to States, the Court then inquired whether the 1986 amendments to the FCA evinced an intent to alter the FCA by expanding it to make States suable as "persons." Several factors convinced the Court that no alteration was intended.

First, the Court noted that the new civil investigative demand ("CID") section of the FCA (allowing the Attorney General to issue an investigative demand to "any person … possess[ing] information relevant to a false claims law investigation," 31 U.S.C. § 3373(a)(1)) included a definition of "person" that did include States for the purposes of that section — and only that section. 120 S. Ct. at 1868, citing 31 U.S.C. § 3733(*l*)(4). And, the Court reasoned, the inclusion of a broad definition of "person" in the CID section, combined with the exclusion of any special definition applicable to the balance of the Act, suggested an intent to leave the general presumption concerning the meaning of "person" in place in § 3729(a). Id. at 1868-69.

Second, the 1986 Amendments increased damages for violations of the Act from double damages plus a $2000 civil penalty per false claim, see 31 U.S.C. § 231 (1976 ed.), to treble damages plus civil penalties of $5,000 to $10,000 per false claim. See 31 U.S.C. § 3729(a), and thereby made the FCA's remedies "essentially" punitive in nature. The Court found that, given the presumption against imposing punitive damages against governmental entities, Congress' decision to increase liability was inconsistent with a design to expand the definition of "person" to include States. See Stevens, 120 S. Ct. at 1869 (citing Newport v. Fact Concerts, Inc., 453 U.S. 247, 262-63 (1981), for the presumption against government entity punitive liability).

Third, the Court noted that the Program Fraud Civil Remedies Act of 1986 ("PFCRA"), which provides a scheme for administrative remedies for false claims, contains a definition of "person" that does not include States. Id. at 1870; 31 U.S.C. § 3801(a)(6) ("person"

defined as "any individual, partnership, corporation, association, or private organization"). The Court reasoned that if the 1986 Congress wished for the first time to subject States to liability for false claims, it would be "most peculiar" to assume that the legislature wished to do so by subjecting States to a statute with a treble damage remedy (the FCA), but not to a statute with more modest remedies (the PFCRA). Id. at 1870.

Given these indicia of the 1986 Congress' intent, and given the sparse changes the 1986 amendments made to the language immediately surrounding the word "person," see note 2, supra, the Court held that "person" as it is used in §3729(a) of the FCA does not include States. Id.

Thus, the central reasoning of Stevens can be summarized in the following points:

(1) At the time of the FCA's passage in 1863 the term "person" presumptively excluded sovereign States.
(2) There was nothing in the text or legislative history of the 1863 Act that indicated a Congressional intent to alter the presumption excluding States as "persons."
(3) The 1986 Amendments to the FCA indicate no intention on the part of Congress to alter the definition of "person" as it existed in the 1863 Act.

II. SUITS AGAINST MUNICIPALITIES AND OTHER LOCAL GOVERNMENT ENTITIES

The essential consideration which led the Stevens Court to conclude that a State is not a § 3729(a) "person" — namely, that the 1986 Congress did not intend to alter the 1863 Congress' understanding of that word — serves to establish that a municipality or other local government entity is a "person" within the meaning of that provision.

A.

We start with the proposition that, by the time the FCA was initially enacted in 1863, the law was settled that the term "person" presumptively included municipalities. The Supreme Court's decision in Monell v. New York City Dept. of Social Services, 436 U.S. 658, 687 (1978), makes this clear.

The question presented in Monell was whether a municipality was a "person" for the purposes of § 1 of the Civil Rights Act of 1871, 42 U.S.C. § 1983, which subjects to liability "any person" who, under color of law, subjects another to a "deprivation of any [civil] rights." In holding that a municipality was a "person," the Monell Court began with the observation that "[b]y 1844" — after a period of some controversy over the matter — the doctrine that corporate entities were "persons" had become clearly established in American jurisprudence. Monell, 436 U.S. at 687-88 (citing Louisville R. Co.

v. Letson, 2 How. 497, 558 (1844)). The Court noted further that throughout the 1844-1871 period, municipalities were routinely sued as "persons" in federal courts without any special definition of that term. Monell, 436 U.S. at 688.[3] And, the Court added, this understanding of the term "person" was "well known to Members of Congress." Id. (quoting the statement of Representative Shellabarger that "counties, cities, and corporations of all sorts, after years of judicial conflict, have become thoroughly established to be an individual or person or entity of the personal existence").

Given the prevailing understanding in 1871 that persons included corporations and that corporations in turn included municipal corporations, and given that there was nothing in the text or legislative history of the 1871 Civil Rights Act pointing to a departure from that understanding, the Monell Court concluded that the word "person" in the 1871 Act was properly read to include municipalities. Id. at 688. See also Newport v. Fact Concerts, Inc. 453 U.S. 247, 259 (1981) ("It was generally understood by 1871 that a municipality, like a private corporation, was to be treated as a natural person subject to suit"); Owen v. City of Independence, 445 U.S. 622, 638-39 (1980) ("by 1871, municipalities — like private corporations — were treated as natural persons for virtually all purposes of constitutional and statutory analysis"). See also Chattanooga Foundry & Pipe Works v. Atlanta, 203 U.S. 390 (1906) (concluding that it was clear from the fact that "person" in the 1890 Sherman Antitrust Act was defined to include "corporations," see 26 Stat. 209, 210, that the statute likewise was intended to encompass municipal corporations).

The recognition in the mid nineteenth century that municipalities were "persons" equally amenable to suit as other corporations coincided with the demise of the doctrine that municipal entities were "sovereigns" entitled to invoke the defense of sovereign immunity, or to invoke related privileges and immunities available only to sovereigns, such as Eleventh Amendment immunity from suit in federal court. See Will v. Michigan Dept. of State Police, 491 U.S. 58, 67 (1989) ("by the time of the enactment of [the 1871 Civil Rights Act], municipalities no longer retained the sovereign immunity that they had previously shared with the States"); Newport, 453 U.S. at 259 n.19 (same); and see generally Lincoln County v. Luning, 133 U.S. 529, 530 (1890) (holding that municipalities lack Eleventh Amendment sovereign immunity).

Thus canons of statutory construction disfavoring the inclusion of "sovereigns" within the scope of statutes authorizing suit against "persons" — such as the canon invoked by the Supreme Court in Stevens, 120 S. Ct. at 1867-68 — have no application in the case of municipalities. This was made explicit in Will v. Michigan Dept. of State Police, where the Court held that the word "person" in 1871 included corporations — including public corporations — but not States. 491 U.S. at 69 & n.9 ("[a] public corporation, in ordinary usage [at the time of the 1871 Civil Rights Act], was another term for

a municipal corporation," which in turn "included towns, cities, and counties, but not States"). See also Alden v. Maine, 119 S. Ct. 2240, 2267 (holding that an important limit to the principle of sovereign immunity is that "it bars suits against States but not lesser entities").

The reasoning in Monell and its progeny applies with equal force to the 1863 False Claims Act. The prevailing understanding in 1863 as in 1871 was that "person" included corporations — including municipal corporations. And, the Supreme Court in Stevens itself held that there was nothing in the text of the 1863 version of the FCA that would "cast doubt on the courts' assumption" in interpreting that version of the Act that the term "person" "extend[ed] to corporations." 120 S. Ct. at 1867-68. Nor is there anything in the text of the 1863 version to override the ordinary presumption that the term "person" was intended to extend as well to municipal corporations. Thus, the ordinary presumption applies, and municipalities were "persons" under the 1863 Act.

If the 1863 version of the FCA had contained a provision purporting to impose mandatory punitive damages, there might be reason to question this conclusion, given the presumption against interpreting statutes containing such provisions as applying to taxpayer-funded government entities. Cf. Newport v. Fact Concerts, supra; but see City of Lafayette v. Louisiana Power & Light Co., 435 U.S. 389, 396 (1978) (municipality may be held liable as a "person" under Sherman Antitrust Act notwithstanding that Act's apparently mandatory treble damages provision); Community Communications Co. v. City of Boulder, 455 U.S. 40, 50 (1982) (same); and see infra at 25 (further discussing relevance of Sherman Act cases).

The 1863 version of the False Claims Act, however, did not impose punitive damages. To the contrary, as the Supreme Court twice has held, the civil remedies provided in the 1863 Act — double damages and a civil penalty of $2,000 per false claim — were not punitive in nature but instead were designed only to make the Government completely whole for the losses occasioned by frauds.

The first occasion for the Supreme Court to address this point came in United States ex rel. Marcus v. Hess, 317 U.S. 537, 548-53 (1943). The question there was whether the Double Jeopardy clause of the Fifth Amendment barred a *qui tam* suit brought after the conclusion of a successful criminal prosecution. Central to the Court's holding that double jeopardy concerns were not implicated was the Court's determination that the 1863 FCA's civil remedies were not punitive in nature. See 317 U.S. at 548-53. The Court explained that "the chief purpose of the [Act's civil remedy provision] was to provide for restitution to the government of money taken from it by fraud, and that the device of double damages plus a specific sum was chosen to make sure that the government would be made completely whole." Id. at 551-52; see also id. at 149 ("[w]e cannot say that the

remedy now before us requiring payment of a lump sum and double damages will do more than afford the government a complete indemnity for the injuries done it").

Following the rationale of Hess, the Court in United States v. Bornstein, 423 U.S. 303, 315 (1976), held that the double-damage provisions of the predecessor Act were to be applied by doubling the amount of the defendant's overcharges before, rather than after, deducting any offsets, reasoning that "this method of computation comports with the congressional judgment that double damages are necessary to compensate the Government completely for the costs, delays, and inconveniences occasioned by fraudulent claims." 423 U.S. at 315 (emphasis added). See also Rex Trailer Co.v. United States, 350 U.S. 148, 152 (1956) (holding that statute with remedial provisions virtually identical to those in the 1863 Act was intended to provide compensatory and not punitive remedies); cf. United States v. Halper, 490 U.S. 435, 4466 (1989) (Congress "may demand compensation in somewhat imprecise formulas, such as reasonable liquidated damages or a fixed sum plus double damages, without being deemed to have imposed a … penalty"), overruled on other grounds by Hudson v. United States, 522 U.S. 93 (1997).

Therefore, because the 1863 FCA, as definitively construed by the Supreme Court, was not intended to impose punitive damages, the presumption against including governmental entities within the ambit of the term "person" simply does not apply to that version of the Act. Cf. Stevens, 120 S. Ct. at 1869-70 (holding that treble damage provisions, unlike double damages provisions, are "essentially" punitive in nature); see also supra at 17. Because that presumption does not apply, and because there is no other basis for believing that the 1863 Congress intended to depart from the prevailing understanding that the term "person" included municipal corporations, see Monell, supra; Will, supra, it follows that the 1863 FCA's provision making "any person" liable to the United States for false claims encompassed municipal corporations.

That, of course, does not end the matter, since the question of present concern is not whether municipalities were "persons" within the meaning of the 1863 version of the FCA, but whether they are "persons" now under the 1986 Act. Nevertheless, if the current FCA, and in particular the current 31 U.S.C. § 3729(a) does not include municipalities within the scope of the term "person," this can only have been the product of the modifications made by Congress in 1986, and of an intent by the 1986 Congress to restrict the reach of § 3729(a).

Such a view of Congress' intent would, however, contradict the fundamental premise of Justice Scalia's opinion in Stevens — viz., that, because the 1986 Congress made no significant changes to the operative language of § 3729(a), the 1863 understanding of the term "person" in the precursor to § 3729(a) carries over into the 1986 Act and contin-

ues to govern. Stevens, 120 S. Ct. at 1867-8 & n.12. Justice Scalia made it clear that this was his central premise in a critical footnote responding to the dissent:

> The dissent claims that "[t]he term `person' in §3729(a) that we are interpreting today was enacted by the 1986 Congress, not by the 1863 Congress." But the term "person" has remained in the statute unchanged since 1863; the 1986 amendment merely changed the modifier "[a]" to "[a]ny." This no more caused the word "person" to include States than did the replacement of the word "any" with "[a]" four years earlier.

120 S. Ct. at 1868 n.12 (emphasis added).

At this juncture in the Court's opinion, the Court, to be sure, did go on to discuss various provisions of the 1986 Act — including, most significantly, the provision that created treble damages liability and increased the penalties for submitting false claims. But in that portion of the Court's opinion, the Court simply was identifying an aspect of the 1986 Act that supports the Court's basic conclusion that the 1986 Amendments were not intended to expand the universe of § 3729(a) "persons" to include States for the first time. 120 S. Ct. at 1869-70. As noted above, the Court, after citing the Newport v. Fact Concerts presumption concerning punitive damages, reasoned that if the 1986 Congress had intended for the first time to subject States to liability for false claims, it would have been out of the ordinary for the legislature to have done so by subjecting them to treble damages. The Court, however, nowhere indicated that the addition of a treble damages remedy demonstrated any intent on the part of the 1986 Congress to contract the universe of § 3729(a) "persons" amenable to suit.

Indeed, in the case of a statute (such as the FCA) in which a remedy asserted to be "punitive" is introduced by way of an amendment enacted well after the decision has been made by an earlier legislature to subject "any person" to suit, it makes no sense to apply the Newport presumption as an aid to construing the term "person." The presumption is based on the hypothesis that, all other things being equal, a single legislature is unlikely to simultaneously (a) impose punitive damages liability and (b) make the category of "persons" subject to suit broad enough to include government entities. The hypothesis falls apart when two different legislatures are involved, and when the legislature that adds the punitive damages remedy has done so against a backdrop of decisional law (such as here, the Monell line of cases) clearly holding that a particular type of entity (here, a municipality) already was covered by the term "person."

Moreover, given the legislative history and the overall direction of the 1986 Amendments, it is particularly untenable to maintain that, by expanding the remedies to treble damages, the 1986 Congress sub silentio narrowed the scope of the term "person."

The only legislative history concerning the "person" issue in the 1986 Act is a passage in the Senate Report accompanying the Act which states that the pre-amendment FCA applied to "political subdivisions" of States as well as to "States" themselves. S. Rep. No. 99-345 (1986) ("Senate Report"), p. 8; U.S.C.C.A.N. 1986, p. 5273. While this passage cannot, in light of Stevens, be invoked as authority for the proposition that Congress intended to broaden the scope of the term "person" beyond the pre-1986 understanding, see Stevens, 120 S. Ct. at 1868 n.12 (noting that the passage was wrong as to the pre-existing case law concerning States), the passage severely undercuts any notion that Congress intended to actually narrow the scope of that term.

Furthermore, the entire thrust of the 1986 Amendments was to extend, rather than curtail, the reach of the FCA. One reads the text of those Amendments and their legislative history in vain for any indication of an intent to narrow the application of the Act in any regard. Every single change made to the statute in 1986 reflects the view, repeated throughout the legislative history, that the previous statute was inadequate to the task of combating the "rampant fraud" that was then plaguing Government programs, and that strong and vigorous new measures were needed across the board. S. Rep. No. 99-345 (1986), p.4, reprinted in 1986 U.S.C.C.A.N., p. 5269.

To identify just a few of the most significant changes, the 1986 Amendments (i) expanded the availability of *qui tam* suits under the Act by replacing the old "government knowledge" bar with a substantially more liberal "public disclosure" bar; (ii) relaxed the scienter requirement applicable to all FCA suits by abrogating the doctrine in many circuits that "specific intent" was required to establish liability; (iii) created a new cause of action for so-called "reverse" false claims (i.e., frauds involving the avoidance of an obligation to the Government); (iv) created a retaliatory discharge cause of action for persons terminated for bringing or assisting in the bringing of *qui tam* suits; (v) lowered the burden of proof from the "clear and convincing" standard that had prevailed in some circuits to a "preponderance of the evidence" standard; (vi) made *qui tam* suits more attractive by making the award to the relator mandatory rather than discretionary and by increasing the percentage of the Government's recovery that must be paid to the relator; (vii) made attorneys' fees available to successful relators; and (vii) increased the damages and penalties for submitting false claims. See Pub. L. No. 99-562, 100 Stat. 3153, §§ 1-8 (1986).

Read in the light of this uniform and comprehensive drive toward making the 1986 FCA a more potent statute than its predecessor, it becomes especially evident that Congress did not intend in 1986 to cut back on the class of persons who could be sued under the FCA.

B.

The only authority that we have found which takes the position municipalities are not § 3729(a) "persons" is the district court decision in United States ex rel. Graber v. City of New York. 8 F. Supp.2d 343, 348-56 (S.D.N.Y. 1998). That decision, however, relies on an approach to interpreting § 3729(a) that is clearly inconsistent with the Supreme Court's approach in Stevens. In particular, the court in Graber considered the text of the 1986 FCA without regard to the fact that § 3729(a) left unchanged the operative language adopted by the 1863 Congress. With that ahistorical premise as its starting point, the Graber court, though acknowledging that municipalities were understood to be persons at common law, found in the 1986 Act's "punitive" treble damages provision an indication that the 1986 Congress had intended to override the traditional understanding. That analysis, as we have said, cannot be squared with the view of the Court majority in Stevens that the 1863 Congress' understanding of the term "person" was carried over into the 1986 Act.

Nor should the result that a municipality is a "person" within the meaning of § 3729(a) be altered by cases interpreting other statutes to exclude municipalities from the meaning of "person." For example, a handful of courts have held that a municipality may not be held liable under the civil provisions of the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. §§ 1961-1968, because of the common-law presumption described in Newport against holding municipalities liable for punitive-type damages. See Genty v. Resolution Trust Corp., 937 F.2d 899, 914 (3rd Cir. 1991) (concluding that it "perceive[d] no intention" on the part of the 1970 Congress that enacted RICO "to abrogate the … principle of common law prohibiting punitive damages against municipalities."); Dammon v. Folse, 846 F. Supp. 36 (E.D. La. 1994); Massey v. Oklahoma City, 643 F. Supp. 81 (W.D. Okla. 1986).

Unlike the FCA, however, RICO's treble damage provision and its provision identifying suable "persons" were adopted at the same time by the same legislature, and both provisions were in the statute from its inception. Thus, it arguably makes sense in interpreting RICO's use of the term "person" to consider the Newport presumption against imposing punitive damages on municipalities. In the case of the FCA, by contrast, the proper mode of inquiry, as Stevens teaches, is to ask first whether, as originally enacted, the statute's use of the term "person" included municipalities; and to ask next if the 1986 Act's inclusion of a treble-damages remedy evinced an intent to alter that understanding. As we have explained, since the damages available under the 1863 FCA were remedial in nature, and since there is no hint that the 1986 Congress intended to alter the traditional understanding that "persons" included municipal corporations, there is no basis for construing the term "person" in § 3729(a) as excluding municipalities.

Quite apart from this, Genty and its progeny are suspect on their own terms in that they overread Newport's principle forbidding assessment of punitive damages against gov-

ernment entities absent a Congressional intention to the contrary. Most significantly, those cases do not take adequate account of the fact that, even where a statute has provided for treble damages from the first — as in the case of the 1890 Sherman Antitrust Act — the Supreme Court has not reflexively excluded municipalities from the class of suable "persons."

Thus, in City of Lafayette v. Louisiana Power & Light Co, the Court held that a municipality is liable as a "person" under the Sherman Act, and that the question of whether a municipality may further be held liable for treble damages under that statute did not have to be decided in order to reach the conclusion that municipalities were "persons." Lafayette, 435 U.S. 394-97 & 402 n.22. The Court adopted this position over the dissent of Justice Blackmun, who expressed concern that the Sherman Act's apparently mandatory treble damages provision would be applied to taxpayer-supported entities.

Moreover, four years later, the Supreme Court, having decided Newport v. Fact Concerts in the interim, reaffirmed Lafayette's holding that municipalities are Sherman Act "persons," and again reserved the question of application of the treble damages remedy, Community Communications v. City of Boulder, 455 U.S. at 56-57 n.20 — this time over the dissent of Justice Rehnquist. In his dissent, Justice Rehnquist expressed the view that it would "take a considerable feat of judicial gymnastics to conclude that municipalities are not liable for treble damages" under the Sherman Act given the damage provision's apparently mandatory language. Boulder, 455 U.S. at 65 n.2 (Rehnquist, J., dissenting). The majority, however, adhered to the view that the "person" issue and the treble damages issue were not inextricably linked in the case of municipalities, and suggested that municipalities might have some special defense to treble damages that is not available to private defendants. 455 U.S. at 56-57 n.20.

Thus, whatever the validity of the dissenters' policy concerns in the antitrust decisions,[4] it remains the case that the Court has twice held that the existence of a mandatory treble damages provision in a statute does not establish a sufficient basis for narrowing the definition of the term "person" to exclude municipalities.

Nonetheless, the Third Circuit in Genty — despite acknowledging that RICO's civil remedies were modeled after those of the antitrust laws — relied on Justice Rehnquist's dissent in Boulder for the proposition that a municipality could not be liable as a "person" under RICO, instead of relying the Court's opinions both in that case and in Lafayette. See Genty, 937 F.2d at 914. Genty therefore not only is distinguishable (by reason of the different circumstances under which the RICO and FCA "person" and treble damages provisions developed), but is based on reasoning actually rejected by two Supreme Court holdings.

In sum, the FCA must be construed to include a municipality as a "person" in § 3729(a). At the time the statute initially was enacted, the accepted construction of that term included a municipality. Later, in 1986, Congress evinced no intention to disturb the existing definition of "person." Rather, Congress' principal aim was to increase the liability of any person, including a municipality, who violated the Act.[5]

III. SUITS AGAINST PROPRIETARY/INDEPENDENT STATE ENTITIES

There are a great number of State-affiliated entities that, although governmental in nature, are financially independent from the State that created them and to a large degree autonomous from the State. Although the term is somewhat awkward, we will refer to such bodies in this Part as "proprietary/independent" government entities, since neither "proprietary" nor "independent" provides an accurate shorthand description of the type of entity involved.

Some, but not all, hospitals, transit authorities, water resource authorities, and educational institutions fall into this category, as do numerous other categories of quasi-governmental entities. The key word here is "some," because not all States fund, control, and operate their hospitals, universities, transit authorities, and the like in similar ways.

As to those State entities that are controlled by the State government and funded through general State taxpayer revenues — such as the Vermont Agency of Natural Resources in Stevens — it is clear that, under Stevens, such entities are not "persons" subject to suit under the FCA in a pure *qui tam* action.

As to those State entities that are not so controlled and so funded — as to those entities that, in other words, are proprietary/independent entities rather than "arms of the State" — the case law indicates that such entities are "persons" subject to *qui tam* suit.[6] That conclusion can be reached by either of two separate and distinct lines of reasoning.

A.

The first line of reasoning which establishes that proprietary/independent government entities are "persons" essentially duplicates the analysis spelled out in Part II of this Article, and it proceeds as follows.

In 1863 when the FCA originally was enacted, state government entities that were neither States themselves nor mere "arms" of a State held the status, not of "sovereigns" entitled to a presumption against being subject to suit, see Stevens, 120 S. Ct. at 1866, 1870, but instead of ordinary corporations that were subject to a presumption in favor of being subject to suit as "persons." That such entities were "persons" and not "sovereigns" flows directly from Monell, which, in the course of holding that municipalities were uniformly

considered to be "persons" from as early as 1844, also made it clear that other government entities lacking status as States or as "arms of the State" were considered to be "persons" as well. See Monell, 436 U.S. at 690 n.54 (the term "person" includes "local government units which are not considered part of the State for Eleventh Amendment purposes"); Will v. Michigan Dept. of State Police, 491 U.S. 70 (the doctrine excluding "sovereigns" from the scope of the term "person" "applies only to States or governmental entities that are considered 'arms of the State' for Eleventh Amendment purposes") (emphasis added.); see also id. at 67-68 & n.9; cf. Alden v. Maine, 119 S. Ct. at 2267 ("sovereign immunity … does not extend to suits prosecuted against a municipal corporation or other governmental entity which is not an arm of the State").[7]

Because the principle of Monell extends to proprietary/independent government entities, the same considerations that establish that municipalities were "persons" within the purview of the 1863 FCA — i.e., that the 1863 FCA was passed against the same legal backdrop as the 1871 Civil Rights Act, and that the FCA's original damages provisions were remedial rather than punitive in nature so that the Newport presumption concerning "punitive" statutes does not apply, see supra at 22, 24 — establish as well that proprietary/independent government entities likewise were "persons" within the purview of the 1863 FCA. And, once it established such entities were "persons" under the 1863 FCA, it follows from the balance of the analysis set out in Part II of this Article that such entities remain "persons" under the 1986 FCA. As recounted in detail in that Part, the 1986 Congress made no change to the original 1863 FCA's provision establishing the class of "persons" subject to suit, and there is nothing in the text or legislative history of the 1986 Amendments suggesting that Congress somehow tacitly intended to narrow that class. Accordingly, proprietary/independent entities are "persons" under the current FCA.

B.

As indicated above, there is an alternative line of reasoning that supports the proposition that proprietary/independent government entities constitute § 3729(a) "persons" under the 1986 FCA. In this line of reasoning, such entities are "persons" even under the assumption that it is the 1986 FCA's remedial provisions, rather than the 1863 FCA's remedial provisions, that are to be consulted in determining the applicability of the Newport presumption against imposing punitive damages. This reasoning is that the Newport presumption, regardless of its effect on the status of ordinary government entities, would not affect the status of proprietary/independent government entities, since such entities — practically by definition — do not draw from general taxpayer revenues when called upon to pay damage judgments, including "punitive" damage judgments.[8]

In developing this point, we start with Newport itself. The question in Newport was whether 42 U.S.C. § 1983 — which three years earlier in Monell already had been inter-

preted to apply to municipalities — permitted awards of punitive damages against municipalities. The Court answered that question in the negative, reasoning that punitive damages are not "sensibly assessed" against ordinary government entities (i) because damages awarded against such entities are borne by taxpayers and do not achieve the "retributive" or "deterrent" aims that usually justify exemplary damages; and (ii) "[b]ecause … the unlimited taxing power of [an ordinary government entity such as a municipality] may have a prejudicial impact on the jury" and lead to a "windfall recovery" to the plaintiff that is likely to be "unpredictable, and, at times, substantial." See 453 U.S. at 267-71.

These concerns — though very real in cases involving ordinary taxpayer-supported government entities and statutes that impose no limits on the amount of punitive damages or the criteria used to set them — are not present in cases involving proprietary/independent government entities arising under statutes (like the FCA) that set their "punitive-type" damage awards according to a predetermined formula.

First, unlike in the case of an ordinary government entity — where an award of punitive-type damages does not achieve its retributive purpose because the award would ultimately be borne by "unknowing" taxpayers whose only connection to the government entity is that they reside within its jurisdiction, see Newport, 453 U.S. at 267 — in the case of a proprietary/independent government entity, the award is not passed along to such an entirely disconnected group, because the entity, as we have emphasized, draws its funding from its own operations or from other voluntary, non-taxpayer sources.[9] See Barnett v. Housing Auth. of Atlanta, 707 F.2d 1571, 1581 (11th Cir. 1983) (indicating in dicta that Newport's rationale does not extend to financially independent state entities); but see Bolden v. SEPTA, 953 F.2d 807, 831 (3rd Cir. 1991) (en banc) (holding to the contrary).

Similarly, unlike in the case of an ordinary government entity — where an award of punitive-type damages does not achieve its deterrent purpose because there is reason to assume that corrective action against the responsible parties would occur even in the absence of punitive damages, 453 U.S. at 269 — in the case of a proprietary/independent government entity which is responsible for its own financial soundness, the prospect of punitive damages is apt to deter wrongdoing and to do so in exactly the same manner as it does in the case of private corporations.

In addition, the Newport Court's repeated concern regarding the unpredictable and potentially unlimited punitive damage liability that could result if juries were permitted to base awards on the wealth and tax-revenue generating power of a municipal government, see 453 U.S. at 268, quite simply is inapplicable in cases where the damages are not set by a jury influenced by the wealth or power of the defendant, but are set by the court according to a

predetermined statutory formula such as the FCA's designed to keep the ultimate award in proportion both to the actual damages and to the degree of wrongdoing.

For these reasons, even if it were considered appropriate to interpret the 1986 FCA divorced from its non-punitive 1863 antecedent and thereby to determine the meaning of "person" by reference to the canon of statutory construction applicable to punitive statutes, the pertinent canon still would provide no support for the proposition that proprietary/independent State government entities are not suable "persons." And, that being so, there is no basis for departing from the ordinary understanding, recognized in Monell and its progeny, that such State entities are suable "persons" within the meaning of the FCA.

As a final point, we note that it follows as a matter of course — given the proposition that State proprietary/independent entities are suable as "persons" regardless of the applicability of the Newport presumption — that local proprietary/independent entities are suable as "persons" as well. Both types of entities, by hypothesis, draw their funding and pay their judgments from sources independent of taxpayer-generated general treasury funds. Thus, even if one were to conclude that, by reason of the Newport presumption, municipalities themselves were not "persons," it would nevertheless be the case that municipal entities which are not mere "arms" of a municipal government are § 3729(a) "persons."[10]

IV. INDIVIDUAL CAPACITY SUITS

On any conceivable reading of Stevens, it is clear that FCA suits can be maintained against a State or local government employee who is responsible for the submission of false claims on behalf of her government employer, provided that the suit is brought against the employee in her individual capacity. Since the employee herself is a natural person — a "person" in the most basic sense of the term — there is no sovereign immunity or other similar obstacle to such a suit.

Any doubt on that score is erased by Hafer v. Melo, 502 U.S. 21 (1991). In Hafer, the Supreme Court confirmed that a state officer sued in his individual capacity may be held personally liable for damages as a "person" under 42 U.S.C. § 1983 based upon actions taken in his official capacity. Id. at 312. The Court reasoned that, in contrast to official-capacity suits, which "generally represent only another way of pleading an action against an entity of which an officer is an agent," "[p]ersonal capacity suits …seek to impose liability upon a government officer" rather than the government itself. Id. at 25. Thus Hafer makes clear that the concerns that often lead courts to construe "person" to exclude the government itself do not exist when it is an individual government employee's personal liability that is in issue.

Furthermore the text of the FCA itself strongly indicates that even federal government employees may be sued under 31 U.S.C. § 3729, because in §§ 3730(e)(1) and (e)(2), Congress carved out a narrow exemption prohibiting *qui tam* suits against "a member of the armed forces arising out of such person's service in the armed forces" and against "a senior executive branch official." These sections would make no sense if any and all government officials acting in their official capacities were outside the group of "persons" who could be sued as individuals. Careful exceptions for certain types of government employees/officials, of course, would be unnecessary if they were not "persons" to begin with.

What is more, the availability of an individual-capacity suit against a local government official under the FCA has already been recognized by at least one circuit court. See Smith v. United States, 298 F.2d 299 (5th Cir. 1961) (upholding FCA judgment against local government official sued in his individual capacity).

Nor could States defeat FCA claims against their employees by simply opting to indemnify their employees against loss. A State's voluntary decision to indemnify its employees does not create Eleventh Amendment immunity by converting an individual-capacity suit to one against the State's treasury. See Stoner v. Wisconsin Dept. of Agric., 50 F.3d 481, 483 (7th Cir. 1995) ("it would be absurd if all a state had to do to put its employees beyond the reach of section 1983 and thereby make the statute ineffectual … was to promise to indemnify state employees for any damages awarded in such a suit.") (citations and quotations omitted); accord Beardsly v. Webb, 30 F.3d 524, 531 (4th Cir. 1994); Cf. Regents of Univ. of Calif. v. Doe, 519 U.S. 425, 431 (1996) ("it is the entity's potential legal liability, rather than its ability or inability to require a third party to reimburse it … that is relevant.").[11] And by parity of reasoning, a State's voluntary decision to indemnify its employees does not convert them from suable "persons" to nonpersons under the FCA.

However, one question that arises in the context of individual-capacity suits is the availability of a defense for qualified or good faith immunity. The Court stated in Hafer that "officials sued in their personal capacities, unlike those sued in their official capacities, may assert personal immunity defenses such as objectively reasonable reliance on existing law." 503 U.S. at 25. Thus, under § 1983, an official sued in her individual capacity is immune from damages if her conduct does not violate "clearly established [law] of which a reasonable person would have known." Harlow v. Fitzgerald, 457 U.S. 800, 818 (1982).[12] However, given the intent standard required for a violation of the FCA, requiring, at minimum, a showing of "reckless disregard,"[13] it is unlikely that an official sued in her personal capacity would be protected by such qualified immunity. Virtually any violation of the Act would involve a degree of culpability that would satisfy Hafer's requirement that the conduct of the government employee violate a legal principle, duty, or reg-

ulation of which a reasonable person should have been aware. In addition, a recent circuit decision has held that a defense of qualified immunity is entirely unavailable against a claim for violation of the FCA's whistleblower protection provision, § 3730(h). Samuel v. Holmes, 138 F.3d 173 (5th Cir. 1998). There the court reasoned:

> qualified immunity seems particularly ill-suited, given the goals of the Act… [t]he FCA's purpose is to discourage fraud against the government, and the whistleblower provision is intended to encourage those with knowledge of fraud to come forward. Granting government officials the protection of qualified immunity would hardly spur reluctant employees to step forward.

Id. at 78. The policies behind the Act, therefore, also militate in favor of disregarding any defense of qualified immunity.

Whatever the legal viability of a *qui tam* claim against a state official in her personal capacity, the claim is of little value if the defendant cannot satisfy a judgment against her. In most circumstances, therefore, a plaintiff's best hope for recovery is a provision in state or local law that provides indemnification for liabilities incurred by an official acting within the scope of her governmental duties. It will be extremely important to investigate the nature of indemnification on a case-by-case basis. The scope of an official's right to indemnification will vary widely, and it is beyond the scope of this Article to provide a comprehensive treatment of the subject. We can only offer here some very broad outlines as to what issues may arise when considering statues that authorize indemnification of public employees.

Typically, an indemnification statute or ordinance will provide payment for damages caused by an official's wrongful acts done within the scope of employment. See Phillip E. Hassman, Validity and Construction of State Authorizing or Requiring Governmental Unit to Indemnify Public Officer or Employee for Liability Arising Out of Public Duties, 71 A.L.R.3d 90 § 2 (1976 & 1999 Supp.). Such provisions may cover a select group of employees (such as police or firefighters), while excluding others. Id. § 4.

Oftentimes, the statutes will exclude coverage for damages arising out of an official's willful and wanton misconduct. See id. § 24. Where such exclusions exist, they may force *qui tam* plaintiffs to tread a very thin line between arguing that the official's conduct was, on the one hand, "knowing," yet, on the other hand, did not rise to the level of being "willful and wanton," such that the statute would exclude coverage.

In addition, many indemnification statutes do not allow for recovery of punitive damages. See id. § 38. In that case, only partial recovery may be available. However, in light

of the Supreme Court's decision in Smith v. Wade, 461 U.S. 30 (1983), that punitive damages may be assessed under § 1983 for "reckless or callous indifference," some legislatures have expanded their indemnity laws to include coverage of punitive damage awards.[14]

As outlined above, personal-capacity suits provide an alternative option — albeit an imperfect one — for *qui tam* plaintiffs whose claims have been jeopardized by the decision in Stevens. It is important to reiterate, however, that any individual-capacity claim should be preceded by a thorough investigation of the applicable indemnification statute and any limitations or exclusions that could interfere with a full recovery.

CONCLUSION

While the Supreme Court's decision in Stevens has foreclosed pure *qui tam* suits against States and against State agencies that function as "arms" of the State, Stevens leaves open suits against lesser governmental entities as well as proprietary/independent government entities that do not draw on tax revenues to pay money judgments. It also leaves open *qui tam* suits brought directly against individual State employees. Finally, as Justice Ginsburg suggested in her concurring opinion, and as we address in a forthcoming Article, Stevens leaves open the possibility that even suits against States themselves remain viable when the Federal Government is a plaintiff.

ENDNOTES

[1] In a forthcoming article, we will address the last question. We simply note here that Justice Ginsburg, joined by Justice Breyer, wrote a concurring opinion in Stevens in which she stated that she "read[s] the Court's decision to leave open the question whether the word 'person' encompasses States when the United States itself sues under the False Claims Act." 120 S. Ct. at 1871 (Ginsburg, J., concurring).

[2] The Court noted that the only change made in 1986 to the language surrounding the term "person" was a change in the modifier before "person" from "[a]" — the modifier that had been in place from 1982-1986 — to "[a]ny" — the modifier that had been in place from 1863-1982. See id. at 1868 n.12. The Court further noted that the 1982 change was a pure "housekeeping" change not intended to have any substantive effect. Id.

[3] See also Monell, 436 U.S. at 688 n.49, 673, & 673 n.28 (citing Board of Comm'rs v. Aspinwall, 24 How. 376 (1861); Gelpcke v. Dubuque, 1 Wall. 175 (1864); Von Hoffman v. City of Quincy, 4 Wall. 535 (1867); Riggs v. Johnson County, 6 Wall. 166 (1868); Weber v. Lee County, 6 Wall. 210 (1868); Supervisors v. Rogers, 7 Wall. 175 (1869); Benbow v. Iowa City, 7 Wall. 313 (1869); Supervisors v. Durant, 9 Wall. 415 (1870); 6 C. Fairman, History of the Supreme Court of the United States: Reconstruction and Reunion, 1864-1888, chs. 17-18 (1971)).

[4] Soon after the Court's ruling in City of Boulder, Congress passed the Local Government Antitrust Act, Pub. L. No. 544, 98 Stat. 2750 (1984), which limited a local government entity's antitrust liability to single, rather than treble, damages.

[5] If, contrary to the argument in this Article, a court finds that the Newport presumption applies to the FCA, the best course would be that chosen by the Newport Court itself – namely, that the statute should, for reasons traceable to municipalities' common-law immunity from punitive damages, be interpreted to impose only compensatory damages on government entities rather than deeming them not to be "persons" at all. See 453 U.S. at 271. It is clear from the antitrust cases of Lafayette and Boulder that a complete bar to suit would be inappropriate.

We believe that the more natural reading of the language of the FCA, given its 1863 antecedent, is to read "person" as including municipalities, and to apply the FCA's treble damages remedy to all persons — including municipalities — since the FCA provides, with no pertinent exceptions, that a "person" who violates the Act "is liable to the United States for … 3 times the amount of damages which the Government sustains because of the act of that person." 31 U.S.C. § 3729(a). But if the choice had to be made, it would be more faithful to Congressional intent to deem the punitive liability provision inapplicable to municipal governments than to render such governments altogether exempt from liability for false claims.

[6] It is beyond the scope of this Article to provide a detailed analysis of the many factors that are used to determine whether a particular government entity is an "arm of the State." Such an analysis is provided in a number of treatises on federal civil rights law, including, e.g., Nahmod, Civil Rights and Civil Liberties Litigation: The Law of Section 1983 (West Group 1999). For the purposes of this Article, it suffices to note that the critical factor is whether the entity pays its judgments out of general taxpayer-revenue generated treasury funds. See note 8 infra.

[7] In the wake of Monell and Will, the federal courts as well as the state courts uniformly have concluded that the term "person" in the Civil Rights Act of 1871, 42 U.S.C. § 1983, was intended to encompass not only municipalities but also State-created entities that are not so fiscally and politically dependent on a State as to be considered mere "arms of the State." See, e.g., Christy v. Pennsylvania Turnpike Comm'n, 54 F.3d 1140 (3d Cir. 1995) (State turnpike commission subject to suit); Kovats v. Rutgers, The State University, 822 F.2d 1303 (3d Cir. 1987) (university funded in part by State subject to suit). See also Mancuso v. N.Y. State Thruway Auth., 86 F.3d 289 (2d Cir. 1996); Brotherton v. Cleveland, 173 F.2d 552

(6th Cir. 1999); Simon v. State Compensation Ins. Auth., 946 P.2d 1298, 1301-1303 (Colo. 1997) (collecting state cases on the "person"/"arm of the state" question under the 1871 Civil Rights Act).

[8] The test for determining whether a particular government entity is an "arm of the State" for the purposes of the Eleventh Amendment and 42 U.S.C. § 1983 includes a variety of factors, but every court of appeals to have addressed the matter has concluded that the critical factor is whether the entity in question operates in such a way that any judgment against it would be paid out of general State treasury revenues. In the Fourth Circuit, for example, the rule is that if the state treasury will pay the judgment, the entity is conclusively an "arm of the State," but if the treasury will not pay the judgment, then other factors must be considered. Harter v. Vernon, 101 F.3d 334, 339-40 (4th Cir. 1996). Other courts have appeal have adopted somewhat different tests, but, as we have said, none rejects the proposition that the source-of-payment factor is the critical one. See generally Hess v. Port Authority Trans-Hudson Corporation, 513 U.S. 30, 48, 51 (1994) (noting that "Courts of Appeals have recognized the vulnerability of the State's purpose as the most salient factor in Eleventh Amendment [arm-of-the-State] determinations" and citing several cases for that proposition).

[9] To be sure, the cost of the award may ultimately be borne by consumers or, in some cases, bondholders, but that fact holds true for punitive-type awards against any corporation, and it never has been suggested that statutes imposing punitive liability are presumed not to apply to ordinary corporations.

[10] Because, as stated in Part II of this Article, municipal governments are not "sovereigns" and do not have Eleventh Amendment immunity, there is no body of case law — and there has been no need for any body of case law — addressing whether particular municipal entities are "arms" of the municipality that established them. However, if, as a result of Stevens, the reasoning in Newport v. Fact Concerts concerning the policy against imposing punitive liability on taxpayer-funded municipal entities becomes an important part of the test for determining whether a particular entity is a "person" for FCA purposes, it can be expected that such a body of law will develop and will largely mirror the body of law that has developed to determine whether particular entities are arms of a State.

[11] See also Downing v. Williams, 624 F.2d 612, 625 (5th Cir. 1980), vacated on other grounds, 645 F.2d 1226 (1981); Wilson v. Beebe, 770 F.2d 578, 588 (6th Cir. 1985) (en banc); Ashker v. Calif. Dept. of Corrections, 112 F.3d 392, 395 (9th Cir. 1997); Greiss v. Colorado, 841 F.2d 1042, 1046-47 (10th Cir. 1988); Jackson v. Georgia Dept. of Transp., 16 F.3d 1573, 1577-78 (11th Cir. 1994).

[12] Under § 1983 some officials are entitled to absolute immunity for actions taken in certain contexts. However, absolute immunity is limited to those performing judicial, legislative, and prosecutorial functions, see Erwin Chemerinsky, Federal Jurisdiction § 8.6.2 (2d ed. 1994), and would likely have no application to violations of the FCA.

[13] Under 31 U.S.C. § 3729(b), a defendant is liable if she either "know[s]" that the claims she is submitting are false or "acts in reckless disregard of the truth or falsity of the information."

[14] See James D. Cole, Defense and Indemnification of Local Officials: Constitutional and Other Concerns, 58 Alb. L. Rev. 789, 807-809 (1995) (discussing changes in New York Law in light of Smith v. Wade).

The False Claims Act and Wall Street: How a *Qui Tam* Case Reformed the Municipal Bond Market

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In December 1993, Michael R. Lissack was on vacation in Florida and read a brief article in the financial press that aggravated him. The article reported that documents produced by a public agency in California had failed to turn up evidence that Merrill Lynch and Lazard Freres & Co. were engaging in illegal fee- and market-splitting arrangements. At that time, both banks were under active investigation for violations of securities laws in public finance transactions undertaken in Massachusetts and the District of Columbia.[1]

Lissack, an investment banker, knew that federal investigators were missing a much larger scandal by focusing on the fee-splitting allegations. He went to a pay phone near the beach and made an anonymous call to the U.S. Attorney's office mentioned in the article to let the government in on Wall Street's dirty — but very profitable — little secret. For several years, he told them, investment banks had engaged in systematic, industry-wide overpricing of securities sold in connection with certain municipal bond transactions. Hundreds of millions of dollars in illegal profits had been pocketed by Wall Street. Lissack stressed that these overpricing practices — known as "yield burning" — were the true scandal on Wall Street, for they infected thousands of transactions across the country and touched nearly every public issuer of municipal debt. Yield burning was hurting the Treasury, the bond markets, and the taxpayers far more than any market-splitting arrangement.

With that phone call, Lissack became determined to educate the government about one of the largest illegal schemes ever to have affected the municipal bond market.

Michael Lissack had enjoyed a stellar career as an investment banker at Smith Barney. He joined the firm's public finance department in 1981. Six years later he was the second youngest person to have been made a managing director in Smith Barney's history. With one phone call, he placed it all at risk.

In his first conversation with the U.S. attorney's office, and in four or five later telephone conversations, Lissack laid out the pricing fraud to the U.S. attorney's office and FBI agents. He explained how Wall Street's yield-burning practices were diverting hundreds of

millions of dollars from the Treasury into the pockets of Wall Street bankers. In the course of his anonymous conversations, Lissack gave the FBI the names of ten people, including himself, to interview about his overpricing allegations. His anonymity was important for he knew his job was at risk. Lissack was among the highest level Wall Street "defectors" to come willingly to the Government. Ten months later, the FBI asked Smith Barney's permission to interview him at their offices in connection with a public finance investigation. Lissack thought that the FBI was making its way down his list and had finally gotten to his name. He was surprised when they did not ask him a single question about yield burning.

As a consequence of this interview, Lissack came to the view that the Government would not act unless he first took action. In February 1995, Smith Barney terminated Lissack in major part because of his objections to the firm's business practices. A month later, Lissack filed a *qui tam* lawsuit under seal against numerous Wall Street and regional investment banks. Several days later, he accused the industry of improper yield burning in a front-page story of *The New York Times.* It was then that the government began to investigate his allegations.

Lissack's resolve, and the *qui tam* lawsuits he filed against numerous Wall Street and regional investment banks, resulted in a major multi-agency federal investigation and the payment, to date, of about $180 million by 20 investment banks to settle "yield-burning" charges. It also has brought Securities and Exchange Commission (SEC) sanctions against individual bankers, and an Internal Revenue Service (IRS) review of the tax exempt status of hundreds of tax free municipal bonds. Perhaps most importantly, Lissack's allegations have caused a fundamental change in the way state and local entities purchase investments from Wall Street.

I. WALL STREET'S YIELD-BURNING FRAUD

"Yield burning" refers simply to the artificial lowering of a security's yield by pricing it in excess of its fair market value. Yield and price have an inverse relationship: As the price of a security goes up, its yield goes down.

Yield burning came to have a more specialized significance for the securities industry in the early 1990s, however, for yield was "burned" in connection with transactions that are strictly regulated by federal law. As explained in detail below, securities purchased with the proceeds of tax-exempt municipal bonds must (1) be priced no higher than "fair market value," and (2) earn an aggregate yield that does not exceed that earned on the tax-exempt municipal bond. These regulatory restrictions and others grew out of a long history of abuse by Wall Street's public finance bankers.

Public finance concerns the financing of public projects — highways, subways, schools, bridges — through the underwriting and issuance of tax-exempt municipal bonds and the investment of those bond proceeds. Securities and tax laws intersect in the public

finance area and make it a field dense with regulations. Even so, the esoteric nature of public finance historically has created opportunities for investment banks to obtain extraordinary and illegal profits at the Government's and taxpayers' expense.

The "arbitrage" of public, tax-exempt bond proceeds is at the heart of the yield-burning fraud that Lissack exposed. Bond arbitrage occurs when any portion of the proceeds from a tax-exempt bond is used — either directly or indirectly — to acquire higher-yielding investments. State and municipal bonds receive the benefit of federal tax exemption (which effectively lowers the interest rates paid to bondholders and thereby lowers the municipalities' costs), and for that reason their bond proceeds may only be used in a manner that furthers the intended public purpose of the bond. The investment of tax-exempt bond proceeds for profit is not regarded as a valid public purpose and is strictly prohibited as a result. Issuers of tax-exempt bonds are barred from earning a higher yield on their investment of the bond proceeds than they pay in interest to bondholders. This prohibition is termed "yield restriction." Federal law requires that the Treasury be reimbursed for any "positive arbitrage" — or profit — that is obtained from the investment of bond proceeds at yields above the yield-restricted rate.

Arbitrage schemes have a long history on Wall Street. The proliferation of "invested sinking funds" in the 1970s, "blind pool" funds in the early 1980s, and "hedge bonds" in the late 1980s gave federal lawmakers great concern, for they all were created by Wall Street bankers to earn arbitrage profits. Progressively over this period, the Government tightened arbitrage regulations so that by 1989 it was impermissible to acquire arbitrage profits by investing bond proceeds at yields above the yield-restricted rate.

II. YIELD BURNING ON MUNICIPAL REFINANCINGS

The prohibition on investing bond proceeds for profit applies to initial bond issues as well as any subsequent refinancing. At times when interest rates fall, refinancing municipal bonds may make economic sense. Refinancing allows a public agency to capture interest rate savings by refinancing higher rate, outstanding municipal bonds with lower rate "advance refunding bonds."

As a general matter, falling interest rates in the period between 1990 and 1994 made advance refunding transactions an attractive means for municipal issuers to realize present value savings on bonds with "call" provisions that prevented their immediate redemption. Bond refinancing was a sensible alternative for municipal governments that had issued earlier bonds at much higher interest rates. From 1990 to 1995, nearly 8,100 tax-exempt advance refunding bonds were issued by municipal agencies in every state, as well as the District of Columbia, Puerto Rico, and the Virgin Islands. The aggregate value of advance refunding bonds issued during this five-year period was more than $261 billion.

Advance refunding transactions have two chief components, both of which are critical to achieving the maximum savings: (1) low-rate advance refunding bonds are issued and (2) the refunding bond proceeds are invested in an escrowed "defeasance" portfolio of U.S. Treasury securities that is used to make interest and principal payments on the prior, higher rate "refunded" bonds. Federal law requires that escrow investment yields that create "positive arbitrage" - *i.e.*, yields above the restricted rate - must be rebated to the Treasury lest the entire tax exempt bond issue be deemed taxable. Yield restrictions on escrow investments, thus, are the means by which the government regulates profit-taking and speculation through bond arbitrage.

Issuers have two alternative means of achieving the yield-restricted rate and rebating positive arbitrage to the Federal Treasury. They may invest all of the refunding escrow in "State and Local Government Series" bonds (SLGS), which pay varying interest rates — including no interest — and which are sold by the federal government's Bureau of Public Debt. Issuers may subscribe to the Bureau to purchase SLGS bonds that will earn the exact yield-restricted rate. Thus, issuers that choose to invest all of the defeasance escrow in SLGS have no risk of violating the prohibition on bond arbitrage.

Alternatively, issuers may invest the escrow in higher-yield open market Government bonds and then "blend" the investments down to the yield-restricted rate by purchasing no-interest SLGS in the final period of the escrow. An escrow invested in this manner makes "profit" from the open market bonds in the early maturity years, which is recaptured by the Government in the form of no-interest SLGS in the escrow's final maturity years. No interest SLGS allow yield-restricted investments to be blended with precision and thus assure that the federal government will not pay higher interest on escrow investments than a municipal government pays on its tax-exempt bonds. The "blended" escrow yield requirement was designed to ensure that the Government would recover any positive arbitrage that it paid on open market bonds in a defeasance escrow's early years, by paying no interest on SLGS in the escrow's final years.

In contrast, escrow yields that are below the refunding bonds "restricted rate" create "negative arbitrage," which causes the issuer to suffer a dollar-for-dollar loss in present value savings. Because inflated security prices will artificially depress investment yields, federal law also mandates that refunding escrow investments be priced at their "fair market value." These regulations are intended to prevent positive arbitrage profits from being diverted from the federal Treasury by dealers inflating escrow investment prices and "burning yield" down to, or below, the refunding bonds' restricted rate. Fair market pricing of refunding escrow investments is essential to maintaining the tax-exempt status of advance refunding bonds.

In short, maximum savings are achieved when the escrowed Treasury securities earn the highest yield allowed by federal law, and federal law is satisfied when escrow securities are priced fairly and positive arbitrage is rebated to the U.S. Treasury.

III. A FEDERAL INVESTIGATION OF SYSTEMATIC YIELD BURNING PRACTICES IS LAUNCHED

Lissack's allegations were sweeping and direct. He asserted that the securities industry and investment bankers across the U.S. systematically stole positive arbitrage owed to the federal government on refunding escrows by selling overpriced Treasury securities to unsuspecting bond issuers who relied on their representations of fair pricing. Never before had the workings of Wall Street's public finance banking been subject to such scrutiny on an industry-wide basis.

Lissack anticipated that the investment banks would try to defend their high security prices by contending that refunding transactions were "risky" and justified high markups.[2] He understood that it was for us, his *qui tam* team, to move swiftly and to establish empirically that Wall Street opportunistically and unfairly inflated security prices in a manner unrelated to risks. The relator's team saw a potential chink in the Street's likely "transaction risk" defense: About 15 percent of advance refunding escrows were purchased on a competitive bid, rather than a sole-source, basis. It was Lissack's experience that, in most cases, competitively purchased escrow securities were priced with very little markup over cost, while sole-source purchases were loaded with undisclosed price markups. Because competitive and sole source transactions held identical transaction risks, a demonstrable differential in price markups would establish that high prices were not related to transaction risks, but only to the method of sole-source purchase.

Surprisingly, no empirical or academic study had previously examined the valuation and pricing of U.S. Treasury securities. Starting from scratch in March 1995, the *qui tam* team requested public bond transaction documents from issuers across the country. By the end of 1995, requests had been made to more than 500 issuers. Materials were received for several hundred transactions. With our expert economists, the sole-source and competitive transactions were closely analyzed and priced using daily published high/low/close prices. More than 1,900 individual Treasury securities were priced and analyzed, each using three different sets of pricing assumptions. The validity of our analysis was rigorously tested with multiple regression analyses.

This pricing analysis resulted in several simple but compelling conclusions:

- In the period between 1990 and 1995, Wall Street investment banks consistently overpriced Treasury securities purchased for municipal advance refunding escrows on a sole-source, non-competitive basis.
- The most conservative economic analysis showed that sole-source refunding escrow transactions were burdened with average price markups of over $4 for every $1,000 of a par bond.
- Treasury securities purchased for advance refunding escrows on a competitive basis were, in contrast, priced with an average markup of just 3 cents over published market prices.

The transactions analyzed by the *qui tam* team were similar in all essential respects and risks. Only the method of security purchase was consistently different.

The pricing analysis not only established the "fair market pricing" of Treasury securities for the first time, but most importantly for the litigation it left Wall Street without a tenable "risk" defense.

IV. OPENING A SECOND FRONT

In August 1995, the *qui tam* team opened a second front in the yield-burning litigation by filing a California False Claims Act case on behalf of the Los Angeles County Metropolitan Transportation Authority (LAMTA) against Lazard Freres & Co. The action arose out of Lazard's fraudulent sale of overpriced U.S. Treasury securities to the LAMTA in connection with an advance refunding in April 1993.

Unbeknownst to LAMTA, Lazard's prices on this single transaction were close to $4 million over fair market value. In fact, Lazard's prices were so excessive that not only did they "burn" all the "positive arbitrage" owed to the federal government, but they also caused about $3 million in "negative arbitrage" damages to be suffered directly by the LAMTA.

Lissack again initiated the action. LAMTA joined in 1996 and hired Lissack's legal team[3] to represent the agency as well. The case presented a unique opportunity, both because *qui tam* counsel was in control of prosecuting the entire action and because a success in California would certainly influence events in the federal action.

V. PARALLEL FEDERAL INVESTIGATIONS INCREASE THE PRESSURE

Since advance refunding transactions also are governed by federal securities and tax laws, the SEC and IRS had their own interests in taking enforcement action against yield-burning investment banks. The involvement of multiple agencies, each with its own perspective on the fraudulent conduct, was unique. While DOJ was interested in recovering the Treasury's losses through a False Claims Act remedy, the SEC was charged with protecting the integrity of the securities markets and investor interests. The IRS was concerned about the validity of public issuers' tax-exempt status. While there was interagency cooperation and collaboration throughout the litigation, the agencies' unique perspectives also were manifested in separate enforcement and regulatory actions.

The IRS first acted in the summer of 1996 by issuing a Revenue Procedure that would have placed the financial liability on public issuers — rather than on Wall Street — even though the municipal agencies in nearly all instances did not profit from yield-burning practices. Revenue Procedure 96-41 specifically provided that issuers that did not repay yield-burning profits on their transactions within a year would be subject to investigation and audit, and potentially the revocation of tax-exempt status.

The loss of tax exemption would be catastrophic for an issuer, for it would generate potentially huge tax liabilities for bondholders and cause tremendous instability in the

bond market. Not surprisingly, municipal governments were outraged that they were going to be forced to foot the bill for a yield-burning fraud that they neither participated in or knew about. They protested that holding state and local agencies accountable while Wall Street's yield-burning profits went unchallenged was fundamentally unfair.

Although the IRS deferred implementation of the Revenue Procedure, it continued investigating many dozens of individual refunding transactions. This scrutiny, coupled with the looming threat of losing tax-exempt status, created significant — albeit indirect — pressure on the Wall Street defendants. After all, it was the investment banks' own issuer-clients who were being squeezed to pay back profits enjoyed by the bankers. It was an uncomfortable position for bankers who wanted to maintain an ongoing business relationship.

Meanwhile, the SEC initiated multiple investigations of individual banks' yield-burning practices and filed its own action against an individual regional investment bank in January 1998. Securities and Exchange Commission v. Rauscher Pierce Refsnes and James Feltham, (D. Ariz. 1998). The complaint alleged that Rauscher Pierce's yield-burning overcharges on an Arizona refunding transaction violated various securities laws, including (1) Section 10(b) and Rule 10b-5 for Rauscher's failure to disclose material information and making false representations in connection with escrow price markups; (2) Section 17(a) for engaging in a scheme to defraud in the sale of escrow securities; and (3) Section 206(1), (2) and (3) of the Advisers Act for engaging in conduct that deceived and defrauded an investment advisory client.

The threat of individual SEC litigations, sanctions and censures and IRS revocation of issuer tax-exempt status, along with the federal and state *qui tam* actions, all helped push the Wall Street defendants toward settlement.

In April 1998, CoreStates Financial Corp. became the first investment bank to settle multi-agency yield-burning charges. It paid $3.7 million to settle yield-burning allegations against Meridian Capital Markets, which CoreStates acquired in 1996 acquisition.

The CoreStates settlement established a framework for settling similar yield-burning charges pending against other banks, for it covered potential False Claims Act, security law and IRS liabilities. As part of the settlement, the IRS agreed not to challenge the tax-exempt status of bonds issued by Meridian clients.

VI. RESOLUTION OF THE STATE *QUI TAM* CASE SETS THE STAGE FOR FEDERAL SETTLEMENTS

The California *qui tam* action against Lazard created great momentum in settling the federal case against the Wall Street banks. After vigorous motion practice and intense

discovery by both parties, Lazard settled in September 1998, just a few weeks before trial. Lazard agreed to pay the LAMTA $9 million to settle False Claims Act and other charges relating to one refunding transaction in which the single damages to LAMTA were roughly $3 million.

The settlement of the California *qui tam* action for three times the value of single damages sent a strong message to Wall Street: Yield-burning liability is a serious exposure.

Other settlements followed. In April 1999, Lazard paid $11 million to resolve the federal yield burning charges. Seven months later, BT Alex Brown Inc. agreed to pay $15.3 million to settle its yield burning liabilities.

In April of this year, the majority of the yield burning cases were settled. Seventeen regional and national securities firms agreed to pay a total of $140 million to resolve the charges — bringing the total damages to date to nearly $180 million. The most recent defendants to settle are: Salomon Smith Barney; PaineWebber Inc.; Dain Rauscher Inc.; Warburg Dillon Read LLC; First Union Securities Inc.; Prudential Securities Inc.; Edwards & Sons Inc.; Goldman, Sachs & Co.; Merrill Lynch, Pierce, Fenner & Smith Inc.; Lehman Brothers Inc.; William R. Hough & Co.; Raymond James & Associates Inc., Morgan Stanley Co. Inc.; U.S. Bancorp Piper Jaffray Inc.; Credit Suisse First Boston Corp.; J.C. Bradford & Co.; and Southwest Securities Inc.

VII. THE FALSE CLAIMS ACT'S APPLICATION TO YIELD-BURNING FRAUDS

(1) The Federal Case

Michael Lissack's yield-burning allegations brought the False Claims Act to Wall Street for the first time of which we are aware. In this unusual case, the defendants' securities' pricing fraud set in motion a series of events that resulted in enormous financial loss to the Government. Although the mechanism through which the fraud was accomplished is somewhat complicated, the fraud itself was very simple and not materially different from other, more garden variety frauds in which overcharges were passed on to the federal Treasury through an unwitting third party.

The defendants charged municipal issuers exorbitant prices on the open-market Treasury securities purchased to fund the refinancings. Since the municipalities were not lawfully allowed to earn an arbitrage profit, they had no economic incentive to question the advice given to them by their investment professionals that the bonds were priced at their fair market value. By using higher prices to reduce the yield on the Treasury bonds, rather than lowering the Government's interest obligations to obtain the same reduced yield, the defendants were able to take for themselves money that otherwise would have gone to the Government in the form of lower interest payments.

To obtain their yield-burning price markups, the defendants made and caused to be made a series of false statements designed to assure all concerned, including the issuers and the Federal Government, that the advance refunding bonds were not used for impermissible arbitrage. The net result of their false statements and fraudulent conduct was payment by the Government of claims for interest due on Treasury securities that substantially exceeded the payments the municipalities were lawfully entitled to receive and the Government was obligated to pay. To the extent there were any "arbitrage" profits from municipal bond refinancings, those profits were by law supposed to go to the Treasury in the form of lower interest payments — not to investment banks in the form of illegal mark-ups of the Treasury security prices.

The positive arbitrage profit that was paid to the banks in the form of high-escrow price markups deprived the federal Treasury of lower interest rates. As a result, Wall Street's yield-burning scheme caused two companion harms to the federal Government — both actionable under the False Claims Act. First, a yield-burning escrow causes the federal Treasury to pay more interest than it otherwise would if the escrow complied with federal regulation. Second, a yield-burning escrow also deprives the federal Treasury of recouping that excess interest (yield) through no-interest borrowing via the zero-interest SLGS program.

Accordingly, in the federal case, causes of action under Sections 3729(a)(1), (2), (3) and (7) of the Act alleged that the defendants caused false claims for interest payments to be presented and made and caused to be made false records to get these false claims paid; conspired with other defendants to get false claims for interest paid; and made and caused to be made false records to avoid or decrease an obligation to pay positive arbitrage to the federal Treasury.

(2) LIABILITY UNDER THE CALIFORNIA FALSE CLAIMS ACT

As stated above, the California *qui tam* action against Lazard Freres alleged that LAMTA was caused direct financial harm because of Lazard's undisclosed and excessive markups. That case alleged that Lazard's escrow pricing caused approximately $3 million of negative arbitrage harm directly to the LAMTA, (and an additional approximately $1 million of positive arbitrage to be diverted from the federal Treasury.)

Lazard's California False Claims Act liability was based primarily on the numerous, allegedly false representations to LAMTA concerning the sale of escrow securities at fair market value. In this case, Lazard's alleged misrepresentations were the direct cause of the public agency's financial harm. Unlike the federal case, there were no intervening entities or transactions that occurred between the alleged fraudulent statement and the ultimate financial harm. There was no "pass through" of the fraud, but rather direct claims for payment that harmed a public agency that relied on the representations and advice of its financial advisor. It was alleged under California Government Code

Sections 12651(a)(1) and (2) that Lazard presented false claims for payment to LAMTA for overpriced U.S. Treasury securities, and that it also made false records and statements in support of those false claims.

VIII. REMEDIAL IMPACT OF THE YIELD BURNING LITIGATION

Lissack's False Claims Act litigations substantially helped eradicate yield-burning pricing practices in municipal finance today. By forcing attention to be paid to this nationwide overpricing practice, the action contributed both to the industry-wide shift from noncompetitive to competitive purchases of open-market escrow securities, and to regulatory changes that encourage *bona fide* competitive bid practices.

In this case, the insights from a False Claims Act case not only exposed a fraud scheme, but also dramatically increased federal, state and local awareness of Wall Street's yield-burning practices. As a result, Wall Street has had to change the way it does business with tax-exempt public agencies. Making the sale of open-market securities to public entities a transparent and fair process is a lasting and healthy change for the public finance community. It is one that we believe would not have been made but for the *qui tam* provisions of the False Claims Act.

ENDNOTES

[1] These investigations ultimately resulted in the conviction of Mark Ferber to 33 months in federal prison and a $1 million fine, and the payment of a combined $24 million in fines by Lazard and Merrill Lynch.

[2] The investment banks purchased the Treasury securities in the open market on the issuer's behalf, and then significantly marked up those purchase prices for resale of the Treasuries to the issuer.

[3] Hennigan Mercer & Bennett of Los Angeles joined Phillips & Cohen as co-counsel in the LAMTA litigation.

ALLEGATION: FALSE CERTIFICATION OF TESTING/FAILURE TO MEET DESIGN SPECIFICATIONS

U.S. ex rel. Keehle v. Handy & Harmon et al. (ND NY No. 99-CV-103)

In March 2000, DOJ intervened in a *qui tam* suit alleging that Strandflex, a division of Maryland Specialty Wire, Inc., sold aircraft flight control cable to the Government which did not meet military contract specifications. The cable is used to connect cockpit controls to the engines, landing gear, rudder, and wing surfaces of military aircraft. According to the complaint, Strandflex did not possess the equipment necessary to perform the rigorous quality assurance tests on the cable which are required by military regulations. The lawsuit also alleges that the cable failed to meet design specifications relating to essential aspects such as flexibility and strength. The *qui tam* action was filed in 1999 by Patricia Keehle, a former Quality Assurance Manager for Strandflex. Maryland Specialty Wire, Inc. is a wholly-owned subsidiary of New York-based Handy & Harman, Inc. The relator is represented by Mark Polston (Washington, D.C.) and Dean Gordon of Levitt & Gordon (New Hartford, NY). Assistant U.S. Attorney Charles Roberts is representing the Government.

ALLEGATION: SUBSTANDARD NURSING HOME CARE

U.S. v. NHC Healthcare Corp. (WD MO No. 00-3128-CV-S-BD)

In April 2000, DOJ filed a False Claims Act suit against NHC Healthcare Corp. (d/b/a NHC Healthcare Center of Joplin) and its subsidiary NHC/OP LP, alleging that the nursing home operators billed Medicare and Medicaid for patient services and benefits that were either inadequate or not rendered at all. According to the complaint, the facility received tens of thousands of dollars from Medicaid and Medicare while providing inadequate care to the nursing home residents in violation of applicable statutes, regulations, and contract requirements. The complaint details the companies' alleged failure to remedy health and safety violations which included, among others, failure to treat patients' pressure sores, failure to provide adequate nutrition, and staffing shortages. Assistant U.S. Attorney Andrew Lay is representing the Government.

ALLEGATION: COST ACCOUNTING FRAUD

U.S. ex rel. Kimball v. Mercy Healthcare Sacramento et al. (ED CA No. CIV-S-99-292)

In May 2000, DOJ partially intervened in a *qui tam* suit alleging that four hospitals belonging to Mercy Healthcare of Sacramento and its parent company, Catholic Health West, defrauded the Medicare program in a variety of ways. Among the main allegations are that Mercy Healthcare kept double books and reserve accounts in case overpayments were discovered by auditors. According to the complaint, Mercy received over $2 million in total overpayments from the Medicare intermediary but did not report the overpayments to auditors. Instead, according to the lawsuit, Mercy characterized the overpayments as reserves on cost reports and created reserve accounts to hold the funds. In addition, Mercy allegedly billed Medicare for nonreimbursable hospital costs, listing the costs as reimbursable home health agency (HHA) expenses. Although Medicare does reimburse hospitals for HHA costs, it does so only if the HHA is an inte-

gral and subordinate part of the hospital. Mercy's home health agencies allegedly did not meet these qualifications.

Mercy operated a hospice at a location adjacent to its HHA. The complaint alleges that the staff of Mercy's HHA provided non-allowable services to hospice patients without transferring costs to the hospice. By shifting staff costs, the complaint contends the defendants were able to increase their overall level of reimbursement from Medicare. Additionally, the defendants purportedly claimed the full amount of losses on multiple bond defeasements in a single year, rather than amortizing the losses over the life of the bonds as required by Medicare regulations. The *qui tam* suit was filed in 1999 by former Mercy employee Joseph Kimball. The relator is represented by Paul Scott (San Francisco, CA).

ALLEGATION: FAULTY GEAR BOX SAFETY DEVICES

U.S. ex rel. Swensen v. McDonnell Douglas Helicopter Company d/b/a The Boeing Company (D AZ No. CIV-98-1476-PHX-SMM)

In June 2000, DOJ intervened in a *qui tam* suit against The Boeing Company, formerly known as McDonnell Douglas Helicopter Company, alleging that the company installed faulty gear box safety devices in Apache Attack Helicopters manufactured at its Mesa, Arizona plant. The device, called a "fuzz buster," is designed to attract and burn off small pieces of debris from the oil in the Apaches' engine systems. If the devices detect debris that is too large to be burned off, a cockpit warning light illuminates and Army regulations require pilots to land immediately as a safety precaution. According to the complaint, Boeing's Apache Helicopters did not provide enough electrical power to the fuzz busters, causing false engine failure warnings and numerous unnecessary landings, aborted missions, and unnecessary maintenance. The lawsuit alleges that Boeing knew the device, manufactured by subcontractor TEDECO, was not installed properly and thus Boeing failed to comply with contractual requirements to install and integrate subcontractor parts to the Army's design specifications. The Army Criminal Investigation Command and the DCIS investigated the matter. Eugene Swensen, a former engineer at McDonnell Douglas, filed the *qui tam* suit in 1998. Susan Cannata of Miller, LaSota & Peters (Phoenix, AZ) and Lisa Foster of Phillips & Cohen (San Diego, CA) are representing the relator. Handling the case for the Government is Assistant U.S. Attorney David Duncan.

U.S. ex rel. Lissack v. Salomon Smith Barney et al. (ED NY No. CR-99-566)

In April 2000, the Securities and Exchange Commission announced that seventeen brokerage firms agreed to pay a total of $138.8 million to settle allegations that they had violated the False Claims Act and other laws by engaging in "yield burning." Yield burning refers to the artificial lowering of a security's yield by pricing it in excess of its fair market value. According to the SEC, the accused brokerage houses, acting as municipal-bond underwriters, inflated the price of Treasury securities purchased with proceeds from the sale of municipal bonds. By therefore artificially lowering the yield on the securities, the brokers allegedly diverted money owed to the Federal Government and the municipalities that purchased the securities. The global settlement resolves two separate *qui tam* actions. In 1995, Michael Lissack, a former managing director with Smith Barney (now Salomon Smith Barney) filed a *qui tam* action against sixteen brokerage firms. Two years later, Florida financial advisor Joseph Mooney filed a separate complaint in a *qui tam* action against Salomon Smith Barney which also alleged yield burning.

The settlement assigns roughly $20 million of the proceeds to the municipalities that purchased the bonds and $120 million to the Federal Government. The biggest payer is Salomon Smith Barney contributing $38 million, with the remainder of the settlement being divided among the following firms: PaineWebber; Dain Rauscher; First Union Corp.; Dillon Read; Prudential Securities; A.G. Edwards, Inc.; Goldman, Sachs & Co.; Merrill Lynch & Co.; Lehman Brothers, Inc.; William R. Hough & Co.; Raymond James & Associates; Morgan Stanley Dean Witter & Co.; CS First Boston Corp.; U.S. Bancorp Piper Jaffray, Inc.; J.C. Bradford & Co.; and Southwest Securities. The Government intervened in the *qui tam* actions the day before the settlement was finalized. The relators' share was not disclosed. Erika Kelton of Phillips & Cohen (Washington, D.C.) represented the relators. The Government's case was handled by the SEC, DOJ, Department of the Treasury, and the IRS. *See* Spotlight, page 35.

U.S. ex rel. Norris et al. v. PorterCare Adventist Health et al. (D CO No. 96-M-2383)

In April 2000, PorterCare Adventist Health System agreed to pay $1.5 million to settle a *qui tam* suit alleging that one of its hospitals submitted false respiratory therapy claims to Medicare. From 1994 to 1996, PorterCare Adventist Hospital contracted with Extended Care Services, Inc., d/b/a Hospital Therapy Services of Grand Terrace, California (HTS), to provide respiratory therapy services at skilled nursing facilities in Colorado. The lawsuit alleged that PorterCare and HTS billed for longer periods of respiratory therapy than actually provided and falsified billing records. HTS and its owners, Glen and Judy Conley, agreed in a separate settlement to pay $40,000 to resolve the suit. The *qui tam* action was filed in 1996 by respiratory therapists Gary Norris, Julie Christiansen, Lea Desmond, Shawn McGurran, Kelly Gruber, and Christie Leborne, all formerly employed by PorterCare. The relators' share is 18 percent or $277,200. The matter was investigated by the FBI and HHS OIG. The relators were represented by John Parisi of Shamberg, Johnson & Bergman, Chtd. (Overland Park, KS). The Government was represented by Assistant U.S. Attorney Michael Theis.

Albuquerque Cab Company, Inc.

In April 2000, Albuquerque Cab Company agreed to pay $337,000 to the Federal Government and to the State of New Mexico to settle allegations of improperly claimed Medicaid reimbursement for transportation services. According to DOJ, Albuquerque Cab and its former owners, Abdul Azeez Hindi, Baheej Hindi, and Moneer Hindi, rounded up fractional mileage and improperly used meter fares when billing Medicaid for cab services to and from medical appointments. As a result, Medicaid allegedly was billed for charges exceeding both the actual miles and the Medicaid reimbursement rate. Assistant U.S. Attorney Howard Thomas represented the Government in this matter.

Beebe Medical Center, Inc.

In April 2000, Beebe Medical Center, Inc. of Delaware agreed to pay the Government nearly $1.4 million to settle allegations that it submitted false billings to Medicare over a seven-year period. Under Medicare's Prospective Payment System (PPS), inpatients are assigned a diagnostic-related group (DRG) code that determines the amount of reimbursement a hospital is to receive for each patient's stay. If a patient is sent home, the hospital receives the full DRG reimbursement; however, if a patient is merely transferred to another hospital, the transferring hospital receives only a pro-rated share of the DRG. According to DOJ, Beebe failed to state in its claims to Medicare that certain patients were transferred to another hospital. Rather, Beebe allegedly indicated on claim forms that the patients were sent home or moved to non-hospital facilities. The case resulted from a national initiative among by DOJ and HHS OIG. DOJ announced that this is the first settlement or adjudication of a case of this nature in the country. Assistant U.S. Attorneys Virginia Gibson-Mason and Luis Matos handled the case for the Government.

Johnson City Medical Center

In April 2000, DOJ announced that Johnson City Medical Center agreed to pay $1.28 million to settle allegations that the Center billed Medicare and TennCare, Tennessee's Medicaid program, for upcoded pneumonia claims. The center allegedly claimed to have treated 341 cases of bacterial pneumonia, a rare form of pneumonia which supports a higher reimbursement rate, when in fact the center could only document the validity of 54 of these claims. Upon learning of a 1996 *qui tam* suit filed by Health Outcomes Technologies against more than 100 hospitals for similar pneumonia upcoding claims, the medical center voluntarily disclosed its pneumonia upcoding to the Government. Johnson City Medical Center was not named in the suit. This matter was investigated by the FBI and HHS OIG. The Government was represented in this case by Assistant U.S. Attorney Cynthia Freemon Davidson.

U.S. v. Fromer (ED NY No. CR99-566)

In April 2000, DOJ announced that Dr. Carl Fromer agreed to pay $8.5 million in exchange for the release of civil claims, including False Claims Act liability, arising from allegations that Fromer billed Medicare for medically unnecessary, contraindicated, and unperformed ophthalmological services. The settlement agreement, which is part of a global settlement covering both civil and criminal liability, also provides that Fromer will enter a guilty plea in response to a federal criminal indictment based on the alleged Medicare fraud and related conduct. According to DOJ, Fromer's own medical charts did not justify the wide scope of services for which he submitted bills. DOJ further alleged that Fromer created and submitted new documentation, sometimes years

after the questioned dates of service, to justify his claims after Medicare requested supporting documentation. Fromer has been permanently excluded from all federally funded health care programs. HHS OIG investigated the matter. The Government was represented by Assistant U.S. Attorneys Ilene Jaroslaw, Richard Molot, and Richard Faughnan.

Louisiana State University

In April 2000, DOJ announced that Louisiana State University's Board of Supervisors agreed to pay nearly $1.5 million to settle allegations that the University's Health Sciences Center (LSU-HSC) submitted false claims to Medicare and Medicaid for anesthesia services. According to DOJ, LSU-HSC billed for the anesthesia services of Dr. Jonathon Skerman, who held three degrees in dentistry but was not licensed in Louisiana as a physician, nurse-anesthetist, or nurse. LSU-HSC also admitted to billing the Government for services provided by Skerman when in fact he was not present. The matter was investigated by HHS OIG. The matter was handled for the Government by Assistant U.S. Attorney Scott Newton.

U.S. ex rel. Abbott-Burdick et al. v. University Medical Associates et al. (D SC No. 3:96-1676-10)

In April 2000, the Medical University of South Carolina (MUSC) and its physicians' group, University Medical Associates (UMA), agreed to pay $5.2 million to settle a *qui tam* action alleging that the providers submitted claims to federally funded health care programs for services not provided by the named physicians. According to the lawsuit, MUSC and UMA submitted claims to Medicare, Medicaid, and CHAMPUS under qualified doctors' names for medical services that were provided while the named doctors were absent. The suit also alleged that MUSC and UMA billed for attending physicians' services which were actually provided by unqualified employees. The *qui tam* action was filed in 1996 by Terri Abbott-Burdick, Cinda Gridley, Richard Koonz, and James Salvo, all former employees of the defendants. The relators' share was 23 percent or nearly $1.2 million. The relators were represented by John Moylan and Carl Muller of Wyche, Burgess, Freeman & Parham (Greenville, SC). The suit was handled for the Government by Assistant U.S. Attorneys Deborah Barbier and Jennifer Aldrich.

North American Pipe Corporation

In April 2000, the North American Pipe Corporation (NAPCO), a subsidiary of Westlake Chemical Company, agreed to pay the Government $500,000 to settle a *qui tam* suit alleging that the company sold untested polyvinyl chloride pipe to DOD and the Federal Bureau of Prisons. The Government alleged that the pipes sold did not meet the requirements of applicable industry standards or government contract specifications. Stan Price, an independent salesman who formerly sold pipe manufactured by the company, filed the *qui tam* suit in 1996. Pursuant to the settlement, NAPCO also agreed to provide a 30-year warranty to recipients of grants and loans from the USDA and HUD who used the federal funds to purchase NAPCO pipe. NAPCO is a Delaware corporaton with its headquarters in Houston, Texas. The case was investigated by the DCIS, DOJ OIG, and the Department of Agriculture OIG. The relator will receive $100,000 as his share of the settlement. The relator was represented by Albon Head, Jr. of Jackson & Walker, LLP (Fort Worth, Texas) and Robert Vogel of Washington, D.C. Assistant U.S. Attorney Michelle Zingaro represented the Government.

Newark Cardiovascular and Thoracic Surgery Group

In April 2000, DOJ announced that the Newark Cardiovascular and Thoracic Surgery Group agreed to pay $500,000 to settle allegations that it submitted false claims to Medicare for services that were not provided. The medical practice specializes in complex heart bypass and transplant surgeries. According to DOJ, the surgery group routinely submitted claims to Medicare seeking reimbursement for both a primary surgeon and an assistant at surgery for heart bypass and other surgeries performed at Newark Beth Israel Hospital. DOJ alleged that these claims were submitted regardless of whether a second physician provided services or was even present for the operation. Medicare regulations require the active participation of the surgical assistant in order to bill for his or her services. The FBI investigated the matter.

Community Health Systems

In May 2000, DOJ announced that Community Health Systems (CHS), a Brentwood, Tennessee-based hospital chain, agreed to pay $31 million to settle allegations that it submitted false claims to Medicare, Medicaid and TRICARE. DOJ alleged that CHS systematically upcoded with regard to eight diagnoses, including pneumonia, septicemia, and certain cardiac conditions. In this instance, upcoding is the improper assignment of inpatient diagnosis codes in order to increase reimbursement. According to DOJ, after being notified of the investigation into the diagnostic coding practices of several of its hospitals, CHS disclosed chain-wide upcoding to the Government. CHS owns or operates 46 hospitals in 20 states. The settlement expressly excludes from its scope a *qui tam* action against CHS which is currently pending in Tennessee (U.S. ex rel. Smith v. Community Health Systems, Inc., Civil Action No. 3-99-0869). Illinois, New Mexico, South Carolina, Tennessee, Texas, and West Virginia will receive portions of the settlement as compensation for losses to the states' Medicaid programs. The Government was represented by Jamie Ann Yavelberg and Tracy Hilmer of the DOJ Civil Division.

U.S. ex rel. Schrage v. Bethphage et al. (D NE No. 8:98cv555)

In May 2000, Bethphage, a Nebraska-based non-profit affiliate of the Evangelical Lutheran Church of America, agreed to pay the Federal Government and the state Medicaid agencies in Nebraska, Iowa, and Indiana $296,000 to settle a *qui tam* action alleging that it had submitted improper claims to Medicaid for administrative costs. According to the lawsuit, Bethphage submitted employee health care charges and travel costs without appropriate documentation and requested excessive reimbursement for workers' compensation costs. The allegations did not involve the support services Bethphage provides to clients with developmental disabilities. DOJ intervened in three of the seven claims included in the *qui tam* complaint filed by former Bethphage employee Larry Schrage in 1998. These three claims were resolved by the settlement, with the remaining claims voluntarily dismissed by the relator. The relator's share was 18 percent or $55,480. Assistant U.S. Attorney Laurie Kelly represented the Government.

Cabaco, Inc.

In May 2000, DOJ announced that Cabaco, Inc. agreed to pay $180,000 to settle allegations that it billed the Navy for painting services which did not meet contract specifications. From 1994 to 1998, the Navy contracted with Cabaco to provide maintenance and repair services at its Murphy Canyon Heights family housing com-

plex in San Diego. DOJ alleged that Cabaco failed to fully prime wall surfaces before painting them, in violation of contract specifications requiring such priming, and billed the Government for its work while knowing of this violation. Assistant U.S. Attorney Stephen Segreto handled this matter for the Government.

Lockheed Martin Corporation

In May 2000, Lockheed Martin Corporation reportedly agreed to pay $5 million to settle claims that two of its subsidiaries overcharged the Navy for components used in anti-submarine warfare aircraft. Lockheed Aeronautical Systems and Lockheed Sanders allegedly failed to disclose accurate and complete pricing data, in violation of the Truth In Negotiations Act, during contract negotiations for the manufacture of S-3B Viking anti-submarine aircraft. According to the Government, Lockheed's production costs were lower than the contract prices, causing the United States to overpay Lockheed by at least $1.8 million. The settlement resolved a longstanding investigation into this matter by the Naval Criminal Investigative Service and the DCAA. Assistant U.S. Attorney Patrick Walsh represented the Government.

U.S. ex rel. Kohler et al. v. Galichia et al. (D KS No. 97-1029-JTM)

In May 2000, Joseph Galichia, M.D., and Galichia Medical Group, P.A., agreed by consent judgment to pay the Government $1.525 millon to settle allegations that the medical group submitted false bills to Medicare. The settlement also resolves a *qui tam* lawsuit filed in 1997 by relators Beth Kohler, Susan Bright, and Thomas Scholler, all former employees of the heart disease specialty practice. According to DOJ, between 1993 and 1998 Galichia upcoded Medicare claims, double billed, and billed for unnecessary tests and procedures. The relators' share is 18 percent or $27,450. Representing the relators was Chistopher Christian of Hutton & Hutton (Wichita, KS). The Government was represented by Laurie Oberembt of the DOJ Civil Division and Assistant U.S. Attorney Richard Schodorf.

U.S. ex rel. Wu v. Thomas Jefferson University et al. (ED PA No. 97-3396)

In May 2000, Thomas Jefferson University agreed to pay $2.6 million to settle False Claims Act allegations that it and a number of its employees had engaged in fraud with regard to two federal research grants. The global settlement executed by the university also resolved a *qui tam* suit filed in 1997 by Dr. Yong Wu, a former post-doctoral research fellow at the university. Wu's lawsuit alleged that researchers at the university used fabricated research data to support the university's application for and continued funding of gene therapy research into the inhibition of the HIV virus. The AIDS gene therapy research grant was awarded to the university by the National Institute of Allergy and Infectious Diseases of the National Institute of Health (NIH). The settlement also resolved allegations regarding a grant for cancer research awarded to the University by NIH and the National Cancer Institute. According to DOJ, the expressly designated principal researcher ceased work on the project and moved to Italy during the grant term, but the defendants represented to NIH that he was present and performing research pursuant to the grant. DOJ further alleged that the university improperly charged to the grant the salaries for post-doctoral fellows who in fact had nothing to do with the research. The HHS Office of Research Integrity, NIH Office of Extramural Research, and the FBI jointly

conducted the investigation. The relator's share and attorney's fees amounted to $90,000. The relator was represented by James Ratner (New York, NY). The matter was handled for the Government by Assistant U.S. Attorney David Hoffman.

Capital Health System

In June 2000, DOJ announced that Capital Health System, Mercer Campus, formerly known as the Mercer Medical Center, agreed to pay $450,000 to settle claims that it submitted false bills to Medicare for inpatient hospital stays. DOJ alleged that the medical center submitted claims for inpatient hospital stays for patients who received outpatient services. This resulted in higher reimbursement than if the medical center had properly billed for the outpatient services provided. This matter was investigated by HHS OIG. The Government was represented by Assistant U.S. Attorney Michael Chagares.

Humana Inc.

In June 2000, managed care provider Humana, Inc. agreed to pay the Government $14.5 million to resolve allegations that the company falsely described patient eligibility on claims submitted to Medicare. From 1990 to 1999, Humana allegedly classified patients as dually eligible for Medicare and Medicaid, allowing the company to collect higher capitation fees, while it knew that the patients were not dually eligible. Medicare pays up to two times more in premiums to HMOs that cover patients eligible for both programs. Half of the settlement is related to allegations that Humana defrauded Medicare and half is related to simple overpayment. The settlement follows an investigation by the HHS OIG. Assistant U.S. Attorney Barbara Bisno represented the Government.

U.S. ex rel. Johnson et al. v. Shell Oil Company et al. (ED TX No. 9:96CV66)

In April 2000, DOJ announced that BP Amoco agreed to pay $32 million to settle a *qui tam* suit alleging that the corporation had underpaid royalties due for oil produced on federal and Indian lands. The suit, alleging that 14 oil companies engaged in systematic underreporting for millions of barrels of oil, was filed in 1996 by J. Benjamin Johnson and John Martinek, former employees of Atlantic Richfield Co. According to DOJ, BP Amoco was required to submit reports reflecting the amount and value of oil the company produced pursuant to leases administered by the Department of the Interior. Instead, the company allegedly submitted reports for a ten-year period that undervalued the oil and, as such, paid fewer royalties than owed. The relators' share was more than $5.4 million.

In June 2000, DOJ announced that Devon Energy Production Company (formerly Pennzoil) and Sunoco, Inc. agreed to pay the Government $11.9 million and $200,000 respectively to resolve similar claims. DOJ alleged that for ten years Pennzoil and Sunoco also underpaid royalties due for oil produced on Federal and Indian leases. DOJ has previously reached settlement agreements with several other defendant oil companies in this action, including a $95 million settlement with Chevron Corporation, a $26 million settlement with Conoco, Inc., and a $7.3 million settlement with Oxy USA. Michael Havard and Reuben Guttman of Provost & Umphrey Law Firm (Beaumont, TX) represented the relators. Representing the Government was U.S. Attorney Mike Bradford.

FCA Conference Materials

- As part of its information clearinghouse activities, TAF has materials available for distribution at conferences and other programs. Information can be tailored to a legal or general audience. Resource material, including statistical information, is also available for those writing articles on the FCA.

Qui Tam Practitioner Guide

- The *TAF Qui Tam Practitioner Guide: Evaluating and Filing a Case* can be ordered at no charge by phone, fax, or mail. This "how to" manual includes sections on evaluating the merits and viability of a case, pre-filing and practical considerations, and preparing and filing the complaint.

TAF on the Internet

- TAF's Internet presence, designed to educate the public and legal community about the False Claims Act and *qui tam*, has expanded to highlight the growing health care trend and recent legislative developments. TAF's site is located at http://www.taf.org.

Previous Publications

- Back issues of the *Quarterly Review* are available in hard copy as well as on TAF's Internet site.

Quarterly Review Submissions

- TAF seeks submissions for future issues of the *Quarterly Review* (e.g., opinion pieces, legal analysis, practice tips). We thank our outside contributors for their articles in this issue. To discuss a potential article, please contact Staff Attorney Amy Wilken.

Anniversary Reports and Video

- To mark the anniversary of the 1986 FCA Amendments, TAF has available a variety of resources including a Tenth Anniversary Report, an Assessment of Economic Impact, and an educational video highlighting the effectiveness of the Act. These materials are available at no charge.

Call for Experts and Investigators

- In response to inquiries, TAF is working to compile a list of experts and investigators across an array of substantive areas. Please contact TAF with any suggestions you may have.

Qui Tam Attorney Network

- TAF is continuing to build and facilitate an information network for *qui tam* attorneys. For an Attorney Network Application or a description of activities, please contact TAF. Be sure to ask about TAFNET, our electronic mail system for Attorney Network members.

TAF Library

- TAF's FCA library is open to the public, by appointment, during regular business hours. Submissions of case materials such as complaints, disclosure statements, briefs, and settlement agreements are appreciated.

Acknowledgments

- TAF thanks the Department of Justice and *qui tam* counsel for providing source materials.