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Legal Materiality and the Implied Certification Theory of the False Claims Act: Why Courts Have Rejected the Traditional Standards of Materiality in Favor of a Precondition to Payment Requirement

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I. Introduction

Imagine a scenario where a primary care physician submits a claim for payment under Medicare either for services rendered or medical supplies ordered on behalf of a patient. The doctor, as a necessary procedural aspect of submitting the claim, must certify compliance with the vast array of applicable Medicare regulations. Now consider that the doctor falsely certified compliance with one of the multitude of regulations governing Medicare. Assuming that the doctor did so knowingly (which is a requirement under the statute), did the doctor submit a false claim to the government so as to make him liable under the False Claims Act (FCA)? In other words, what exactly must be true in a typical claim for payment made to the government? Does it encompass only *factual* truths, i.e., is the claim false only when there is a factual inconsistency such as overcharging or billing for services that were not provided? Or does it extend to *legal* compliance with statutes and regulations that govern the claim for payment as well? If the truth of the claim extends to legal compliance with statutes and regulations, then exactly which statutes and regulations does one need to comply with? Is compliance with *all* applicable statutes and regulations that govern the claim for payment a requirement, or merely those statutes and regulations that explicitly condition payment of the claim upon compliance with their terms? And lastly, how does one determine whether a particular statute is a *precondition to payment* of the claim as opposed to a *condition of participation* in the Medicare program?

These are the types of questions a court must answer when confronted with a FCA action predicated on the implied certification theory. In a nutshell, this theory basically involves the question of whether and how far in submitting a claim for payment one

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implies certification with certain statutes and regulations. The answer to this question, which is the subject of this Article, may have huge consequences not only for the healthcare sector, but for all government contractors and payees under government programs. This is so because when an individual or entity does business with the government, it is a far different affair than one solely between two private individuals or entities. “Whereas between private parties even an express lie about performance will often go unpunished, the mere request for payment by a noncompliant government contractor can result in significant legal liability.”\(^2\) The individual dealing with the government must traverse an Odyssean myriad of statutes and regulations that govern the financial relationship between the individual and the government, thus turning any violation of a statute or regulation into a potential false claim. To make matters worse, fraud allegations of this sort are becoming more and more common lately, thanks in large part to the proliferation of qui tam suits brought by plaintiffs (known as relators) in the name of the government. As such, it is important that there be certainty in this area of the law so that government contractors and payees are made aware of the extent of liability they may incur for statutory and regulatory violations.

This Article provides an answer to the question of the scope of liability under the implied certification theory by exploring the issue of materiality, a required component of any FCA action.\(^3\) In particular, it inquires as to why most courts have rejected the traditional “outcome determinative” and “natural tendency” standards of materiality under the FCA in favor of a precondition to payment requirement when dealing with cases predicated on the implied certification theory. It then argues why the precondition

\(^2\) Michael Holt & Gregory Klass, Implied Certification Under the False Claims Act, 41 PUB. CONT. L.J. 1, 2 (2011).

to payment requirement is the best method for determining materiality under implied certification cases and then proposes a simple method courts can utilize under this standard to determine materiality much more accurately and efficiently. Part II will begin by providing a brief history and background of the False Claims Act. Part III will look at the origin of the implied certification theory and its history of interpretation in the federal courts and will also explore the concept of materiality under the FCA and how it has evolved into two different standards, one broadening liability (“natural tendency”) and the other narrowing it (“outcome determinative”). Part IV discusses the concept of materiality in the context of the implied certification theory and why the nature and scope of liability under this theory requires a new and distinct standard of materiality, one that focuses on the legal falsity of the claim rather than the actions of an obscure government agent, which is what the other two standards of materiality are based on.

II. Background to the False Claims Act

The origin of the False Claims Act dates back to the Civil War. It was passed in 1863 to combat the rampant fraud and abuse perpetrated by individuals and companies dealing with the Government, in particular the “fraud and corruption in the sale of supplies and provisions to the Union army during the Civil War.” The FCA, therefore, became “the exclusive remedy [provided by Congress] for recovering damages from all attempts to cause the government to pay out money as a result of false or fraudulent claims.” As the government’s “primary litigative tool for combating fraud,” the Act

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4 Holt, supra note 2, at 5.
6 Id. at 184.
contains both civil and criminal penalties.\(^8\) This Article is concerned with the civil aspect of the FCA, which is the provision under which the implied certification theory arises.

Under the civil penalties provision, codified at 31 U.S.C. § 3729, a person can be held liable for an FCA violation if he presents (1) a claim or statement (2) that is false or fraudulent (3) to the United States Government (4) that is knowingly made and that (5) seeks payment from the federal treasury.\(^9\) A “claim” under the FCA is a request for money or property from the Government.\(^10\) The second element, what makes a claim false or fraudulent, is the subject of this Article. There are three different ways a claim can be false or fraudulent for purposes of the FCA. A \textit{factually false} claim is one that “incorrectly describes the goods or services provided or a request for goods or services never provided.”\(^11\) A \textit{legally false} claim can be either \textit{express} or \textit{implied}, depending on what type of certification is made on the claim form. An \textit{express} certification is where a claim contains an express statement that “falsely certifies compliance with a particular statute, regulation or contractual term, \textit{where compliance is a prerequisite to payment}.”\(^12\) On the other hand, an \textit{implied} certification is where “the act of submitting a claim for reimbursement itself implies compliance with the governing federal rules \textit{that are a precondition to payment}.”\(^13\) The difference in an implied certification case, then, is the absence of any express statement of compliance.


A claim “to the United States government” can be “made directly to the government, or it might be made to a third party that is supplying money or property on the government's behalf.”\textsuperscript{14} The claim must also be made “knowingly,” which is defined in the statute as “actual knowledge of the information,” “deliberate ignorance of the truth or falsity of the information,” or “reckless disregard of the truth or falsity of the information”;\textsuperscript{15} no proof of specific intent to defraud is required.\textsuperscript{16} An individual who submits a false claim under the FCA is liable to the government “for a civil penalty of not less than $5,000 and not more than $10,000…plus 3 times the amount of damages which the Government sustains because of the act of that person.”\textsuperscript{17}

The Act also allows for private enforcement “through \textit{qui tam} actions, in which a private party, or ‘relator,’ brings suit on behalf of the Government.”\textsuperscript{18} To bring an action, the \textit{qui tam} relator must have “direct and independent knowledge of the information on which the allegations are based, and have voluntarily provided such information to the Government before filing an action.”\textsuperscript{19} Suits based on public information are barred.\textsuperscript{20} In bringing suit, the \textit{qui tam} relator receives a bounty of between twenty-five and thirty-five percent of the amount recovered if the government chooses not to intervene and between fifteen and twenty-five percent if the government elects to intervene in the action.\textsuperscript{21} As a result of the substantial increase in suits brought by \textit{qui tam} relators in recent years,\textsuperscript{22}

\footnotesize
\begin{enumerate}
\item Holt, \textit{supra} note 2, at 6.
\item \textit{United States v. Science Applications Intern. Corp.}, 626 F.3d 1257, 1274 (D.C. Cir. 2010).
\item Holt, \textit{supra} note 2, at 9.
\item \textit{Id.}
\item \textit{Id.}
\item \textit{Id.} at 9-10.
\end{enumerate}
courts have more stringently applied the requirements under the Act, such as requiring higher scienter and reading a separate requirement of materiality into the statute. This in turn has “influenced judicial interpretation of the Act’s substantive provisions,” most notably those on the issue of implied certification, since many qui tam actions are predicated on a defendant’s implied certification with a statute or regulation that was alleged to have been violated. These judicial interpretations of the implied certification theory and their effect on FCA litigation will be examined in the next section.

III. A Framework of Two Judicially Constructed Doctrines

As will be seen further, in its original form as passed in 1863, the False Claims Act did not address the issue of implied certification, i.e., allegations of falsity based on noncompliance with underlying statutes or regulations; neither did it contain an express requirement of materiality. Both of these doctrines were later incorporated into the statute throughout its history of interpretation and application by federal courts. This evolution of the FCA came about, in essence, as a response to a wide array of societal and policy goals that attempted either to expand (implied certification) or limit (materiality) the reach of the statute. This Part deals with both judicially-constructed doctrines by exploring their history in FCA jurisprudence and will thus act as a primer to Part IV, which discusses the intersection between the two doctrines of implied certification and the concept of materiality. It will then explain why the precondition to payment materiality standard is better suited to the contours of the implied certification theory.

24 Holt, supra note 2, at 10.
25 Hoffman, supra note 5, at 181.
26 Hoffman, supra note 5, at 181.
A. The Law of Implied Certification: A Brief History

From its inception, the False Claims Act contemplated only “factually false” claims, i.e., claims for goods or services that were never provided or where the government had been overcharged for such goods or services. This made sense because Congress, at the time the Act was passed (Civil War), was concerned with “reports of crates labeled ‘muskets’ sold to the Government that were in fact filled with sawdust and individual horses or mules [being] sold to the Government several times over.” It was not until 1976 that courts began to recognize FCA causes of action based on allegations of non-compliance with applicable statutes and regulations, or “legally false claims.” Courts of this era, however, did not speak in terms of express and implied certification. Rather, courts held that a claim was false or fraudulent if the defendant made a “false certification” of compliance with a statute or regulation that caused the government to pay out money to which the defendant was not entitled. During this period, however, all actions brought pursuant to this “false certification” theory involved an express certification of compliance, i.e., where a defendant expressly certifies compliance, either in a government contract or in a claim form, with certain statutes or regulations.

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29 Holt, supra note 2, at 16.
32 United States v. Hibbs, 420 F.Supp. 1365, 1368 (E.D. Penn., 1976), vacated, 568 F.2d 347 (1977) (“The government has met its burden of establishing that the false certifications caused to be submitted by the defendant, Hibbs, resulted in the filing of a false claim by the mortgagee against the United States”).
33 See Joseph R. Berger, Recent Rulings on Implied Certification Under the False Claims Act: Limitations on a Common-Law Theory, 16 No. 5 WESTLAW JOURNAL HEALTH CARE FRAUD, 10 (2010) (a federal court first took up the issue of implied certification in 1994).
The issue of whether a defendant, by submitting a claim for payment, could be held liable for implying certification with a statute or regulation was not addressed until 1994 in the seminal case *Ab-Tech Constr., Inc. v. United States*. There, the plaintiff construction company brought an action to collect money it alleged was due under its contract with the government. The government filed a counterclaim, alleging that the company failed to comply with certain conditions under the Small Business Act, thereby causing it to submit false claims in violation of the FCA. The court held that although the plaintiff had never expressly certified compliance with the SBA’s program requirements in its claims for payment, nevertheless “[t]he payment vouchers represented an implied certification by Ab-Tech of its continuing adherence to the requirements for participation in the [SBA] program.” This argument was predicated on the fact that the plaintiff had signed a “‘Statement of Cooperation’ [upon entering into its contract with the government] acknowledging [its] understanding of, and…compliance with, the program's requirements for continuing eligibility.”

While courts and commentators have been quick to acknowledge *Ab-Tech* as the avant garde in the new emerging doctrine of implied certification, few have properly distinguished it from later cases involving a different type of implied certification. In their article on implied certification, which is the earliest of its kind known to this author, Susan Levy and Daniel Winters laid out two scenarios under which a claim could be false under a theory of implied certification. The first, an implied certification of continued
compliance with a prior express certification, was of the type involved in Ab-Tech.\textsuperscript{40} This type of implied certification is common in the health care context where relators bring suits alleging that a provider had previously certified compliance with an underlying statute or regulation governing payment under Medicare and that the provider had violated the statute or regulation, thus making any claims submitted after that alleged violation false under the FCA.\textsuperscript{41} These statutes or regulations can be either conditions of participation or conditions of payment; the difference between the two will be discussed later in this Article. In cases of the first type, it is relatively easy for courts to assign liability because the defendant expressly certified compliance with a statute or regulation, either in a cost report\textsuperscript{42} or in a provider application.\textsuperscript{43} According to Levy and Winters:

This first application of the implied certification theory appears noncontroversial in that it works to hold a defendant liable for express certifications it actually made in order to be eligible to receive federal funds. The law simply implies that the defendant repeats those certifications each time it submits an invoice for payment as a participant in that federal program. In these types of circumstances, it is fair for the Government to assume that once a party expressly certifies compliance with certain funding prerequisites (e.g., that it will not pay recruiters, will remain a minority-owned business, or will comply with Medicare cost report regulations), it will continue to comply with those requirements.\textsuperscript{44}

The second type of implied certification does not involve a prior express certification at all; instead, it relies on the submission of a claim for payment as impliedly representing compliance with all statutes and regulations governing the program under

\textsuperscript{40} Id. at 136; Ab-Tech Constr., Inc. v. United States, 31 Fed.Cl. 429, 434 (Fed. Cl. 1994) (“The payment vouchers represented an implied certification by Ab-Tech of its continuing adherence to the requirements for participation in the 8(a) program”).

\textsuperscript{41} United States ex rel. Augustine v. Century Health Services, Inc., 289 F.3d 409, 415 (6th Cir. 2002); United States ex rel. Wilkins v. United Health Group, Inc., 659 F.3d 295, 312 (3rd Cir. 2011); United States ex rel. Hendow v. University of Phoenix 461 F.3d 1166, 1176 (9th Cir. 2006).

\textsuperscript{42} United States ex rel. Augustine v. Century Health Services, Inc., 289 F.3d 409, 414 (6th Cir. 2002).


\textsuperscript{44} Levy, supra note 31, at 138.
which payment is sought.\(^{45}\) For example, a physician who submits a claim for payment to Medicare, although he does not \textit{expressly} certify compliance with the Medicare statutes and regulations, nevertheless this certification of compliance can be \textit{implied} by mere submission of the claim. The rationale used to justify this type of implied certification is that in submitting a claim for payment, the defendant has impliedly certified compliance with those statutes and regulations governing the government program under which the defendant seeks payment. Many of the cases relying on this type of implied certification are brought against health care providers “where relators rely on some alleged violation of one of the vast number of complex [Medicare] rules and regulations…as the basis for an FCA claim.”\(^{46}\) In \textit{United States ex rel. Barrett v. Columbia/HCA Healthcare Corp.} (2003), the court held that although the defendant health care corporation was not required under the Medicare statute to file annual cost reports or other documents expressly certifying compliance with Medicare regulations, this did not preclude a finding of liability under the FCA.\(^{47}\) In coming to this conclusion, the court relied heavily on a materiality analysis, holding that “where the government pays funds to a party, and would not have paid those funds had it known of a violation of a law or regulation, the claim submitted for those funds contain[s] an implied certification of compliance with the law or regulation and [is] fraudulent.”\(^{48}\)

The second type of implied certification has received criticism from numerous arenas of legal academia\(^ {49}\) partly because of the fear of “relators who [seek]…to expand

\(^{45}\) \textit{Id.} at 139.
\(^{46}\) \textit{Id.}
\(^{47}\) \textit{Id.}
\(^{49}\) Levy, \textit{supra} note 31, at 142-43 (“Mikes and other cases as well] serve[] as a warning to relators-especially in the Medicare context where FCA actions are often brought given the large number of
the scope of the FCA to pursue their own recovery.”

But much of the criticism of this form of implied certification is, at the very least, unwarranted. As will be seen, this type of implied certification, as with the former type and with express certification as well, all require a showing of materiality before liability can attach.

**B. Materiality Under the False Claims Act**

One of the most vague concepts in criminal and civil jurisprudence to date has been the concept of materiality. This is so because its definition has always depended upon the context in which it is used. Black’s Law Dictionary defines it as “having some logical connection with the consequential facts” or “of such a nature that knowledge of the item would affect a person’s decision-making.” Unfortunately, in the context of the False Claims Act, the definition of materiality has been just as fleeting. While it is currently defined by statute, federal courts have constantly adjusted its meaning to suit particular instances of fraudulent conduct and to achieve social and policy goals. This section will deal with the history of materiality under the FCA and how it has evolved into two distinct definitions, one expanding liability and the other narrowing it. It will then look at how the emergence of legal certification cases have altered the analysis of what constitutes material falsity and how this change has led to the formulation of a new materiality standard that focuses on the legal sufficiency of a claim.

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50 Berger, supra note 33, at 1.

51 TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 439 (1976) (in context of Rule 14a-9 of Securities and Exchange Act: “a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote.”); Fedorenko v. United States, 449 U.S. 490, 509 (1981) (“if disclosure of the true facts would have made the applicant ineligible for a visa”); United States v. Bagley, 473 U.S. 667, 682 (1985) (“a reasonable probability that, had the evidence been disclosed to the defense, the result of the proceeding would have been different”).


1. “Outcome Determinative” Standard

As it was passed in 1863 and until 2009, the False Claims Act did not explicitly contain an element of materiality.\(^\text{54}\) Courts, however, had implicitly read a requirement of materiality into the Act beginning with *Cahill v. Curtiss-Wright Corp.* (1944).\(^\text{55}\) Speaking in the context of a qui tam suit alleging damages in an amount in excess of $10 million for numerous violations of the false claims statute, the court held that “[f]raud consists in the false representation of a material fact, made with knowledge of its falsity and with the intent to deceive the other party, which representation must be believed and acted upon by the party deceived to his damage.”\(^\text{56}\) This standard of materiality would require the government to prove that it had actually acted or relied\(^\text{57}\) upon the false information submitted. Put another way, it requires the government to prove causation as an element of materiality.\(^\text{58}\) To date, however, the Eight Circuit Court of Appeals is the only federal circuit that has explicitly applied the “outcome determinative” test in an FCA case.\(^\text{59}\)

2. “Natural Tendency” or “Capable of Influencing” Standard

The early “outcome determinative” standard did not evolve much beyond its strictures until the 1986 amendments to the FCA that “transferred [enforcement] from

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\(^\text{56}\) *Id.* at 616.

\(^\text{57}\) *See United States v. Hibbs*, 568 F.2d 347, 352 (“the parties agree that the applicable rule of law for computing the damage figure is the difference between the amount the government actually paid in reliance on the false claims and the amount it would have paid had there been fair, open and competitive bidding.” (quoting *Brown v. United States*, 524 F.2d 693, 706 (CtCl. 1975))).

\(^\text{58}\) *Id.* at 351 (“The statutory limitation, ‘by reason of’ the commission of the unlawful act, compels consideration of the element of causation. That requirement should be liberally construed so as to provide the government restitution from those whose fraud has caused loss. It should not, however, be disregarded completely so as to eliminate the relationship between the unlawful act and the injury ultimately sustained”).

\(^\text{59}\) *United States ex rel. Costner v. United States*, 317 F.3d 883, 887 (8th Cir. 2003).
virtually exclusive control of the [Department of Justice] to a shared enforcement with private attorneys representing qui tam relators." The DOJ, responding to this shift in enforcement, initially held that materiality was not a requirement under the FCA, but changed gears soon after the decision in Mikes v. Straus in 2001. At that point the DOJ realized that because most federal circuits had begun to require at least some showing of materiality, "[b]y continuing to argue that materiality was not a required element of the FCA, the DOJ was losing the ability to define what was required under the FCA." As a result, in 2004 the DOJ took the position that "[t]he proper standard for determining whether the alleged false statements in the instant case were material is whether they had the potential or natural tendency to affect the Government's payment decision." This less stringent standard of materiality merely requires "the [c]ourt to examine the grant provisions with which the relator contends that the defendant misrepresented its compliance, to determine whether any of these provisions was a condition of payment... If the defendant's false statements are determined to be related to a condition of payment-and the Government takes no position on this issue-those statements had a natural tendency to affect the Government's payment decision and were therefore material."

To be sure, DOJ lawyers were not the first to propose that the "natural tendency" standard of materiality be used in the context of FCA cases. In fact, one of the earliest cases to articulate this standard, albeit in the background of a criminal false statement

\[\text{Boese, supra note 28, at 297.}\]
\[\text{Id. at 298.}\]
\[\text{Id. at 299.}\]
\[\text{Id.}\]
\[\text{Id.}\]
\[\text{Id.}\]
\[\text{Id. at 300.}\]
\[\text{Id.}\]
statute (18 U.S.C. § 1001), was *Weinstock v. United States* (1956).\(^{67}\) There, the D.C. Circuit held that “[t]he meaning of the word [materiality] appears to be consistent in the[...] various fields [of]...insurance law, bankruptcy, agency, motions for new trial upon the ground of newly discovered evidence, and in respect to perjury [as] whether the false statement has a natural tendency to influence, or was capable of influencing, the decision of the tribunal in making a determination required to be made.”\(^{68}\) More than thirty years later, the Supreme Court in *Kungys v. United States* (1988), citing *Weinstock*, affirmed the “natural tendency” standard in the context of a statute revoking citizenship for false statements.\(^{69}\) Justice Scalia, writing for the majority, noted that “[t]he federal courts have long displayed a quite uniform understanding of the “materiality” concept as embodied in such [willful concealment] statutes.”\(^{70}\) The court further declared that “[w]hile we have before us here a statute revoking citizenship rather than imposing criminal fine or imprisonment [as with willful concealment], neither the evident objective sought to be achieved by the materiality requirement, nor the gravity of the consequences that follow from its being met, is so different as to justify adoption of a different standard.”\(^{71}\)

In 1997, the Supreme Court in *United States v. Wells* (1997) again considered the issue of the proper definition of materiality, this time with respect to false statements made to a federally insured financial institution under 18 U.S.C. § 1014.\(^{72}\) There, Justice Souter opined on behalf of the court that while Congress did not intend for materiality to be an element of § 1014,\(^{73}\) nevertheless “[w]e...understand[] the term in question to mean

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\(^{67}\) *Weinstock v. United States*, 231 F.2d 699 (D.C. Cir. 1956).

\(^{68}\) Id. at 701.


\(^{70}\) Id. at 770.

\(^{71}\) Id.

\(^{72}\) *United States v. Wells*, 519 U.S. 482 (1997).

\(^{73}\) Id. at 483.
having a natural tendency to influence, or being capable of influencing, the decision of
the decisionmaking body to which it was addressed.”

Two years later in *Neder v. United States* (1999), the Supreme Court again ruled that in a prosecution for false
statements made in connection with a tax return, the alleged false statement must have
“a natural tendency to influence, or [be] capable of influencing, the decision of the
decisionmaking body to which it was addressed” in order to be material. As such, the
“natural tendency” standard remains the definitive interpretation of materiality with
regard to false statements by this nation’s highest court.

While solidified in the context of other statutes, as well as notable Supreme Court
cases outlined above, it was not until *United States ex rel. Berge v. Board of Trustees of
the University of Alabama* (1997), however, that the “natural tendency” standard was first
used in a FCA setting. In *Berge*, a relator brought an action against her former
university employer alleging that the university made false statements to the National
Institutes of Health in connection with a research grant. The Fourth Circuit overturned
the trial court’s grant of a judgment in her favor, holding that the “evidence amounts at
most to a scintilla, which is insufficient to sustain the verdict.” After holding, for the
first time, that the FCA contains a materiality requirement, the court reasoned from its

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74 Id. at 489.
76 Id. at 16.
statement statute); *United States v. McFarland*, 571 F.2d 701, 703 (2nd Cir. 1966) (18 U.S.C. § 1621-
perjury in a grand jury investigation); *United States v. Pruitt*, 702 F.2d 152, 155 (8th Cir. 1983) (18 U.S.C.
§ 287- criminal false claims statute).
78 *Kungys v. United States*, 485 U.S. 759 (1988); *United States v. Wells*, 519 U.S. 482 (1997);
79 *United States ex rel. Berge v. Board of Trustees of the University of Alabama*, 104 F.3d 1453
(4th Cir. 1997).
80 Id. at 1456.
81 Id. at 1462.
82 Id. at 1459.
prior holding in *United States v. Norris* that the proper test for determining materiality, i.e., whether the university’s false statements were material to NIH’s decision to pay out the grant, is “whether the false statement has a natural tendency to influence agency action or is capable of influencing agency action.” Although the defendant’s alleged false statements did not pass muster under the newly enunciated “natural tendency” standard, the court’s decision nevertheless laid a firm precedent for other circuits to follow. In fact, the “natural tendency” standard is now the definitive standard of materiality for typical FCA cases in most circuits.

3. Materiality In Light of the 2009 Amendments to the False Claims Act

While most courts had required at least some showing of materiality before FCA liability could attach, there still was no explicit requirement of materiality in the language of the statute. This changed in 2009 with the coming of the financial crisis and subsequent recession. As part of the Fraud Recovery and Enforcement Act of 2009, Congress specifically provided for a materiality requirement in the statute by replacing the words “to get” in subsection (a)(2) with the words “material to”. Further, it defined the word “material” as “having a natural tendency to influence, or being capable of influencing, the payment or receipt of money or property.” In providing this definition,

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83 Id. at 1460.
84 Id.
88 Id.
the Senate Judiciary Committee noted that “[t]his definition is consistent with the Supreme Court definition, as well as other courts interpreting the term as applied to the FCA.” 89 In a footnote to this statement, the Judiciary Committee cited to the Supreme Court decision in Neder supra as well as six other circuits that followed the “natural tendency” standard set out in Neder. 90 Part IV will discuss why implied certification courts have still rejected the “natural tendency” standard in favor of a precondition to payment standard despite the 2009 amendments to the FCA.

IV. The Precondition to Payment Requirement: A Different Standard for a Different Type of Falsity

With an understanding of the history and evolution of the two traditional standards of materiality under the False Claims Act, we now consider the concept of materiality in the context of the implied certification theory and how the purpose of the FCA as a litigative tool to combat fraud against the government, the legal and policy implications set forth by Congress and the courts in enacting and applying the FCA, and the societal impact of a broader reading of the FCA through expanded use of the implied certification theory shaped and developed an entirely distinct standard of materiality that has manifested as a precondition to payment requirement. We will also look at why the nature of falsity under the implied certification theory, legal falsity, requires a materiality standard that looks at the legal sufficiency of the claim.

A. In Search of a New Materiality Standard for Implied Certification

Recall the example at the beginning of Part I of this Article. The physician submits a claim for payment to Medicare for goods purchased or services rendered. However,

89 Id.
90 Id. at 20 (footnote 6).
suppose he is not in compliance with the Anti-Kickback Statute, a statute that governs claims for payment under Medicare and other Federal health care programs. It “prohibits, among other things, the payment or receipt of any type of benefit in return for the referral of business that is reimbursable under a ‘Federal Health Care Program.’” Assume, also, that the mens rea requirement is satisfied. Does the doctor’s submission of a claim for payment to Medicare constitute a violation of the FCA? In other words, does the doctor’s non-compliance with the Anti-Kickback Statute make his claim for payment to Medicare false under the FCA? In order to answer this question, one must naturally ask whether the doctor’s certification of compliance with the Anti-Kickback Statute was material to the government’s decision to pay. But materiality can have different meanings in different situations, and as such the solution is easier stated than applied.

Sometimes materiality requirements have been imposed as a response to unanticipated problems that arise whenever new theories or novel statutory interpretations are put forward. “False certification cases have presented two problems. First, because false certification cases are often based upon the alleged failure to comply with laws or regulations, some courts have been concerned that the False Claims Act may be used to impose additional penalties for violations of other laws and regulations…Second, in some cases plaintiffs have not identified a document or form falsely certifying compliance with a law or regulation, but have argued that the certification of compliance was ‘implied’ in the defendant's request for payment.” This

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92 Id. at § 1320a-7b(a)(1).
94 Sylvia, supra note 30, at § 4:33.
section will look at how the precondition to payment requirement has been employed by most courts as a response to the broad liability concerns associated with the implied certification theory and why this materiality standard is actually a rejection of the traditional standards of materiality.

1. Ab-Tech and the Early Cases

With the advent of the implied certification theory came the realization of the unprecedented extent of liability it brought in its wake. As a result, courts began to require that the statute or regulation upon which non-compliance was alleged be a precondition to payment of the claim before FCA liability could attach. This doctrine, curiously enough, was the brainchild of Ab-Tech Constr., Inc. v. United States. Recall that Ab-Tech was the first time a court explicitly recognized a FCA action under a theory of implied certification. 95 There, the Federal Claims Court held that “the Government was duped by Ab-Tech’s active concealment of a fact vital to the integrity of [the SBA] program. The withholding of such information—information critical to the decision to pay—is the essence of a false claim.” 96 (emphasis added) This requirement can be seen as a safeguard against uncontrolled liability and abuse of the statute by qui tam plaintiffs and the government and in many ways this language soon became the precursor of the precondition to payment requirement in future cases.

Two years after the decision in Ab-Tech, the Ninth Circuit took up the issue of implied certification in United States ex rel. Hopper v. Anton (1996), a case involving a school district that allegedly submitted false claims for federal funds. 97 In addressing the breadth of liability under the Act, the court held that “[v]iolations of laws, rules, or

95 Berger, supra note 33, at 10.
97 United States ex rel. Hopper v. Anton, 91 F.3d 1261, 1263 (9th Cir. 1996).
regulations alone do not create a cause of action under the FCA. *It is the false certification of compliance which creates liability when certification is a prerequisite to obtaining a government benefit.*”⁹⁸ Apparently, the court was under the impression that because “[t]here are administrative and other remedies for regulatory violations[,]”⁹⁹ it would be improper to hold the school district liable for submitting a false claim. The Fifth Circuit also followed a similar rationale in *United States ex rel. Thompson v. Columbia/HCA Healthcare Corp.* (1997), a case involving claims submitted to Medicare by a physician who was in violation of the Anti-Kickback Statute.¹⁰⁰ There, the court held that “where the government has conditioned payment of a claim upon a claimant's certification of compliance with, for example, a statute or regulation, a claimant submits a false or fraudulent claim when he or she falsely certifies compliance with that statute or regulation.”¹⁰¹

2. Conditions of Payment vs. Conditions of Participation

As we have seen above, statutes or regulations that require compliance with their terms before FCA liability can attach have been categorized by courts as preconditions to payment. This section, therefore, looks at how courts dealing with actions under implied certification have made the distinction between these types of statutes and those that do not, by their nature, require compliance with their terms in order for payment to follow. While there currently is no definitive method for distinguishing conditions of payment from conditions of participation, nevertheless a common thread that runs through these

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⁹⁸ Id. at 1266.
⁹⁹ Id. at 1267.
¹⁰¹ Id. at 902.
cases has been a focus on the legal significance of the statute or regulation at issue and not on the actions of the government.

a. *Mikes*: Existence of Administrative Remedies

The seminal case on the topic of conditions of payment vs. conditions of participation is *Mikes v. Straus* (2001). In that case, a former employee physician brought an action against partner physicians, alleging that they submitted fraudulent Medicare claims. The gist of the employee’s allegations were that the defendant physicians did not conform to American Thoracic Society (ATS) guidelines when performing spirometry tests on patients and that this non-compliance with the guidelines violated § 1320c-5(a), which requires health care practitioners to ensure that goods or services provided by the practitioner “be of a quality which meet[] professionally recognized standards of health care[,]” which in turn, according to the plaintiff, rendered the claims for payment to Medicare false under the FCA. The court began by holding that “a claim for reimbursement made to the government is not legally false simply because the particular service furnished failed to comply with the mandates of a statute, regulation or contractual term that is only tangential to the service for which reimbursement is sought.” With this logic in mind, the court concluded that “[t]he structure of [§ 1320c-5(a)]…informs us that [it] establishes conditions of participation, rather than prerequisites to receiving reimbursement.” This was so because, according to the court, “[t]he fact that § 1320c-5(b) permits sanctions for a failure to maintain an

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103 Id. at 692.
106 Id. at 697.
107 Id. at 701.
appropriate standard of care only where a dereliction occurred in ‘a substantial number of cases’ or a violation was especially ‘gross and flagrant’ makes it evident that the section is directed at the provider’s continued eligibility in the Medicare program, rather than any individual incident of noncompliance.”

b. Hendow: Nature of Government Program

In United States ex rel. Hendow v. University of Phoenix (2006), a case involving claims submitted to the federal government under Title IV and the Higher Education Act that were alleged to be in non-compliance with the statutory and regulatory requirements of those programs, the Ninth Circuit held that in the context of those programs, the distinction between condition of payment and conditions of participation was “a distinction without a difference.” In coming to this conclusion, the court reasoned that in the context of those programs, “if we held that conditions of participation were not conditions of payment, there would be no conditions of payment at all-and thus, an educational institution could flout the law at will.” The defendant University, in attempting to distinguish the two, claimed that “for a condition of participation, an institution says it ‘will comply’ with various statutes and regulations, but for a condition of payment, an institution says that it ‘has complied.’” The court, however, struck down this attempted differentiation between the two, holding that “[t]his grammatical haggling is unmoored in the law.” What the Ninth Circuit is saying, then, is that it matters not if a statute or regulation requires compliance retrospectively or prospectively

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108 Id. at 702.
109 United States ex rel. Hendow v. University of Phoenix, 461 F.3d 1166, 1169 (9th Cir. 2006).
110 Id. at 1176.
111 Id.
112 Id.
113 Id.
in distinguishing between conditions of payment and conditions of participation. While
the court does not provide a definitive answer as to what the discerning factor is, the
court does seem to suggest that the nature of the government program under which
payment is being sought can provide an answer to this question. In fact, in its analysis of
Mikes v. Straus, the Ninth Circuit held that “the Mikes court was dealing with the
Medicare context, to which the court specifically confined its reasoning[,]”114 and noted
that Mikes “imposed an additional requirement on Medicare cases: that the underlying
statute ‘expressly’ condition payment on compliance.”115 The court in Hendow, however,
made clear that “[a]n explicit statement…is not necessary to make a statutory
requirement a condition of payment, and we have never held as much.”116

c. Conner: Language of Statute

In United States ex rel. Conner v. Salina Regional Health Center, Inc. (2008), a
qui tam relator brought an action alleging that the defendant submitted fraudulent claims
to Medicare.117 The plaintiff’s theory of liability was premised on the fact that because
the defendant submitted an “annual cost report” with the government certifying
compliance with Medicare laws and regulations, each and every time it submitted a claim
for payment to the government knowing it was not in compliance with the laws and
regulations was a violation of the FCA.118 In holding that the relator did not state a valid
claim under the FCA, the court began by noting that the language in the “annual cost
report” certifying compliance with the Medicare laws and regulations contained “only

114 Id. at 1177.  
115 Id.  
116 Id.  
118 Id.
general sweeping language and does not contain language stating that payment is conditioned on perfect compliance with any particular law or regulation.”\textsuperscript{119} The court then went on to distinguish the two types of conditions from one another: “Conditions of participation, as well as a provider's certification that it has complied with those conditions, are enforced through administrative mechanisms, and the ultimate sanction for violation of such conditions is removal from the government program...Conditions of payment are those which, if the government knew they were not being followed, might cause it to actually refuse payment.”\textsuperscript{120}

According to the court, because the relevant regulations “grant “[a]ll providers and suppliers an opportunity to correct the deficient compliance before a final determination to revoke billing privileges[,]...and then [o]nly after finding that the provider has not substantially complied may the government, at its discretion, terminate a Medicare participation agreement.”\textsuperscript{121} As such, the court is essentially looking at the language of the statute in determining whether it is a condition of payment, and the main distinction the court uses here, it seems, is whether there are other statutory or administrative remedies available to the government instead of, or prior to, withholding payment. In making this argument, the court distinguished its decision from Hendow, holding that other courts, such as Hendow, have recognized that “some regulations or statutes may be so integral to the government's payment decision as to make any divide between conditions of participation and conditions of payment a distinction without a difference.”\textsuperscript{122} One interesting point to note, however, is that the court in Conner did

\textsuperscript{119} Id. at 1219.
\textsuperscript{120} Id. at 1220.
\textsuperscript{121} Id. at 1221.
\textsuperscript{122} Id. at 1222.
wish to emphasize that “our resolution of this case does not preclude the possibility that certain Medicare statutes or regulations might expressly or implicitly condition payment on certification of compliance under a false certification theory.”

B. Focusing on the Legal Falsity of the Claim Rather than the Actions of the Government

With a clear understanding of the characteristics of all three materiality standards that have been used in a FCA setting, we can now determine which is best suited to the requirements of the implied certification theory. Remember that this theory concerns itself not with factually false claims, but with legally false claims. The distinction essentially turns on what information in the claim form is being certified as true: if it is certain facts, such as whether the contractor has provided the requisite goods or services, then we are concerned with a factually false claim. If instead it is a statement of compliance with applicable statutes and regulations, then we are dealing with a legally false claim.

1. Searching for Compatibility: An Analysis of the Three Materiality Standards

The following test suites will examine the scope of liability under each of the three standards of materiality: outcome determinative, natural tendency and precondition to payment. Through analysis of these test suites, we will be able to determine which materiality standard is better suited to the policy goals of the FCA. Further, they will show that a materiality standard that focuses on the actions of the government, as the

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123 Id.
124 Holt, supra note 2, at 16.
125 Id.
126 Levy, supra note 31, at 134.
outcome determinative and natural tendency standards do, is incorrect in the context of the implied certification theory. For each scenario, we will assume that the defendant did not comply with the applicable statutes or regulations at issue, whether he expressly certified compliance or not.

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<th>Outcome Determinative</th>
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<th>Precondition to Payment</th>
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As defined above, the outcome determinative standard of materiality requires the government to prove that it would have acted upon false information in a claim for payment, not that it could have. Or in other words, that it actually relied on the false information, not that it may have. As the test suites clearly show, the outcome determinative test does not depend on whether the statute or regulation at issue is a precondition to payment. Rather, it simply looks at the action of the government, i.e., whether it paid the claim or not. If the claim was paid, liability attaches. The problem with this standard, however, is that it expands liability beyond the original scope of the FCA by holding defendants liable when they were either ignorant or unaware of the
multitude of regulations surrounding their activity, such as a primary care physician working within the vast framework of Medicare regulations. This unprecedented expansion of liability undoubtedly conflicts with the mens rea requirement of the statute, which provides for liability only when a person “knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval.” As such, the outcome determinative test remains a poor standard for materiality in the context of the implied certification theory.

The natural tendency standard fares no better. In fact, it is far more dangerous in that liability does not end when the government does not pay the claim, as with the outcome determinative standard. Rather, even if the government does not pay the claim, a defendant can still be held liable if the government could have been influenced to pay out the claim. What suffices to satisfy this ambiguous “could have been” standard will usually depend upon a fact-intensive analysis of the circumstances surrounding the claim for payment. While no clear definitive approach exists, owing to the complex nature of this materiality standard, some courts have held that overt acts on the part of the defendant to get the claim paid may be relevant, while others have held that the nature of the government program at issue may be helpful in determining liability. In reality,
however, such a dubious standard ultimately depends upon an analysis of the mental state of the government *agent* who paid the claim. This is so because in the context of claims for payment to the government, the government is not some abstract notion of a sovereign entity dealing out fairness and justice. Rather, it is a government agent or employee who approves or rejects such claims. Having established this reality, we can now turn our attention to the *unreality* of a judge or jury determining what information a random government agent within a federal agency relied upon in deciding to pay out a claim. To put it succinctly, how can one inquire into the mind of another by delving into his thought processes to determine the extent of his knowledge and intent as to what information he considered relevant and material in paying out a claim? This type of mental probing would require telekinetic abilities that are not yet available to human beings.

If the absurdity of this approach to materiality under the natural tendency standard is not yet apparent, consider that under this standard, which still remains the explicit standard of materiality under the FCA, the government need only prove that the falsity was of such a nature that a *reasonable person* could rely on it. Further, “[a] statement or omission is ‘capable of influencing’ a decision even if those who make the decision

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130 United States v. McBane, 433 F.3d 344, 351 (3rd Cir. 2005) (“[T]he language of the [natural tendency] materiality standard and the decisions applying that standard require only that the false statement at issue be of a type capable of influencing a reasonable decisionmaker”); United States v. An Antique Platter of Gold, 184 F.3d 131, 138 (2nd Cir. 1999) (“[I]nformation that has a natural tendency to influence a reasonable customs official”).
are negligent and fail to appreciate the statement's significance.”

It is for these reasons that at least one court has explicitly called into question the validity and scope of the “natural tendency” standard in the context of an implied certification case. As such, it remains clear that the natural tendency standard is ill-suited to the implied certification theory, which requires far more certainty than this indeterminate and conjectural materiality standard can supply. Instead of focusing on factual inquiries into a government agent’s mental state, which because of the obvious speculation inherent in this process, must be supplemented by a court’s determination of a defendant’s overt acts or the nature of the government program at issue, rather the cynosure of any materiality inquiry should be based entirely on the legal significance of the statute or regulation at issue. That is where the precondition to payment materiality standard comes in.

2. The Precondition to Payment Standard: A Perfect Fit for the Policy and Fairness Considerations of the Implied Certification Theory

The precondition to payment standard means exactly what it says: it requires the government to prove that compliance with the statute or regulation upon which the certification is based is a sine qua non, or prerequisite, to payment. This differs from the two traditional standards of materiality in that it does not focus on the acts of the government (or more accurately, a government agent) in determining whether materiality has been satisfied. Instead, the precondition to payment standard focuses entirely on the

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132 United States v. Rogan, 517 F.3d 449, 452 (7th Cir. 2008).
133 United States ex rel Steury v. Cardinal Health, Inc., 625 F.3d 262, 269 (5th Cir. 2010)
(“Although the FCA now defines the term ‘material’ somewhat more expansively [i.e., as having a ‘natural tendency to influence, or be capable of influencing, the payment or receipt of money or property’], we do not think that our false-certification precedents are obsolete. The prerequisite requirement has to do with more than just the materiality of a false certification; it ultimately has to do with whether it is fair to find a false certification or false claim for payment in the first place”).
legal significance of the statute or regulation at issue. But why should this matter? What is unique about the implied certification theory that it requires a materiality analysis that focuses on the legal significance of the statute or regulation at issue as opposed to one that simply focuses on the action of a government agent?

If we are dealing with *legal* compliance issues, then, one must naturally apply a materiality analysis that focuses on the *legal* sufficiency of a claim. This is what the precondition to payment requirement does. Instead of engaging in an impossible analysis of the vague thought processes of an obscure government agent or employee, we look instead to the legal compliance of the certification: 1) Does the claim certify compliance with an applicable statute or regulation? 2) Was the certification false? 3) Did the defendant do so knowingly? 4) Was the statute or regulation at issue a precondition to payment?

Under the precondition to payment requirement, liability attaches only under one scenario: when the statute is a precondition to payment. If it is not, then it does not matter that a government agent paid the claim; liability cannot attach. Likewise, under the scenario where the statute or regulation *is* a precondition to payment, it is also immaterial whether the government paid the claim or not; liability attaches here as well. This is so because “the False Claims Act clearly prohibits fraudulent acts even if they do not cause a loss to the government.”\(^\text{135}\) The legislative history of the Act also supports this: “[E]ach and every claim submitted under a contract, loan guarantee, or other agreement which was originally obtained by means of false statements or other corrupt or fraudulent conduct, or in violation of any statute or applicable regulation, constitutes a false

claim. Liability here makes sense because it is not unfair to hold a defendant liable for submitting a knowingly false claim even when the government did not pay it. Payees under a government program should be aware of the statutes and regulations they need to comply with in order to receive payment. As such, because it does not matter whether a government agent paid the claim, it is clear that in implied certification cases, i.e., cases dealing with legal certification, materiality truly hinges on whether the statute or regulation at issue is a precondition to payment and not on the actions of a government agent. As such, in the context of legal certification cases, any materiality analysis that focuses on the actions of a government agent, as the “outcome determinative” and “natural tendency” standards do, is clearly incorrect.

Each of the three methods outlined above that are utilized by courts to determining whether a statute or regulation is a precondition to payment (existence of administrative remedies, nature of government program, language of statute) essentially boils down to an analysis of whether the statute or regulation qualifies as a condition of payment or a condition of participation. While each method is useful in its own way, a still better approach to determining whether a statute or regulation is a precondition to payment is simply by asking whether the government could use noncompliance with that particular statute or regulation as a defense to an action for payment by the prospective payee. If this is answered in the positive, then the statute at issue is a precondition to payment and liability will attach. In engaging in an analysis of this sort, a reviewing court should utilize all three methods above in coming to its conclusion and not be bogged down by one approach. In so doing, a court will have its task alleviated considerably.

while at the same time producing a much more accurate result that will lend credence to the result reached by the court.

V. Conclusion

The implied certification theory of the False Claims Act presents a distinct issue with respect to the scope of liability it envisions. The precondition to payment requirement solves this scope of liability concern by focusing not on the overt acts of the government as the traditional standards of materiality do, but rather on the sufficiency of the legal certification itself. Without this distinction, the breadth of FCA liability would be unpredictable at best and unprecedented at worst. This is why courts have historically applied the precondition to payment standard in implied certification cases and it is why courts should continue to do so in the future.

In the high stakes game of FCA litigation based on the theory of implied certification, courts, attorneys and especially the health care sector cannot afford to be unsure as to the possible scope of liability under the FCA. With over 300 FCA actions filed by *qui tam* plaintiffs each year in the past fifteen years\(^\text{137}\) and over $2.5 billion collected in *qui tam* actions in 2010 alone,\(^\text{138}\) the dire importance of certainty in this area of the law can no longer be overlooked. The precondition to payment standard provides this certainty by focusing on what makes a claim for payment truly false and staying true to the original intent of the FCA as a tool to combat fraud. While the implied certification theory gains ground in the federal courts, litigants will continue to test its boundaries,\(^\text{139}\)

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\(^{137}\) Holt, *supra* note 2, at 2.

\(^{138}\) *Id.*

but the precondition to payment requirement should remain as the definitive standard of materiality in cases under the implied certification theory.