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Bad Mules

A Primer on the Federal False Claims Act

Access to
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By Larry D. Lahman

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Worse than traitors in arms are the men who pretend loyalty to the flag, feast and fatten on the misfortunes of the nation while patriotic blood is crimsoning the plains of the south and their countrymen are moldering in the dust.” — Abraham Lincoln

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The Federal False Claims Act (“FCA”)1 was enacted in part because of bad mules. During the Civil War, unscrupulous early day defense contractors sold the Union Army decrepit horses and mules in ill health, faulty rifles and ammunition, and rancid rations and provisions among other unscrupulous actions.

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These frauds caused President Abraham Lincoln to urge Congress to pass in March 1863 the original FCA commonly known as the “Informer’s Law” or the “Lincoln Law” after President Lincoln.2

The FCA made it illegal for someone (claimants) to present false statements in writing (claims) to the United States government to improperly obtain more money from (or in some cases pay less money to) the government than actually owed by the government (or due from the claimant).

THE RELATOR

Importantly the FCA authorized a private citizen (a relator) acting as a “private attorney general” — as well as the government — to sue the claimant to recover the amount actually due the government plus a multiplier and penalties. A key provision of the original FCA was to award 50 percent of the recovery to encourage and reward relators (the “relator’s share”) for exposing and prosecuting the fraud. 3

An action filed by a private relator on behalf of the government is known as a “*qui tam*” action — roughly translated as one who sues for the king4, because *qui tam* actions are found in the

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early English common law.

These *qui tam* lawsuits are commonly known to the public as “whistleblower” lawsuits and in fact the current FCA contains protections for the relator against retaliation from his employer when FCA allegations are made in good faith.⁵

Suits filed by the government do not involve a relator and are known simply as false claims actions *sans qui tam*.

THE 1943 AMENDMENTS

Following perceived abuses by a number of so-called “parasitic” FCA lawsuits filed by plaintiffs relying on information already in the government’s possession or public knowledge, the FCA was crippled by congressional amendment in 1943.

The 1943 amendments greatly reduced the relator’s share and eliminated *qui tam* lawsuits when the government had prior knowledge of the fraud — even when the government had taken no action after a number of years and obviously intended to take no action to stop the fraud.

The 1943 amendments stopped virtually all *qui tam* cases, and fraud against the government increased. The 1943 amendments teach us that the government itself far too often does not want to expose fraud for many reasons.⁶

The 1986 Amendments

During the massive defense buildup of the 1980s, reports of \$900 toilet seats and \$500 hammers aroused congressional ire. A new era for the FCA was ushered in by amendments to the FCA in 1986 championed by U.S. Sen. Charles Grassley of Iowa and signed into law by President Reagan. Grassley remains in the U.S. Senate and continues to champion the FCA by publicizing its successes and attempting to improve its utility.⁷

The 1986 amendments vastly strengthened the FCA as a tool for fighting profiteering and fraud against the government. The 1986 amendments increased the relator’s share⁸, provided for treble damages⁹, granted employees whistleblower protection¹⁰, extended the statute of limitations¹¹ and reduced the level of proof for fraud to “actual knowledge,” “deliberate ignorance” or “reckless disregard.”¹²

Significantly the current FCA allows the government to recover treble the amount it is due as well as penalties¹³ and fees for the relator’s attorneys in *qui tam* cases.¹⁴ Its impact on the

federal “fisc” has been enormous, resulting in the recovery of over \$2 billion in 2003 and more than \$13 billion since 1986. In 2003 about 70 percent of the recovery came from relator initiated *qui tam* lawsuits.¹⁵

Because wrongdoers now face the threat of having to repay more than the amount stolen under its treble damage provisions, the FCA silently deters untold fraud against the government by its mere presence. It has a major impact on deterring fraud on the taxpayers and has been largely unchanged since 1986 despite periodic attempts by those it targets to gut it. ¹⁶

FILING THE CASE

The FCA requires a relator to “disclose” his knowledge of the fraud to the government before filing suit. This is normally done in the form of a “disclosure statement.” The lawsuit is then filed in secret or under “seal” and only the government is notified of the action so that it can investigate the merits of the relator’s allegations.¹⁷

During this “seal period,” which can be extended by the court for “cause” for long periods, the government investigates and decides whether the case has sufficient merit to justify “intervening” and taking over prosecution of the case. Although the initial seal period is 60 days, cases have remained under seal for nearly a decade while the government investigates.¹⁸

GOVERNMENT INTERVENTION

If the government intervenes, the Department of Justice takes over the *qui tam* case from the relator and his attorneys and prosecutes it as any other.¹⁹ Large cases are managed by Department of Justice from the Attorney General’s Office Civil Division in Washington D.C. and U.S. attorneys assist locally. Smaller cases are apt to be controlled in large measure by the local U.S. attorneys with final authority in Washington.

Once the government opts to intervene, the case is “unsealed” and the defendant claimant is served, which is normally the first formal notice the claimant receives of the action.²⁰

Initially the government intervenes in about one-fifth of the cases it reviews.

The relator and his attorneys can and typically do remain involved in varying degrees in an intervened case, but the government through the Department of Justice controls the

case. The government can settle the case if “fair, adequate, and reasonable,” but the relator is entitled to notice and to be heard.²¹

The relator typically seeks government intervention because of the greater resources the government can theoretically bring to bear on a case if it so chooses such as FBI interviews, wiretaps and reviews of internal government documents. This is so even though the relator’s share is reduced in intervened cases because the relator believes that a smaller slice of a larger pie is better.

A tool available to the Department of Justice, somewhat unique to the FCA, known as a Civil Investigative Demand, is also a possibility and is similar to a subpoena.²²

Because of its ability to “cherry pick” by intervening only in good cases, withdrawing from a case which develops problems and getting back in when the case gets better,²³ the government’s track record is of “Babe Ruth” proportions; in fact the government rarely loses intervened cases. This remarkable record of success also results from the specter of penalties and treble damage provisions. The government’s willingness to waive penalties and accept less than triple damages or even less than “doubles” is a powerful inducement to settle for a claimant caught with his hand in the cookie jar.

GOVERNMENT DECLINATION

Conversely, the government may provide notice that it declines to intervene for a variety of reasons including lack of merit. In such cases the relator and his counsel must decide whether to dismiss or prosecute the case on behalf of the government.²⁴

Should the government decline to intervene and the relator opts to proceed with the litigation, the case is “unsealed” and the defendant claimant served which is normally the first formal notice the claimant receives of the action as in an intervened case.

The relator proceeds with the case on behalf of the government and the Department of Justice remains involved in varying degrees receiving notice of filings. The relator can attempt to settle the case but the government is clearly entitled to notice and to be heard. If the settlement is substantial, the government will almost certainly intervene to get “credit” for the settlement and to attempt to reduce the relator’s share which seems to be at variance with congressional intent to reward

whistleblowers who risk much to help the government.

THE RELATOR'S SHARE

At the heart of the FCA is the relator's entitlement to a sizable portion of the recovery which has caused some wrongdoers to refer to the FCA as the "Bounty Hunter's Law." To be sure the possibility of "doing well while doing good" is a major reason for reinvigorating the FCA under the 1986 amendments.

Significantly the relator is entitled to 15–25 percent of the recovery in intervened cases²⁵ and 25–30 percent in declined cases²⁶ and since this includes trebled damages, the relator's share can be sizable.

Some complain these bountiful rewards are unjustified and harm the federal treasury; however, as the government can recover treble damages plus penalties, the net to the government will nearly always exceed what has been taken from it even after the relator's share is deducted. Said another way, the relator makes the government whole for fraud the government knew nothing about, did nothing about, or both.

DEBARMENT AND CRIMINAL PROVISIONS

While not a part of the FCA, the government has the authority to prohibit corporations and individuals guilty of fraud from doing business with the federal government. This "debarment" or exclusion authority is considered the equivalent of the death penalty, because for major health care corporations and defense contractors which rely on federal contracts, denying them federal contracts effectively puts them out of business.²⁷ The government rarely exercises this authority — although it could more often to deter an ongoing pattern of criminal fraud.

Violation of the FCA also has criminal ramifications that the government can in theory pursue without regard to the civil aspects of the FCA.²⁸

GENERAL TARGETS

Beginning with the Civil War and continuing with the 1986 amendments, the FCA primarily targeted defense contractor fraud;²⁹ however, it is increasingly used to recover for Medicare and Medicaid fraud.³⁰ In 1987, medical fraud comprised 12 percent of *qui tam* cases but in 10 years had increased to 54 percent of the cases.³¹

In recent years the oil and gas industry has been subject to the

FCA in cases where the producer failed to pay the government its full share of royalties from government owned lands.³² This illustrates the “reverse false claim” where a claimant submits a false document to the government attempting to reduce the amount paid to the government rather than increase the amount the claimant is paid by the government.³³

Other reverse false claims include bulk or mass mailers certifying that their mailing is eligible for fourth class postage rather than third class that carries a higher rate. Actual recovery in these bulk mailing FCAs have been in the millions.

SPECIFIC FRAUDS

The FCA widely applies to almost any situation where federal dollars are found. The range of FCA cases has grown and will continue to grow limited only by the relator’s ingenuity and creativity. They include but are certainly not limited to:

- education grants
- Medicare fraud
- Medicaid fraud
- part suppliers
- environmental certifications
- emergency relief programs
- housing programs
- defense contracting

Recall that penalties up to \$11,000 may now be imposed for each false claim even where no damages are proven.³⁴ When these penalties are aggregated because of many false claims for small amounts, the resulting FCA recovery can be sizable. This is particularly true in medical fraud where the claims are small but the number is large. A list of the known fraud against the Medicaid program includes:

- kickbacks
- double billing
- upcoding
- services without medical need
- untrained personnel for services
- unsupervised, unlicensed workers
- use of unapproved drugs
- inadequate care
- use of substandard equipment
- forgery of physician’s signatures

- use of phony insurance carriers
- unbundling

MAJOR RECOVERIES

The “Corporate Crime Reporter” recently released a list of the 100 largest FCA recoveries since 1863 and in each the whistleblower relator’s share was more than \$1 million — in one case over \$70 million. Of the top 100 false claims settlements, 56 were with health care corporations, while 23 were defense contractors.

The largest FCA settlement in history was the December 2000 recovery from HCA, formerly known as Columbia HCA. HCA, the largest for-profit hospital chain in the U.S., pleaded guilty to criminal conduct and agreed to pay more than \$840 million in criminal fines, civil penalties and damages for unlawful billing practices. Of this amount, \$731 million was recovered under the False Claims Act.

HCA’s frauds on the taxpaying public included: billing for lab tests that were not medically necessary and not ordered by physicians, “upcoding” medical problems in order to get higher reimbursements for more serious medical issues, billing the government for advertising under the guise of “community education,” and billing the government for non-reimbursable costs incurred in the purchase of home health agencies around the country.

The second largest settlement was also against HCA for \$631 million in June 2003. Rounding out the top five settlements were TAP Pharmaceuticals for \$559 million in October 2001; Abbott Labs for \$400 million in July 2003; and Fresenius Medical Care for \$385 million in January 2000.³⁵

Rampant and pervasive corporate fraud illustrated above, by Enron and WorldCom, as well as on Wall Street and now the insurance industry demonstrates that corporate fraud occurs far too often and provides fertile ground for the FCA.

OKLAHOMA RECOVERIES

The largest FCA settlement in Oklahoma announced in August 2004 was for \$16 million in a Western District of Oklahoma case.³⁶ In this case, farmer and then law student Roger Ediger discovered what he believed to be a problem with interest assist subsidy payments made to Gold Bank by the United States Department of Agriculture Farm Service Agency. These interest

assist payments were intended to benefit farmers with Farm Service Agency guaranteed loans at Gold Bank.

Ediger, acting as relator, and his attorneys successfully prosecuted an FCA action in the Western District of Oklahoma resulting in the \$16 million recovery for the government. The settlement also included statutory attorney fees for Ediger's attorneys.³⁷ At the time of settlement, *Ediger* was among the 100 largest recoveries in the 140-year history of the FCA.

The *Ediger* case was the first known use of the FCA in the Farm Service Agency Guaranteed Loan Program and is an example of the creative uses of the FCA that can be expected to grow in the coming years.

STATE FCAS

Beginning with California in 1987, a number of states have enacted state FCAs with New Mexico the most recent addition. Most of these state FCAs are modeled on the Federal FCA, but several are limited to contractor or medical fraud.

Fourteen states plus the District of Columbia have some version of an FCA: Arkansas,³⁸ California,³⁹ Delaware,⁴⁰ District of Columbia,⁴¹ Florida,⁴² Hawaii,⁴³ Illinois,⁴⁴ Louisiana,⁴⁵ Massachusetts,⁴⁶ New Mexico,⁴⁷ Nevada,⁴⁸ Tennessee,⁴⁹ Texas,⁵⁰ Utah⁵¹ and Virginia.⁵² FCA legislation is pending in a number of other states and even some cities like Chicago and New York City.

Efforts since at least 2000 to pass such legislation in Oklahoma⁵³ have been unsuccessful. Experience elsewhere is that a state FCA would increase revenue to the state and local governments and provide immeasurably improved government at all levels. Honest merchants, tradesmen and contractors who deal with government prefer a level playing field and not be forced to compete against a dishonest competitor. The taxpayer benefits greatly because of recoveries and the mere presence of the FCA.

One only needs to read Oklahoma history about scandals involving the county commissioners in the 1970s, the state Health Department in the 1990s and the Tax Commission in the 2000s to see how an FCA in Oklahoma would be useful. ⁵⁴

RESOURCES

While it's been around since Civil War, the FCA does not occupy a lot of shelf space in law libraries⁵⁵; however, there are three

primary treatises:

- The newest entry, *The False Claims Act: Fraud Against The Government*, West, 2004 (Claire M. Sylvia), is complete, balanced, helpful and readable.
- *False Claims Act: Whistleblower Litigation*, LexisNexis, Third Edition, 2002 (James B. Helmer Jr.) is another very readable recent publication written from the angle of the relator. It offers a good deal of helpful commentary.
- *Civil False Claims and Qui Tam Actions*, Aspen Law & Business, 2nd ed. Supp. 2003-2 (John T. Boese) is written from the viewpoint of one who represents defendants in FCA cases.

The single most valuable FCA resource is the Taxpayers Against Fraud Education Fund — a nonprofit, public interest organization dedicated to combating fraud against government through the promotion and use of the Federal False Claims Act and its qui tam provisions. Taxpayers Against Fraud maintains a Web site of incalculable value at www.taf.org and also publishes the “False Claims Act and Qui Tam Quarterly Review.”

CONCLUSION

As this is intended to be but a primer for those unfamiliar with the FCA, a number of concepts like materiality, original source, exclusions, first to file, public disclosure, corporate integrity agreements, statute of limitations and venue are left to another day. At first reading the FCA appears to be simple. It is not. The above noted resources cover these and many other topics well.

With the epidemic in corporate wrongdoing, the FCA is vital to those concerned about profiteering, fraud and integrity in government. It presents a unique opportunity for those with knowledge of fraud to do well by doing good. So too, does the FCA provide a largely untapped practice area to Oklahoma lawyers likewise disposed to do well by doing good.

1. 31 USCA §§ 3729 et seq., hereafter all sections refer to the FCA unless otherwise noted.
2. Still earlier dating back to at least as early as 1692, the American colonies allowed citizens to sue on behalf of the government but the FCA in its current form originated in the Civil War. Claire J. Sylvia, *The False Claims Act: Fraud Against the Government* (1st ed. 2004) § 2:5, hereafter “Sylvia.”
3. Act of March 2, 1863, ch. 67, § 6, 12 Stat. 698.
4. More fully *qui tam pro domino rege quam pro se ipso in hac*

parte sequitur or “he who brings the action for the king as well as for himself”. 3 Sir William Blackstone, *Commentaries on the Laws of England* 161.

5. § 3730(h).

6. Sylvia § 2:8.

7. Sylvia § 2:9.

8. § 3730(d).

9. § 3729(a).

10. § 3730(h).

11. § 3731(b).

12. § 3729(b).

13. Prior to Sept. 29, 1999, the FCA imposed penalties of at least \$5,000 and up to \$10,000 (“penalties”) at the discretion of the judge. § 3729(a)(1)–(7). These sums increased to \$5,500 and \$11,000 effective Sept. 29, 1999. 28 C.F.R. § 85.3(a)(7).

14. § 3730(d)(2).

15. Sylvia Appendix D.

16. Sylvia § 2:11.

17. § 3730(b)(2).

18. § 3730(b)(3).

19. § 3730(c)(1).

20. § 3730(c).

21. § 3730(c)(2)(B).

22. § 3733.

23. § 3730(c)(3).

24. § 3730(c)(3).

25. § 3730(d)(1).

26. § 3730(d)(2).

27. The authority and procedure required for debarment is found in a number of places in federal and state law. Lists of debarred entities are likewise numerous.

28. 18 U.S.C.A. § 287.

29. Sylvia § 2:13.

30. Sylvia § 2:14.

31. 12 False Claims Act & Qui Tam Q. Rev. 41 (Jan 1998).

32. Sylvia § 2:17.

33. § 3729(a)(7).

34. *Varljen vs Cleveland Gear Co.*, 250 F3d 426, 429 (6th Cir. 2001).

35. “Top 100 False Claims Act Settlements”, “Corporate Crime Reporter,” Dec. 30, 2003,

<http://www.corporatecrimereporter.com/fraudrep.pdf> .

36. *USA ex rel. Roger Ediger vs. Gold Banc*, et al., CIV-02-1493-R, United States District Court for the Western District of Oklahoma.

37. In the interest of full disclosure the author and his firm prosecuted Ediger with Susman Godfrey of Dallas. The

- government intervened for settlement purposes a month after the \$16 million settlement was negotiated by Ediger's attorneys. Ediger is now a member of the author's firm.
38. ARK. CODE ANN. Sec 20-77-901 et seq. (2000). [Medicaid].
 39. CAL. Gov't Code Sec 12650 et seq. (DEERING 2000). [General].
 40. DEL. CODE. ANN. tit. 6, Sec 1201 et seq. (2000). [General].
 41. D.C. CODE ANN. Sec 1-1188.13 et seq. (2000). [General].
 42. FLA. STAT. 68.081 et seq. (2000) [General].
 43. HAW. REV. STAT. Sec 661-22 et seq. (2000). [General].
 44. 740 ILL. COMP. STAT. ANN. Sec 175/1 et seq. (2000). [General].
 45. LA. REV. STAT. ANN. Sec 46:439.1 et seq. (2000). [Medical Assistance].
 46. MASS ANN. LAWS CH. 12, Sec 5(A)-(O).
 47. Signed by Governor Effective May 19, 2004.
 48. NEV. REV. STAT. Sec 357.010 et seq. (1999). [General].
 49. TENN. CODE. ANN. Sec 71-5-181 et seq. (2000). [Medicaid].
 50. TEX. HUM. RES. CODE Sec 36.001-36.117.
 51. UTAH CODE ANN. Sec 26-20-1 et seq. (2000). [Medicaid].
 52. VIRGINIA Fraud Against Taxpayers Act, effective Jan. 1, 2003.
 53. Oklahoma has a *qui tam* law but it has little similarity to the Federal FCA or the false claims acts found in other states, 62 OS §§ 372-373.
 54. "If individuals who violate the law are required to pay more than the actual harm they impose, the sanctions should have a deterrent effect, even if the risk of getting caught is low." Sylvia § 1:3 summarizing Garry S. Becker, "Crime and Punishment, An Economic Approach", 76 J. Political Economy 169 (1968).
 55. For an eminently readable book on the history of the modern FCA and experiences of whistleblowers under the new law, the Giant Killers: The Team and the Law That Help Whistle-blowers Recover America's Stolen Billions by Henry Scammell, Atlantic Monthly Press (New York, 2004) is highly recommended. It reads like a John Grisham book but it's true.

About the Author

Larry D. Lahman is a partner in the Enid law firm of Mitchell and DeClerck. His practice is concentrated in representing whistleblowers against large corporations in *qui tam* and related litigation. He holds a J.D. from the OU College of Law and a B.S. in chemistry, mathematics and physics from Northwestern Oklahoma State University. This is his ninth article for the *Oklahoma Bar Journal*.

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