"Traps, Zaps, and Zingers:" District Court Overturns $350 Million False Claims Act Jury Verdict for Want of Materiality

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On January 11, 2018, the United States District Court for the Middle District of Florida[1] set aside a nearly $350 million False Claims Act (FCA) jury verdict rendered in February 2017 against a group of fifty-three skilled nursing facilities (SNFs).[2] In overturning the jury's decision, the court found that the relator failed at trial to adduce sufficient evidence of materiality or scienter. That is, the relator failed to produce evidence "that the federal government and the state government did not know about the record-keeping deficiency but, had the governments known, the governments would have refused to pay the operators of the fifty-three specialized nursing facilities for services rendered, products delivered, and costs incurred."[3] Here, the jury's determination of materiality and scienter (*i.e.*, the defendants' knowledge of the materiality) was premised entirely on speculation as to how the government *might* have addressed an alleged record-keeping deficiency. Following the Supreme Court's landmark decision in *Escobar*, the court noted that materiality cannot be established merely by showing that the government would have the *option* to decline to pay if it knew of the defendant's noncompliance.[4]

Importantly, the court emphasized the "rigorous standard" for proving both materiality and scienter under the FCA. Because the governments had received "fair value" from the nursing homes, and had continued to make payments despite knowledge of certain record-keeping issues, relator could not demonstrate that such noncompliance was material to the government (or that the nursing homes knew such noncompliance was material). Under *Escobar*, such "traps, zaps, and zingers" – that is, a showing of immaterial contractual or regulatory noncompliance – are insufficient for a finding of liability under the FCA.

I. The Ruckh Decision

On February 15, 2017, the relator obtained a jury verdict of $115 million in actual damages, which the court trebled to $345 million (plus another $2.5 million in civil penalties),[5] based on the theory "that upcoding of RUG levels and failure to maintain care plans made [the defendants'] claims to Medicare and Medicaid false or fraudulent."[6] Thereafter, on March 29, 2017, the defendants moved for judgment as a matter of law, arguing in pertinent part, that relator failed to "establish with legal adequacy that any underlying falsehood was material to the government's payment decision, as defined by the Supreme Court in [*Escobar*]."[7]

The court agreed and granted the motion, vacating the judgment. The court held that relator "offered no meaningful or competent proof that the federal or state government . . . would have regarded the disputed practices as material to each government's decision to pay the defendants and, consequently, that each government would have refused to pay the defendants."[8] The court further held that relator failed to meet the FCA's scienter requirement, which requires a showing that

1 *United States ex rel. Ruckh v. Salus Rehabilitation, Inc.*,No. 8:11-cv-1303-T-23TBM, Dkt. No. 468 (M.D. Fla. Jan. 11, 2018) ["*Ruckh*"].
2 *Ruckh*, No. 8:11-cv-1303, Dkt. No. 430 (Feb. 15, 2017).
3 *Ruckh*, No. 8:11-cv-1303, Dkt. No. 468 at 12 (Jan. 11, 2018).
4 *Universal Health Servs., Inc. v. United States*, 136 S.Ct. 1989, 2003 (2016).
5 *Ruckh*, No. 8:11-cv-1303, Dkt. No. 431 (Mar. 1, 2017).
6 *See* Relator's Opp. to Def.'s Renewed Dispositive Motion for Judgment as a Matter of Law, *U.S. ex rel. Ruckh v. Salus Rehabilitation, Inc.*, No. 8:11-cv-1303, Dkt. No. 454, at 2 (Apr. 12, 2017).
7 *Ruckh*, No. 8:11-cv-1303, Dkt. No. 452, at 6 (Mar. 29, 2017).
8 *Ruckh*, No. 8:11-cv-1303-T-23TBM, Dkt. No. 468, at 2.

"the defendants submitted claims for payment despite the defendants' knowing that the government would refuse to pay the claims if either or both governments [federal or state] had known of the disputed practices."[9] In fact, noted the court, despite its awareness of the disputed practices, the government has not, to date, "ceased to pay or even threatened to stop paying the defendants" for the disputed services since this action's inception in 2011.[10] Said the court:

> [T]he record fatally wants for evidence of materiality and scienter; the evidence that exists gravitates contrary to materiality and scienter. The defendants delivered the services for which the governments [the United States and the State of Florida] were billed; the governments paid and continue to pay to this day despite the disputed practices, long ago known to all who cared to know. . . . [R]elator's burden was to show that the federal government and the state government did not know about the record-keeping deficiency but, had the governments known, the governments would have refused to pay the operators of fifty-three specialized nursing facilities for services rendered, products delivered, and costs incurred.[11]

In drawing this conclusion, the court highlighted the importance of the government's past response to similar deficiencies in determining materiality: "The evidence shows not a single threat of non-payment, not a single complaint or demand, and not a single resort to an administrative remedy or other sanction for the same practices that result in the enormous verdict at issue."[12]

The court also highlighted the importance of distinguishing between alleged deficiencies that go to the heart of the bargain and those that are secondary to the actual service or product that the government is purchasing. As the court noted, "*Escobar* assumes and enforces a course of dealing between the government and a supplier of goods or services that rests comfortably on proven and successful principles of exchange – fair value given for fair value received."[13] The FCA does not support "a system of government traps, zaps, and zingers" that would allow the government to receive and retain the benefit of its bargain while suing to recover the entire cost (multiplied by three) of the goods or services because of some immaterial contractual or regulatory non-compliance.[14]

> Speaking to the factual context of *Escobar*, the court observed:
>
> No reasonable purchaser would accept or pay for psychiatric or psychological diagnosis and treatment from, or accept or pay for psychotropic medication prescribed by, an array of charlatans and quacks. With predictable and sound reciprocity, the law charges the charlatans and quacks with knowledge of their own disrepute, that is, with knowledge that the information they have designed to misrepresent, hide, and distort would, to say the least, materially influence the decision of the party deciding whether to pay.[15]

Thus, it would be "undoubtedly obvious to the provider" that use of "unqualified mental health providers and substandard mental health care" would "profoundly and manifestly affect[] a government's willingness to pay."[16] And it would be obvious to sellers of guns that their inability to shoot (a hypothetical discussed in *Escobar* to illustrate materiality) would affect a government's willingness to pay. But, asked the court, what if the clinicians in *Escobar* were fully qualified but simply failed to provide written proof of their qualifications in the patient's chart? Or what if the hypothetical gun worked as intended and passed the required testing, but the seller discarded or misplaced a required copy of the results of the test?[17] The court did not speculate on the answers to these hypothetical questions, but observed that:

> *Escobar* indisputably requires that, before a party can employ the False Claims Act to effect a disgorgement of the entire price times three for the unqualified mental health services or for the hypothetical defective gun, the relator must prove (1) that, if informed that the proof of licensure was not attached to the file or if the

9 *Id.*
10 *Id.*
11 *Id.* at 10-12.
12 *Id.* at 3.
13 *Id.* at 8.
14 *Id.*
15 *Id.* at 9.
16 *Id.* at 11.
17 *Id.* at 11-12.

> certificate of test firing was not retained, the government would have chosen the remedy of a refusal to pay and (2) that the vendor knew or reasonably should have known the government would refuse entirely to pay but, nonetheless, remained silent, invoiced the government, and accepted the money.[18]

The court noted that a relator's proof on materiality would likely need to account for, and rule out, the possibility of the governments utilizing available remedies less drastic than a full forfeiture (times three) of amounts paid. And that accounting would require consideration of the full circumstances at the time the regulatory non-compliance is discovered, including the negative effects to the government's interest in seeking such a drastic remedy. The court noted that the question was not a hypothetical one of whether a government *might*, if confronted with one or a few instances of missing care plans, opt not to pay, but rather the real and practical question whether the governments *would*, in the circumstances actually alleged (*i.e.*, a dispute about the adequacy of care plans going back years), refuse to pay all of those claims.

The court noted that the jury verdict could not stand because jury could offer no more than a "wild guess" on this issue. And the court cast doubt on this wild guess, offering its own prediction "that under these circumstances no government answerable to the people would refuse to pay, especially in Florida and especially in the pertinent patient population, unless every other administrative and other remedy was exhausted and until an alternative provider was identified and prepared to capably serve the same patients without interruption."[19] Thus, explained the court, the longer a government allows any non-compliance (known or unknown) to continue and the more important and scarce the services provided by the defendant, the less likely it becomes that a government answerable to the people would impose FCA liability rather than a lesser remedy, and the greater the practical impediment to proving materiality. "*Escobar* demands proof of materiality in the circumstances as they are at the time for which the proof is offered and in the place, in the industry, and in the other regnant circumstances that attend the moment for which the proof of materiality is offered."[20] It is not, as *Escobar* explains, sufficient to require the jury to guess at what a government might do in a hypothetical situation under circumstances different from those presented.

II. AGG Analysis

In echoing the Supreme Court's observation that materiality under the FCA is a "demanding" standard, the *Ruckh* decision places a strong emphasis on the rigor with which materiality must be evaluated. In doing so, the court laid out a framework for "an objective and a 'rigorous and demanding' evaluation of the evidence" for purposes of determining materiality. The court highlighted the practical circumstances that must be considered in assessing materiality, including the government's continued payment after learning of alleged deficiency. Indeed, "the government that continues to pay full fare for a product or service despite knowledge of some disputed practice, some non-compliance, or some other claimed defect, relentlessly works itself into a steadily tightening bind that at some point becomes disabling because the government (or the relator, who sues in the government's stead) must prove that . . . the government would not do exactly what history demonstrates the government in fact did."[21]

Ruckh accords with other decisions applying *Escobar* to situations where the government continued to make payments despite actual knowledge of the alleged contractual or regulatory noncompliance. Absent the kind of evidence called for in *Ruckh*, attempts to "trap, zap, or zing" a provider for alleged noncompliance with immaterial conditions should fall short of meeting *Escobar's* rigorous standard for proving materiality and scienter.

18 *Id.* at 12.
19 *Id.* at 18.
20 *Id.* at 20.
21 *Id.* at 23.

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