1-1-2003

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Publication Information
Jay E. Grenig, Are Local Governmental Entities Subject to Qui Tam Actions Under the False Claims Act?, 2002-03 Term Preview U.S. Sup. Ct. Cas. 201 (2003).

Are Local Governmental Entities Subject to *Qui Tam* Actions Under the False Claims Act?

by *Jay E. Grenig*

PREVIEW of United States Supreme Court Cases, pages 201–204.

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ISSUE

Is Cook County a "person" under the federal False Claims Act that can be sued in a *qui tam* action by a former research project director for allegedly fraudulently obtaining funds for a research project from the federal government?

FACTS

Cook County Hospital applied for and received a $5 million grant from the National Institute of Drug Abuse to study the treatment of 300 drug-dependent pregnant women. The hospital submitted an assurance of compliance to the Department of Health and Human Services, representing that it would comply with federal human-subject research regulations. The grant initially was awarded to the hospital but was transferred to Hektoen Institute for Medical Research, an affiliate of the hospital that was established to receive funds and conduct medical research.

The project was designed to provide treatment and conduct medical research. It provided treatment to drug-dependent pregnant women and studied the effect of a stepped-up battery of medical and social services on its patients, compared with a control group receiving the typical treatment available in the community.

Janet Chandler was hired as the project's director in 1993. She came to believe that the defendants were violating the terms of the grant and federal regulations. She also believed they were misrepresenting the success of the program and submitting false progress reports to the government that included information on "ghost" program participants who did not exist. She alleged that the hospital did not follow the protocol for research on human subjects and for dispensing methadone to pregnant women, did not obtain informed consent from study participants, did not obtain thorough medical or drug histories, provided substandard care, failed to

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COOK COUNTY V. UNITED STATES EX REL. CHANDLER
DOCKET NO. 01-1572

ARGUMENT DATE:
JANUARY 14, 2003
FROM: THE SEVENTH CIRCUIT

Case at a Glance

The False Claims Act provides that either the attorney general or any private person can sue any "person" who has filed a fraudulent claim with the federal government. In this case, the Supreme Court is asked to determine whether Cook County, Illinois, is such a "person" that can be sued for treble damages in a *qui tam* action (an enforcement action brought for both a private person and the United States) for allegedly fraudulently obtaining medical research funds.

keep accurate records, and failed to randomize participants.

In 1994 Chandler informed the physicians at the hospital that she was concerned about the handling of the research project. She told the physicians that the program was violating the terms of the grant and pertinent federal regulations. Subsequently, Chandler was discharged and brought a *qui tam* action as a relator (that is, as the private person who provided the facts to support the suit) on behalf of the United States under the federal False Claims Act (31 U.S.C. § 3729 *et seq.*) to recover the research grant money allegedly obtained fraudulently by Hektoen and Cook County, Illinois. (Chandler initially sued Cook County Hospital in addition to these defendants, but the hospital was found to have no identity independent of Cook County and was dismissed from the case.)

Cook County moved to dismiss on the ground that it was not a "person" within the meaning of the False Claims Act. The district court dismissed the suit against Cook County, holding that, as a municipality, the county was immune from punitive damages under the False Claims Act. 118 F.Supp.2d 902 (N.D.Ill. 2000).

Reversing the district court, the Seventh Circuit held that Cook County was a "person" within the meaning of the False Claims Act and was not immune from punitive damages under the Act. 277 F.3d 969 (7th Cir. 2002). The Seventh Circuit explained that the legislative history of the 1986 amendments to the False Claims Act makes it likely that Congress was aware that the act might reach municipalities. Observing that the 1986 amendments protected whistleblowers from retaliation by "employers" including "public as well as private sector entities," the Seventh Circuit reasoned that, unless municipalities are subject to suit under the act, Congress would have no reason to be concerned that municipalities might retaliate against their employees for bringing False Claims Act claims. Because states are excluded from the definition of "person" within the False Claims Act, the Seventh Circuit concluded that the only public entities remaining are municipal corporations and other political subdivisions of states that are not arms or agencies of state government. The court further explained:

> Billions of dollars flow from the federal government to municipalities each year. Congress, in creating, in 1863, and then strengthening, in 1986, a comprehensive mechanism designed to remedy fraud against the federal government clearly determined that recipients of federal funds must be subject to such a deterrent. Given this legislative judgment, municipalities' common-law immunity from suit is inconsistent with Congress' purpose in adopting the FCA. Unlike § 1983, which creates a cause of action without specifying a remedy, the FCA includes a carefully crafted remedy for violations. Accordingly, despite the presumption against the imposition of punitive damages on municipalities, it is clear that Congress, in enacting the 1986 changes to the FCA, made a conscious choice to increase the recoverable damages while in no way indicating that it wished to exempt municipalities.

The Supreme Court thereafter granted Cook County's request for review of the Seventh Circuit's decision. 122 S.Ct. 2657 (2002).

Case Analysis

Originally enacted in 1863 in response to numerous fraudulent claims by government contracts, the False Claims Act imposes civil liability upon any "person" who, among other things, knowingly presents or causes to be presented to an officer or employee of the United States government a false or fraudulent claim for payment or approval.

Under the False Claims Act, a private person (the "relator") may bring a civil action known as a *qui tam* action "for the person and for the United States Government" against the alleged false claimant "in the name of the Government." (*Qui tam* is an abbreviation for a Latin phrase *qui tam pro domine nege qua pro sic ipso in hoc sequitur,* meaning "who pursues this action on our Lord the King's behalf as well as his own.") It is called a *qui tam* action because the plaintiff states that he or she sues for the government and for himself or herself. The relator receives a share of any proceedings from the action—generally between 15 percent to 25 percent if the government intervenes in the action, and from 25 percent to 30 percent if it does not.

Cook County contends that a local government is not a "person" subject to suit under the original 1863 enactment of the False Claims Act. The county says that the plain language of the 1863 act establishes that local governments are not subject to suits under the False Claims Act. In addition, it asserts that the 1986 amendments to the act made local governments absolutely immune from liability.

Chandler argues that Congress intended the term *person* in the original False Claims Act to include municipal corporations. According to Chandler, the purpose, legislative history, and text of the 1986 amendments make it "overwhelmingly unlikely" that Congress intended to eliminate the act's pre-existing coverage of municipal corporations.

In a *qui tam* action, the defendant is liable to the government for a civil penalty of not less than $5,000 and not more than $10,000, plus up to three times the amount of damages the government sustained because of the defendant's violation of the False Claims Act.

Cook County argues that local governments are absolutely immune from False Claims Act suits because Congress did not abrogate common-law governmental immunity from punitive damages in 1986 when it imposed mandatory treble damages in suits under the act. Chandler, however, argues that Congress in 1986 did not believe treble damages to be "essentially punitive in nature" and that application of the punitive-damages presumption about congressional intent is unjustified. She contends that there are essential differences between common-law punitive damages and treble damages. First, she argues that unlike common-law punitive damages in which a jury's largely unbounded discretion generally serves as the only upper limit on what can be both unpredictable and—at times—substantial damages, False Claims Act treble damages follow automatically from proof of the amount of the false claims. Second, she contends that treble damages are rationally related to the government's loss and may, in fact, undercompensate the government.

The county says that Congress's determination not to impose punitive damages on local governments is consistent with strong public policy considerations. According to the county, the United States has avenues other than the False Claims Act to recover for fraud committed by local governments. According to Chandler, however, municipal corporations, like private corporations, can avoid the potential disruption caused by *qui tam* actions by not making false claims with the federal government. She says that to deter such false claims, Congress deliberately made the consequences expensive.

SIGNIFICANCE

The False Claims Act does not define the term person. In other litigation, however, the Supreme Court has ruled that states are not "persons" subject to the False Claims Act's treble damages provisions. *Vermont Agency of Natural Resources v. United States ex rel. Stevens,* 529 U.S. 765 (2000). In that case, the Supreme Court noted that the definition of *person* has remained unchanged since the adoption of the False Claims Act in 1863, and it characterized the act's treble damages remedy as "punitive."

In *City of Newport v. Fact Concerts,* 453 U.S. 247 (1981), the Supreme Court held that a municipality was immune from punitive damages under 42 U.S.C. § 1983, the federal law that enables individuals to recover money damages for violations of their federal constitutional or statutory rights. The Court could find no evidence that Congress intended to disturb the settled common-law immunity of municipalities from punitive judgments in Section 1983 actions.

The federal circuit courts of appeals are divided on whether municipalities can be sued for treble damages in *qui tam* suits under the False Claims Act. Disagreeing with the Seventh Circuit, the Fifth and Third Circuits have held that municipalities are not subject to *qui tam* suits. *United States ex rel. Dunleavy v. Delaware County,* 282 F.3d 448 (3d Cir. 2002); *United States ex rel. Garibaldi v. Orleans Parish School Bd.,* 244 F.3d 486 (5th Cir. 2001), *cert. denied,* 122 S.Ct. 808 (2002).

There are many kinds of local governmental entities that provide such things as schools, roads, transportation, hospitals, law enforcement, and correctional institutions that could be exposed to serious liability by False Claims Act suits. The financial impact of holding that the False Claims Act is applicable to local government entities can be illustrated by the fact that Chandler's share of the proceeds from this one action, if successful, would be $4.5 million (30 percent of $15 million), not including the additional 30 percent of all fines. Critics of such suits claim that upholding the Seventh Circuit's position in this case could result in the pointless punishment of local government in the form of higher taxes or reduced public services, burdening the very taxpayers and citizens for whose supposed benefit the wrongdoer is being chastised. The Supreme Court explained this concern in *City of Newport:*

> Those who violate the laws of their country, disregard the authority of courts of justice, and wantonly inflict injuries, certainly become thereby obnoxious to vindictive damages. These, however, can never be allowed against the innocent. Those [punitive damages] which the plaintiff has recovered ... cannot, in our opinion be sanctioned by this court, as they are to be borne by widows, orphans, aged men and women and strangers, who, admitting that they must repair the injury inflicted by the Mayor on the plaintiff, cannot be bound beyond that amount, which will be sufficient for her indemnification.

453 U.S. at 677.

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On the other hand, supporters of such suits have suggested that no other remedy exists to discover and prosecute fraud and false claims by local governmental entities; no other remedy offers the protections to whistleblowers contained in the False Claims Act. The Seventh Circuit has explained this point of view:

> Unless municipalities are subject to suit under the FCA, Congress would have no reason to be concerned that municipalities might retaliate against their employees for bringing FCA claims. Given that states are excluded from the definition of "person" within the FCA, the only public entities remaining are municipal corporations and other political subdivisions of states which are not arms or agencies of state government.

United States ex rel. Chandler v. Cook County, 277 F.3d 969, 975 (7th Cir. 2002).

Overruling the Seventh Circuit would thus make it more difficult to secure full indemnity for frauds committed on the United States by nonsovereign cities, counties, and other local government entities.

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National Association of Public Hospitals and Health Systems, Contra Costa Regional Medical Center, Grady Health System, Halifax Hospital Medical Center, Grady Health System, Harborview Medical Center, Hurley Medical Center, The Health and Hospitals Corporation of Marion County, Jackson Memorial Health System, Memorial Health Care System, New York City Health and Hospitals Corporation, Parkland Health and Hospital System, Riverside County Regional Medical Center, Santa Clara Valley Health & Hospital System (Charles Luband (202) 347-0066)

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