

## **Regulatory Oversight – S01 Ep11, State of the Law: Contours of State False Claims Acts and How to Stay Out of Harm’s Way**

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### **Stephen Piegrass:**

Welcome to another episode of Regulatory Oversight, a podcast that focuses on providing expert perspective on trends that drive regulatory enforcement activity. This podcast features insights from members of the firm's regulatory investigation strategy and enforcement practice group, including its nationally ranked state attorney general practice, as well as guest commentary from business leaders, regulatory experts, and current and former government officials. We cover a wide range of topics affecting businesses operating in highly regulated areas. Before we get started today, I want to remind all of our listeners to visit and subscribe to our blog at [regulatoryoversight.com](https://regulatoryoversight.com) so you can stay up to date on developments and changes in the regulatory landscape.

Today, I'm joined by my colleagues Amy Williams from our Regulatory Investigations Group, and Asher Funk from our Health Sciences group to discuss the similarities and differences between federal and state false claims acts. We'll also dive into recent examples of conduct that states are pursuing, and discuss what companies can proactively do to avoid being on the receiving end of enforcement investigation activities by state AGs under their False Claims Act authority. Amy and Asher, thank you both for joining us today.

### **Amy Williams:**

Thanks, Stephen.

### **Asher Funk:**

Thanks, Stephen.

### **Stephen Piegrass:**

Why don't we start off by giving our audience an overview. Could you speak a little bit to the question of what are State False Claims Act? What kinds of conduct do they address and what kind of relief is available through those acts?

### **Asher Funk:**

State false claims acts, they're effectively anti-fraud laws and they're predominantly focused on state contractors or healthcare providers with the goal of protecting the treasury and the financial resources of states. They typically will address conduct that relates to submitting false or fraudulent claims or requesting payment from states or state funds that could be viewed as fraudulent. And we'll talk about this a bit more, but there's some expansive construction of those laws that states are using at different industries. I think Amy will talk about that a bit more. About 41 states have some kind of a false claims act. Most of those laws target healthcare fraud through the Medicaid programs and states. And about 30 of them have more broad-based state false claims acts that will cover a wider swath of conduct. Now,

these state false claims acts, Stephen, they typically model the Federal False Claims Act, which is a very old law, dates back to the Civil War, but there's some interesting nuances in wrinkles that we'll get into.

The thing that's important about state false claims acts just like this Federal False Claims Act, is that a party who violates those laws can be responsible for up to three times the amount of any actual damages. Plus there are per claim penalties that can be substantial up to almost \$23,000 per violation. And there's other levers that come in like attorney's fees and costs that a defendant might be responsible for paying. So there's a pretty big hammer that comes with these state false claims acts. And then the last thing to also keep in mind is if a party does violate a state false claims act, there's collateral implications you have to think about. In the Medicaid context, a company could have their provider agreement terminated. If they're a contractor, then maybe barred from future work with state government or receive state funds. So it's not just limited to the action that a provider has to address or potentially resolve, but there's broader consequences to think about.

**Stephen Piegrass:**

Thanks, Asher. That's very interesting. Amy, maybe you could speak a little bit more to the distinction between the state and federal False Claims Act. And I think the history is very interesting. As Asher mentioned, it sounds like the federal act has been in place for many, many years dating back to the Civil War. Maybe you could talk a little bit more about that as well.

**Amy Williams:**

That's right. The federal statute has been in place since the Civil War, but it has expanded in its scope and its application, particularly over even going back the last 30 years or so. And even more recently, Congress has acted to in its view, strengthened the statute and make it broader in its application and eliminate even some defenses that targets of these investigations have traditionally relied upon. And states have gone along with that. One reason that the number of state statutes are modeled closely after the federal statute, particularly in the healthcare context, is that it can actually help states recover more their healthcare dollars from the federal government. But you know something I wanted to point out, if you're not daily involved in these state false claims act statutes is areas where they can be broader than the federal statute.

For example, in New York and Washington DC are good examples of this. Tax fraud can actually be the subject of a False Claims Act case, whereas tax issues are expressly excluded from the federal statute. And there are other state by state, I'll call them quirky provisions. For example, in Commonwealth of Virginia, there's a False Claims Act provision that targets illegal gambling devices and sets out special penalties in the False Claims Act context if you're operating in the legal gambling device and it has any impact. To Asher's point on the Commonwealth's Treasury, a more broadly applicable exception that I would mention. In California, they have a provision that targets third party beneficiaries. If you are an affiliate or involved with a company, for example, who receives an overpayment from the state of California and it doesn't get returned, there are circumstances under which if the AGs office determines that you were a third party beneficiary of that overpayment, even if you didn't have any involvement in getting it to begin with, if you're not diligent about returning the money, you can be on the hook to the state.

And then I guess the other area that I'll mention is that this isn't just state interactions or state governments. There are a number of states, most notably Massachusetts, where the state AGs office can also pursue allegations of fraud directed at local political subdivisions, the state university system,

for example, or even state run hospitals, aside from the normal healthcare coverage there. And New York and California have similar provisions where there's a shared responsibility between state enforcement officials and local enforcement officials. But nonetheless, if you have a contract with a city or a county, you might be facing False Claims Act exposure.

**Asher Funk:**

Amy, something that really changes the game a bit in California and Illinois, those two jurisdictions also have specific state false claims acts that allow private whistleblowers to bring actions for fraud that is targeted at private insurance companies. So even when government funds are not at issue, in those two jurisdictions, it incentivizes and creates a cause of action to pursue potential fraud against insurers, which is another conversation, an another avenue to think about as a corporation is concerned.

**Amy Williams:**

It certainly expands your areas of concern as a company in terms of trying to think about your compliance. And it might be a good time to just mention or remind everyone of the role of whistleblowers or relators. Most of these state statutes, not all of them, but most of them, like the federal statute, allow private, they're called relators, but they're essentially whistleblowers to bring lawsuits. And they bring those lawsuits in secret under seal, and they're not disclosed to the defendant until after the government has had a chance to investigate. So oftentimes, there can be litigation and investigations going on in the background, and a target is not going to be aware of those until the government, and ultimately the court, allows the case to actually be unsealed and made public.

**Stephen Piegrass:**

Thanks for all that insight. I had to chuckle when you brought up the Virginia law, Amy, I've actually handled several cases involving the skill games in Virginia, which were made legal for a very short period of time, and I think there's like ongoing court action as to their legality even today. But that was one of those things where the Commonwealth found it could bring in a great deal of income very rapidly during COVID by requiring large payments from the company's operating those in order to have the right to do so in the Commonwealth. Still being debated today, but interesting that there was a False Claims Act component to that as well.

Asher, I know you've discussed how at least historically the Federal False Claims Act has been used in large part as an adjunct to federal settlements that involve fraud on Medicaid programs. And state false claims acts have paralleled those actions, at least historically. Is that changing today? And if so, how?

**Asher Funk:**

Yeah, I think we are seeing somewhat of a shift. The premise of the Feds leading the charge in many of these investigations related to multi-state Medicaid fraud or larger potential actions or whistleblower cases. There's still some continuation of that trend. But it does seem that states are realizing their power now and that in particular, they don't need the feds. They can pursue cases on their own. In one of the ways that we do see that come up oftentimes is individual states or attorney general's offices coordinating among themselves or coordination through national AG groups, like Namfuku is a good example of that, which is a consortium of all the Medicaid fraud control units in different attorney general's offices. So I think there are alternatives, alignment of states that are occurring to help pursue and bring these cases. And to Amy's earlier point, at least in the Medicaid context, states that have a

DRA compliant False Claims Act, which allows them to get more of their Medicaid dollars back, I think they're incentivized to pursue those cases.

And also too, we're seeing a difference in alignment, priorities of politics. Because what's important to the feds is not necessarily going to be as important or resonate the same way at the state level. There might be a fraud that's happened that involves a state that is deeply important to an attorney general or to their constituents that they want to pursue. And the feds, they look at it and it just doesn't register the same way. So I think the ability to target specific conduct that is important to different attorney general's offices or to the states is helping to drive a certain level of enforcement that we haven't historically seen in these cases. And I think too, success breeds success, or more actions.

And as you see states pursuing on their own in recovering large dollar cases, sometimes they're replicated. There might be a settlement in one state with an A'S office, and then there's a cascade to those settlements. I think it does embolden the AGs offices to pursue those cases. And also just familiarity and track record. The Federal False Claims Act is a very old law. Some of these state acts are far newer, and it takes time for elected officials to get comfortable with using those tools to pursue action. So I think we're seeing more and more of that, which is creating an uptick in investigations and actions and fundamentally to its settlements.

**Stephen Piepgrass:**

That all makes sense. I guess if you're an entity and you receive state funds in any way, state or municipal funds, this is an area you need to be very aware of.

**Asher Funk:**

Yeah, absolutely. I think knowing where you are, what the enforcement climate is, what the priorities are for that AGs office is really an important thing to be aware of, and that's a hard thing to do to have that temperature. But it also places a premium on your compliance programs, and it's something I think we'll talk about a bit more on how to be proactive to avoid ending up in more of a defensive posture. The other thing I'd say too, from a state perspective that I think is happening here, litigation's trickier when you're not in federal court. Or some people would look at it for the more ivory tower spots. I've had most of my career spent litigating cases in federal district courts and federal courts of appeal, but I've been in state courts and almost universally the ability, if you're a defendant, to get a case kicked out on a dispositive motion or even at summary judgment, those judges are just far more reluctant to do it because there's this more local intertwined nature of those cases.

So I think it makes it harder for defense, and I think the AG's offices' know that, and it plays into the chess match that happens when the investigator pursue actions.

**Stephen Piepgrass:**

Yeah, but I know in our experience too, sometimes you end up with state court judges that are very deferential to the AGs office. They see those attorneys all the time, they're representing the state, and there's a certain level of gravitas that comes along with it and deference making it difficult sometimes when those are the courts that you're in.

**Amy Williams:**

We had the same thought at the same time, Stephen, not unusual, but I was going to say the same thing. When you're litigating these issues, you're not going up against just any other lawyer. You're going up against a lawyer in the state AGs office with all of, as you said, gravitas, all of the authority that comes with that. And I would also, building on that, I think one of the reasons that we're seeing an uptick in these kinds of cases generally is that it's always good for the AGs office. It generates great opportunities to reach out to the public, great opportunities for press. If the AGs office can go out to the public and say, "Look, I just brought in \$10 million. I just brought in a \$100 million of what otherwise would've been lost to taxpayer money."

Frankly, I mean, we've seen a lot in the press of late around red states and blue states. When it comes to the False Claims Acts, there were only green states because every AGs office, regardless of where you otherwise stand on issues, is going to be in favor of bringing money back into the government that they can allege, at least shouldn't have gone out to begin with or was fraudulently obtained by a group of defendants. So I think that's why we're seeing a general uptick, including beyond the healthcare context.

**Stephen Piegrass:**

And speaking of that uptick, Amy, what are some of the other contexts where recently we have seen states bringing False Claims Act, claims or investigations?

**Amy Williams:**

Some of the newer twists on really old scenes, I'll talk about two in particular. One is going after a different kind of target and namely private equity investors. This has happened a lot in the healthcare context, but we're seeing it outside of the healthcare context as well, where the state AGs office is looking beyond just the entity who might have submitted a fraudulent bill or who might have gotten overpaid on a bill. And they're taking a look at who owns this entity? Is there a private investor behind the scenes? Is that private investor involved in the management of the company? Do they have their hands dirty in any way in the eyes of the state? And if so, frankly, it's another target, it's another source of reimbursement for the state. And they're pursuing those cases, they're bringing them, and these private equity investors who might very well have thought of themselves as a completely separate entity, who's simply a silent partner, they're finding themselves having to pay out to resolve these kinds of issues.

I think the other thing that I would mention that we've seen more of late is a dual purpose behind the enforcement action. So the enforcement action might be nominally a False Claims Act claim, but underlying it is another kind of allegation, an allegation that the defendant has violated securities laws or engaged in security fraud, for example, or engaged in conduct that's perceived to be anti-consumer or false advertising. California has had a number of high profile, for example, settlements involving financial services companies where there's been an allegation that you caused our teacher pension fund or our public employee fund to invest in vehicles that turned out to be the wrong investments for a pension fund. One of those arose in the mortgage back securities context, and it really came from the 2008 financial crisis in complaints over mortgages that shouldn't have been made. But the AGs office used a fairly creative use of the False Claims Act to gain a really large settlement there for the pension fund.

**Asher Funk:**

And Amy, on the private equity front, I think it's worth just saying it again. The broad scope of these False Claims Acts at the state level, just like at the federal level, they have liability for entities or individuals, not only who submit, but who cause the submission of false claims. And I think this idea of, well, it's a separate corporate entity, we observe corporate formalities, there's independence. It's really not necessarily a defense because, yeah, the state AGs want to go off to where they perceive there to be financial resources, and they're going to demonstrate even through potentially innocent conduct, like reporting of financials or other information from a portfolio company up to private equity, they're going to use that as a hook or a vehicle to try and pursue those entities. So I think it's an important avenue that we've tried to educate our clients about and also just to think through about the relationships more broadly between the sponsors and the portfolio companies.

**Stephen Piepgrass:**

Great point. We have definitely raised the specter of an act that's got some serious teeth to it and acts across the country that do. And I know a lot of our listeners are wondering, what in the world can we do to avoid those teeth clamping down on us? Asher, can you speak to what businesses should be thinking about, how they can be proactively addressing things to avoid False Claims Act claims being brought against them?

**Asher Funk:**

Absolutely. It's perhaps a mix of art and science even in how we counsel about these issues. I think the first thing is, to the extent you can, mindfulness about geography, what the laws look like where you operate as a business are important. If you're in a jurisdiction that only has a Medicaid False Claims Act, but you're in the education or financial services side of things, then you can potentially know right out at the gates what your liability looks like or how you might be within the scope of False Claims Act. But assuming you are, I think having a meaningful compliance program, not just on paper but in practice, is something that's very important because it allows you to create policies and procedures around the receipt of government funds or on how you contract. It can speak to really important things like training and education of your employees so that they're aware as well, and they can be gatekeepers and good stewards for an organization to keep them out of trouble and to be aware of potential issues as they arise.

Now, the other side of this, because there are so many state false claims acts that have that whistleblower provision, encouraging employees to come forward when they have concerns about potential fraud or over payments or non-compliance with state contracts is really important. And even more important that an organization considers those, takes them seriously, quickly investigates them and remediates them if there is truly an issue there. The conversation I have with clients all the time is, look, it's a complex regulatory landscape out there for a lot of our clients that are in healthcare, financial services or other industries. And mistakes will be made, but there's a big difference between having to refund one X or one times whatever it is because you mess something up or there is an innocent mistake. And being on the hook for triple damages, plus per claim penalties, plus other collateral implications when there's a legitimate action that can be brought under a state false claims act.

So if you can quickly get ahead of those issues and turn off the spigots so to speak, you can really limit liability if it's out there.

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The last one I'd make about proactive measures is a pitch for ourselves here is, is advice of counsel is an incredibly important thing when it comes to False Claims Acts. There is a knowledge standard. These aren't strict liability statutes, so they have to demonstrate at the lower end some kind of willful ignorance or recklessness around compliance. And entities that will reach out to their counsel and ask the hard questions, look at difficult regulations or laws, and get advice that they follow. That's one means of offering a defense or pushback that they had the requisite intent to violate the law and that it wasn't just an innocent mistake that shouldn't trigger False Claims Act liability.

**Amy Williams:**

I can't think of a single investigation that I've been involved in which the investigating entity did not ask about compliance programs, did not seek information about what programs did you have in place to prevent a mistake or to catch mistakes and correct them? So it's a super important component of resolving these even if an investigation gets launched.

**Stephen Piegrass:**

Amy, in the last few minutes, could you speak to that a little bit? You said you've been involved in a number of those investigations representing businesses being investigated, and I know we've worked together on those as well. From your perspective, can you talk to the listeners a little bit about what do you do when you get that CID? What do you recommend?

**Amy Williams:**

To echo Asher at the risk of sounding self-serving here, the first thing that you should do is pick up the phone and call your lawyer, whoever that counsel is. Because if you are receiving a CID, you are looking potentially at the tip of the iceberg. The government could have been involved in an investigation of your business for quite some time, and you don't know about it until you get the CID. So the government is in all likelihood ahead of you in terms of at least having a view as to a particular set of issues or what might have happened. Second, experienced outside counsel can really help from the outset of the matter to help shape its trajectory. The early communications with the office involved will help shape the office's view of the target of the investigation as well as what the issues are, and sending the right messages and understanding what is the right message to send is something that really only an experienced lawyer in this space can provide.

And then just there are a number of practical things your outside counsel can do. As I mentioned, it's important to get an investigation underway that's privileged as quickly as possible so that you understand the facts that, more often than not, even if it turns out to be a series of mistakes that can be defensible, something has occurred that management perhaps is not aware of, and certainly that in-house counsel is probably not aware of. And the sooner that you find out what's been happening, the better. And then there are of course, practical measures that need to be taken, holds on document destruction, making sure you understand where documents and data are being kept learning about key information from key clients.

And the last practical point I will make is that in terms of producing documents or data to government entities, there are really important freedom of information laws, steps that you need to take to protect documents and data from just becoming public. So if you're being asked to turn over highly proprietary or confidential documents, there are things that your outside counsel can do to maximize protections

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around that information. And if you turn the documents over first, the horse might have left the barn, so to speak. It might be too late to protect those things.

**Stephen Piegrass:**

All great points, and I know we could do an entire segment just on the issue of what do you do when the CID hits, but those are really great high level responses and things I think all our listeners should be thinking about. Amy and Asher, I really want to thank you both for joining us today on the podcast. I know our listeners really enjoyed your insights and I look forward to further conversations. This has been great. I want to thank our audience as well for tuning in today. Please make sure to subscribe to the podcast through Apple Podcast, Google Play, Stitch, or whatever platform you use, and we look forward to talking with you next time. Thanks.

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