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PERSPECTIVE

Justices should stand up for FCA rules

By Demme Doufekias

The underlying facts of a False Claims Act case argued before the U.S. Supreme Court last week are the stuff of a good Hollywood blockbuster. At the center of *State Farm Fire and Casualty Co. v. U.S. ex rel. Rigsby* are two sisters, Cori and Kerri Rigsby, who worked as claims adjusters for a company hired by State Farm to inspect properties damaged by Hurricane Katrina. In February 2006, the sisters met with a Mississippi lawyer, Richard "Dickie" Scruggs, providing him with documents stolen from State Farm's claims files that they believed showed State Farm had improperly characterized Katrina- related damage as the result of flood waters (covered by federal flood policies) instead of wind (covered by State Farm policies). After handing the documents over, the sisters promptly quit their jobs and took positions as "consultants" with Scruggs, who paid them $150,000 a year apparently to do very little, including showing up for work.

In the meantime, Scruggs used the documents to file a lawsuit under the False Claims Act, a federal law that allows private individuals, known as relators, to file lawsuits in the government's name when they believe the government has been the subject of fraud. The False Claims Act requires that the lawsuit be kept under seal for a minimum of 60 days, primarily to allow the federal government to investigate the claims and decide if they want to intervene in the lawsuit, and also to protect the government's interests in any ongoing criminal investigation of the wrongdoing. Scruggs filed suit in federal court, alleging that State Farm had defrauded the federal government by causing it to pay flood claims that State Farm should have paid as wind damage under its own policies. The government investigated the claims, and ultimately chose not to intervene in the lawsuit.

In the meantime, while the seal was in place, Scruggs provided copies of the evidentiary disclosures supporting the complaint and other information to multiple media outlets, including ABC News, the New York Times, and the Associated Press. Scruggs and the Rigsbys also discussed the suit with a Mississippi congressman, who held a news conference and claimed that State Farm had defrauded taxpayers by violating the False Claims Act. The congressman also provided written testimony about Scruggs' representation of the sisters in the lawsuit to a congressional subcommittee. Finally, Scruggs disclosed the existence of the lawsuit to a PR firm he had hired to assist him and the sisters in their media campaign.

The case ultimately went to trial on a single claim, resulting in a jury verdict against State Farm. Both before and after trial, State Farm argued that Scruggs' and the Rigsbys' disclosures to media outlets and others constituted a violation of the False Claims Act's seal requirement, for which the appropriate remedy was dismissing the whole case.

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The district court and the Court of Appeals court disagreed. In the first instance, the False Claims Act, although requiring that the complaint be filed and kept under seal, says nothing about the appropriate remedy if the relator violates that requirement. Furthermore, after considering the various tests used by courts to address violations of the seal requirement, both the district court and the 5th U.S. Circuit Court of Appeals relied on a 9th U.S. Circuit Court of Appeals test that weighs three factors: (1) whether the government was harmed by the violation; (2) the severity of the violation; and (3) whether the relator acted willfully or in bad faith. Ultimately, both courts refused to dismiss the complaint, finding that the government had not been harmed, that the violations of the seal requirement had been perpetrated primarily by Scruggs, and that his bad faith should not be held against the Rigsbys. It is worth noting that Scruggs withdrew from the case after being indicted in a separate matter for conspiring to bribe a judge. He was subsequently disbarred and jailed.

Despite some apparent skepticism on the Supreme Court's part toward the notion that violations of the seal requirement require dismissal of the complaint, one theme that emerged during oral argument was the court's discomfort with the notion that deliberate violations of a court-ordered seal would go unpunished. Justice Stephen Breyer seemed the most concerned about the impact of a ruling affirming the lower court's holding, stating, "it is a serious thing when someone deliberately breaks a court seal and reveals the contents to the national press. Well, it's not just the [Department of Justice] that has an interest in this. It's the United States judicial system that has an interest in this." Later, Justice Breyer was even more direct: "[T]his is a court order. People don't normally take it upon themselves to decide whether to follow it or not. If you don't like it, lift it. But while it's there, follow it."

Chief Justice John Roberts similarly reacted with doubt toward the idea that the seal requirement was a burden: "I think that [the statute] honestly asks very little of [relators] when it comes to the seal requirement. Just don't disclose it."

State Farm's attorney, not surprisingly, pressed hard the point that allowing the kind of behavior at issue here to go unpunished, even if the government was not harmed, could encourage similar behavior in aggressive relators and their counsel attempting to gain strategic advantage. State Farm argued that affirming the lower courts' rulings would send the "message to every relator in the country ... and their counsel, leak away with no consequence."

It is not difficult to understand where corporate defendants such as State Farm are coming from. In the past five years, the federal government has collected over $21 billion in fines under the False Claims Act. And this represents only cases in which the DOJ intervened — typically less than 25 percent of the cases filed. That damages number is likely to grow significantly since DOJ adopted a rule this year increasing the range of civil penalties for individual False Claims Act violations from $5,500 to $11,000 per claim to between $10,781 and $21,563 per claim. And, keep in mind, those penalties are trebled under the statute.

The idea that a relator could selectively leak evidentiary disclosures or other information related to the complaint without fear of repercussions is a powerful concern for False Claims Act defendants, particularly if the Supreme Court affirms the focus on actual harm to the government, an elusive requirement, especially in cases where the government declines to intervene. State Farm's lawyers were able to find only one case in the last 30 years in which the government took the position that a seal violation had caused actual harm. Even the United States, arguing as an amicus on behalf of the relators, agreed that when Congress adopted the seal requirement, "the Senate expected that there would not be many instances where a seal violation would harm the government." It seems apparent, then, that the most important factor under the test used by the 5th Circuit in *State Farm* is nearly impossible to meet.

The only way the seal requirement retains any meaning in the False Claims Act's statutory framework is if the Supreme Court endorses the view that a showing of actual harm to the government is not necessary to fashion a remedy for violations of the seal requirement, including dismissal of the complaint. Even as the United States argued against mandatory dismissal, it conceded, both in its brief and at oral argument that "the Court could have dismissed this case here," although there was no showing of actual harm to the government. The solicitor general endorsed this result, stating at oral argument that, "if the Court [is] worried about sending the signal that intentional violations don't matter, it could say the district court would have been perfectly within its discretion to dismiss here." These sentiments echoed positions taken by the United States in its amicus brief that "Petitioner is correct that dismissal may sometimes be an appropriate sanction even for FCA seal violations that have caused no demonstrated harm to the government." If the United States itself recognizes that actual harm need not be dispositive in light of the conduct at issue, surely the Supreme Court can see the value of coming to the same conclusion.

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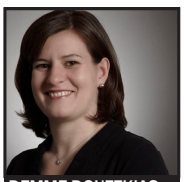
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