Set a rogue to catch a rogue

Why Canada should think before following in the United States' footsteps

by Jonathan S. Aronie, Esq.

Spurred by accounts of companies ripping off the Union Army through fraudulent sales practices, President Abraham Lincoln called upon Congress to give the federal government a vehicle to combat such rampant fraud. On March 2, 1863, it did.

The vehicle given was the civil *False Claims Act (FCA)*. And a powerful vehicle it was, providing for significant damages and penalties for the "knowing" submission of a "false claim" to the United States. What really turbo-charged the *Act*, however, was its novel "*qui tam*" provisions.

Roughly translating into "he who brings an action for the king as well as for himself," the *qui tam* provisions of the *Act* allow a private citizen to bring suit on behalf of the federal government, and to keep for him or herself a significant portion of any recovery. In the words of one of the *Act*'s key supporters, the *qui tam* provisions were founded upon the old-fashioned idea of "setting a rogue to catch a rogue."

In order to prove a violation of the *FCA*, a plaintiff must prove that the defendant submitted a "false claim" to the government (i) with actual knowledge of its falsity, (ii) with deliberate ignorance of its falsity, or (iii) with reckless disregard to its falsity. Since "reckless disregard" often can be proven without evidence of a guilty mind (under the *Act*, a company with the best of intentions still can be reckless), that avenue for proving "knowledge" quickly became a favorite among plaintiffs.

Over the years, the *FCA* has grown into the United States' primary anti-fraud statute. From 1986 to 1995, complaints filed under the *Act*'s *qui tam* provisions averaged about 127 per year. From 1995 to 2005, that number had risen to 399 per year. Financial recoveries rose similarly. By 2005, the United States had recovered more than \$15 billion under the *Act*.

The staggering growth in *FCA* suits and recoveries has been due in large part to a series of amendments passed in 1986 that increased the financial consequences of an *FCA* violation to treble damages plus penalties of up to US\$10,000 per violation. These same amendments also increased the plaintiff's recoverable share of such damages and penalties to up to 30 percent plus attorneys' fees. Needless to say, the United States has no difficulty finding willing plaintiffs (called "relators" under the *Act*).

Without question, the explosion in *FCA* litigation since 1986 has brought with it positive consequences. Companies pay more attention to compliance today than they did in the past. But the *FCA* explosion also brought about some unfortunate unintended consequences – consequences rarely reported in the press.

First, over the years, many activities that traditionally would not have been considered "fraud," have been brought within the *Act*'s reach. Questions regarding administrative contract compliance, scientific and engineering judgments, and complicated accounting decisions routinely are parleyed into *FCA* allegations by plaintiffs and their lawyers. This seemingly insatiable appetite of the *FCA* to swallow up all manner of issues, and the equally insatiable appetite of plaintiffs to second-guess the decisions and judgments made in real time by business leaders, accountants, and engineers, has drastically increased the risk, and therefore the cost, of doing business with the United States.

Second, the *FCA* has become a crowbar used by plaintiffs and the government to extract large settlements from companies, even in cases where an objective person would see no evidence of fraud. Threat of suit under the *Act* – not to mention the collateral consequences of such a suit, for example, the risk of a suspension or debarment – is routinely used by the United States Department of Justice to "encourage" companies to settle.

Third, the potential for massive damages coupled with (i) the *Act*'s relaxed state-of-mind requirements and (ii) the breadth of activities that can support an *FCA* allegation is having a chilling effect upon businesses' willingness to push the technology envelope. Companies are reconsidering whether they should continue to take the sort of technological risks that have made western industry great over the years in a litigious environment where a good-faith judgment proven wrong in hindsight can form the basis of an *FCA* allegation by a Monday-morning-quarterbacking plaintiff.

Fourth, and only one step away from number 3, is that the expansive application of the *FCA* is prompting some companies to stay away from government contracting altogether, or to offer the government only limited products and services. Consequently, the United States government is not always able to obtain the cutting-edge technology or the best and brightest minds that industry has to offer.

Of course, all this is not to say that the US should abandon its *FCA* – or to suggest that Canada should not adopt an *FCA* of its own. Without question, the *FCA* has had some positive impact in the US. The massive recoveries under the *FCA* certainly suggest that the *Act* has helped to identify and penalize fraudulent behavior. But one would be remiss to ignore the *Act*'s very real negative collateral consequences. As in most things, a balanced approach is what is needed. While the United States *FCA* may have started out that way, over the years it has morphed into something wholly different.

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