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## With Actual Knowledge Comes Lack of Materiality: Offering a Reasonable Bright-Line Rule for the Escobar Materiality Standard

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## COMMENT

### WITH ACTUAL KNOWLEDGE COMES LACK OF MATERIALITY: OFFERING A REASONABLE BRIGHT-LINE RULE FOR THE *ESCOBAR* MATERIALITY STANDARD

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## I. INTRODUCTION

The False Claims Act (FCA) is arguably one of the federal government's most powerful weapons to fight against fraudulent government contractors.<sup>1</sup> The Act operates as a deterrent of mass destruction to prevent third-party government contractors from submitting false or fraudulent claims for payment to the federal government.<sup>2</sup> Virtually any transaction between a private business and the federal government falls under the purview of the FCA.<sup>3</sup> To put it another way, it is of the utmost importance that any company doing business with the United States government

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1. See Craig Margolis & Christina Ferma, *The False Claims Act: Why Should A Civil Statute Matter to Criminal Lawyers?*, 31 CRIM. JUST. 26, 26–27 (2017) (“Penalties for violating the FCA are severe.”); see also *Justice Department Recovers Over \$3.7 Billion From False Claims Act in Fiscal Year 2017*, U.S. DEPT OF JUST. (2017), <https://www.justice.gov/opa/pr/justice-department-recovers-over-37-billion-false-claims-act-cases-fiscal-year-2017> [<https://perma.cc/C5JE-U3LJ>] (“[T]he False Claims Act serves as the government’s primary civil remedy to redress false for government funds . . . .”); see also S. REP. NO. 99-345, at 4 (1986), as reprinted in 1986 U.S.C.C.A.N. 5266, 5269 (claiming the FCA is a “powerful tool in deterring fraud”).

2. See Margolis, *supra* note 1, at 26 (“The FCA prohibits companies and individuals from submitting false or fraudulent claims for payment to the government.”); see also S. REP. NO. 99-345, at 4 (1986), as reprinted in 1986 U.S.C.C.A.N. 5266, 5269 (describing the FCA’s strength in deterring fraud).

3. False Claims Act, 31 U.S.C. § 3729 (2009).

understands the FCA in order to shield itself from liability.<sup>4</sup>

The FCA painstakingly lays out seven detailed elements which create liability under the act.<sup>5</sup> Thankfully, however, federal courts have consistently summed up the FCA as requiring three basic elements to establish liability.<sup>6</sup> First, a contractor must knowingly act fraudulently; second, the contractor then must subsequently present to the federal government a claim for payment; and, lastly, the claim must be fraudulent and material to the government's decision.<sup>7</sup> However, Congress did not intend the FCA to be a device used to punish a contractor for immaterial misrepresentations.<sup>8</sup>

On one hand, proponents of the FCA claim the Act is the best weapon the government has at its disposal to battle fraud.<sup>9</sup> On the other hand, critics posit that the FCA is too powerful and is used at times to police mere contractual disputes.<sup>10</sup> Interestingly, the Supreme Court noted the FCA was not intended as an "all-purpose" statute to prosecute simple contractual issues.<sup>11</sup>

Because the FCA is the federal government's primary deterrent against contractor fraud, it should not come as a shock to learn that between 2014 and 2018, the government brought 630 new lawsuits under the FCA—around two new FCA suits per week.<sup>12</sup> In the 2018 fiscal year alone, the

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4. See Angela Bergman, *No Consensus on Materiality: Courts Continue to Grapple With Escobar's Key Holdings*, INSIDE THE FCA (Nov. 9, 2018), <https://www.insidethefca.com/no-consensus-on-materiality-courts-continue-to-grapple-with-escobars-key-holdings/> [<https://perma.cc/FR4V-5JLY>] (noting how *Escobar's* materiality standard creates a need for government contractors need to remain vigilant of anything that could create incur liability for them under the FCA).

5. False Claims Act, 31 U.S.C. § 3729(a)(1)(A)–(G) (2009).

6. See Patricia Meador & Elizabeth S. Warren, *The False Claims Act: A Civil War Relic Evolves into A Modern Weapon*, 65 TENN. L. REV. 455, 462 (1998) (providing three basic elements that trigger liability under the FCA).

7. See *United States ex rel. Thompson v. Columbia/HCA Healthcare Corp.*, 938 F. Supp. 399, 402 (S.D. Tex. 1996) (summarizing the elements that trigger liability under the FCA); see also *id.* (listing the three basic elements of FCA liability as interpreted by most courts).

8. See Natasha Boyadzieva, *The False Claims Act and the Escobar Decision: What is on the Horizon for the Healthcare Industry*, 16 IND. HEALTH L. REV. 1, 3 (2018) (discussing the FCA's limitations).

9. S. REP. NO. 99-345, at 4 (1986), as reprinted in 1986 U.S.C.C.A.N. 5266, 5269.

10. See Jerad Whitt, Comment, *I'm Not Calling You a Liar . . . : Implied Certification Theory Under the False Claims Act*, 85 U. CIN. L. REV. 451, 451 (2017) (noting critics of the FCA worry the act will be used to "punish run-of-the-mill breaches of contract").

11. *Allison Engine Co., Inc. v. United States ex rel. Sanders*, 553 U.S. 662, 672 (2008).

12. See Jessica Sanderson & Michael Volkov, *False Claims Act 2018 Year in Review—Making Sense of the DOJ Fraud Statistics*, JD SUPRA (Jan. 21, 2019), <https://www.jdsupra.com/legalnews/false-claims-act-2018-year-in-review-62368/> [<https://perma.cc/8Z5S-6GN6>] (explaining how often the federal government brought new cases under the FCA in 2018).

federal government recovered over \$2.8 billion from suits brought under the FCA.<sup>13</sup> In fact, the federal government earned more than \$2 billion each year over the past nine years from FCA lawsuits.<sup>14</sup>

Furthermore, the FCA allows relators—colloquially known as “whistleblowers”<sup>15</sup>—to bring suits against allegedly fraudulent government contractors on behalf of the federal government,<sup>16</sup> and these relators can continue a suit under the FCA even if the federal government elects not to intervene.<sup>17</sup> And, if the suit is successful, relators are entitled to a percentage of the judgment or settlement under the FCA.<sup>18</sup> Due to this financial incentive, whistleblowers earned over \$7 billion between 1987 and 2018 from suits brought under the FCA.<sup>19</sup>

The FCA is an important statute because it protects the federal government from being defrauded by third parties.<sup>20</sup> However, the FCA is ambiguous on certain issues, and various circuit courts have not interpreted these ambiguous issues consistently.<sup>21</sup> Thus, the FCA has caused confusion among the federal circuit courts over the years.<sup>22</sup> In 2016, the Supreme Court resolved a significant point of confusion with its decision in *Universal Health Services, Inc. v. United States ex rel. Escobar (Escobar II)*,<sup>23</sup> validating and

13. U.S. DEP'T OF JUST., FRAUD STATISTICS—OVERVIEW, [https://www.justice.gov/civil/page/file/1080696/download?utm\\_medium=email&utm\\_source=govdelivery](https://www.justice.gov/civil/page/file/1080696/download?utm_medium=email&utm_source=govdelivery) [https://perma.cc/9YZL-SWC8].

14. See Sanderson & Volkov, *supra* note 12 (summarizing and graphing the number of, and the amount recovered from, FCA cases from 1987 to 2017); see also U.S. DEP'T OF JUST., *supra* note 13 (analyzing the settlement and judgment awards gained under the FCA by fiscal year).

15. See *Protect the False Claims Act*, NAT'L WHISTLEBLOWER CTR. (Oct. 28, 2019 1:38 PM), <https://www.whistleblowers.org/protect-the-false-claims-act/> [https://perma.cc/9WNB-4WR4] (discussing the *qui tam* provision, also known as the “whistleblower provision,” of the FCA). For the purpose of this Comment, the term “relator” and “whistleblower” will be used interchangeably.

16. 31 U.S.C. § 3729–30 (2009–2010).

17. *Id.* at § 3730(c)(3).

18. *Id.* at § 3730(d).

19. U.S. DEP'T OF JUST., FRAUD STATISTICS - OVERVIEW, *supra* note 13.

20. See Deborah R. Farringer, *From Gums That Do Not Shoot to Foreign Staplers: Has the Supreme Court's Materiality Standard Under Escobar Provided Clarity for the Health Care Industry About Fraud Under the False Claims Act?*, 83 BROOK. L. REV. 1227, 1233–34 (2018) (noting the intention of the False Claims Act).

21. See *id.* at 1234 (explaining how the varying state laws and regulations created differing circuit interpretations of the FCA).

22. See *id.* (noting how the varying state laws and regulations created differing circuit interpretations of the FCA).

23. See generally *Universal Health Servs., Inc. v. United States ex rel. Escobar*, 136 S. Ct. 1989 (2016) (holding under certain circumstances, cases may be brought using implied certification theory under the FCA).

allowing for claims to be made under the FCA using the implied false certification theory.<sup>24</sup>

Under the implied false certification theory, the government or a whistleblower may bring a claim under the FCA in instances where a contractor does not disclose violations of statutory or contractual obligations materially linked to the government's decision to pay the contractor.<sup>25</sup> Circuit courts varied for years about whether the implied false certification theory was a valid method to bring forth a claim under the FCA.<sup>26</sup> Yet, despite the Court clearing up the confusion surrounding the implied false certification theory of the FCA, the *Escobar* decision created even more confusion among the circuits regarding the issue of materiality.<sup>27</sup>

In *Escobar*, the Court described the FCA's materiality standard as demanding and emphasized how not all contractual terms of an agreement are material to the federal government's decision to pay a contractor.<sup>28</sup> The Court further placed a check on the FCA, stating that when a government agency has actual knowledge of a contractor's noncompliance and yet continues to pay or pays the contractor in full, said payment is strong evidence that the contractor's noncompliance was immaterial to the government's decision to make a payment.<sup>29</sup> The Court's opinion in *Escobar* seemingly posits that if the federal government has actual knowledge of a contractor's noncompliance and still pays the contractor, then the noncompliance was not at all material in the government's decision to pay.<sup>30</sup> But, in the years since the *Escobar* decision, the issue of a government agency's continued payment or payment in full despite the agency's actual

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24. *Id.* at 1999.

25. *Id.* at 1995.

26. See Joan H. Krause, *Reflections on Certification, Interpretation, and the Quest for Fraud That "Counts" Under the False Claims Act*, 2017 U. ILL. L. REV. 1811, 1820–21 (2017) (explaining the circuit split regarding interpretation of the implied false certification theory under the FCA).

27. See Vince Farhat et al., *Emerging Trends in False Claims Act Enforcement: 2018 Outlook*, JD SUPRA (Feb. 12, 2018), <https://www.jdsupra.com/legalnews/emerging-trends-in-false-claims-act-88123/> [<https://perma.cc/T3AM-GE7H>] ("Federal appellate courts have begun to interpret the *Escobar* materiality standard in varying ways.").

28. *Escobar*, 136 S. Ct. at 2003. Although the materiality standard originated in *Escobar II*, this Comment will refer to the standard as the "*Escobar* materiality standard" for simplicity. Additionally, the *Escobar II* decision will frequently be referred to as *Escobar* in the body of the text.

29. *Id.* at 2003–04.

30. See generally *id.* at 2003–04 (stating the government's actual knowledge of noncompliance on a contract and the government's continued payment of the contract provide strong evidence that the noncompliance was immaterial to the government's decision to pay).

knowledge of a contractor's compliance created a split between the Fifth and Ninth Circuits,<sup>31</sup> and much confusion among the others.<sup>32</sup>

Since *Escobar*, the issue regarding the materiality of an FCA claim not only caused confusion among the federal circuit courts, but also among the companies who regularly contract with the federal government.<sup>33</sup> Simply put, these companies want some bright-line rules for the FCA.<sup>34</sup> However, despite the call from the business community for a consistent standard, and a circuit split regarding materiality, the Supreme Court continually declines to clarify the materiality standard it proffered in *Escobar*.<sup>35</sup> A bright-line rule regarding the FCA's materiality standard is necessary.<sup>36</sup> The existing confusion surrounding the issue for private businesses and the high amount of confusion among the federal circuit courts are evidence of this necessity.<sup>37</sup>

This Comment suggests the Fifth Circuit's position on the materiality of an FCA complaint is the appropriate bright-line rule.<sup>38</sup> Specifically, this Comment suggests that when the government has actual knowledge of a contractor's noncompliance and, despite this knowledge, continues to pay or pays the contractor in full, the FCA claim against the contractor must

31. Compare *United States ex rel. Harman v. Trinity Indus. Inc.*, 872 F.3d 645, 660–63 (5th Cir. 2017) (explaining how a government agency's payment in full or continued payment creates a near insurmountable presumption that a contractor's noncompliance was not material, causing the complaint to fail for lack of materiality), with *United States ex rel. Campie v. Gilead Scis., Inc.*, 862 F.3d 890, 905 (9th Cir. 2017) (interpreting the *Escobar* materiality standard to mean that when the government has actual knowledge of a contractor's noncompliance and still pays the contractor, said payment can still be proof of the noncompliance's materiality to the government's decision to pay); see also Daniel Seiden, *Fraud Law Circuit Splits Endure as Top Court Ruling Turns 3 (I)*, BLOOMBERG LAW (June 14, 2019, 9:30 AM), <https://news.bloomberglaw.com/federal-contracting/circuit-splits-over-fraud-law-endure-as-top-court-ruling-turns-3> [<https://perma.cc/N7M4-WEBH>] (noting the *Escobar* decision created circuit splits).

32. See Bergman, *supra* note 4 (discussing the confusion among the circuit courts regarding *Escobar*'s materiality standard).

33. See Seiden, *supra* note 31 (describing the confusion felt in the business community about the FCA).

34. *Id.*

35. See *id.* (noting the Supreme Court declined to hear cases regarding the FCA's materiality standard from either the Fifth or Ninth Circuits).

36. See *id.* (examining the need for a bright-line rule).

37. See *id.* (noting the confusion felt in both the circuit courts and business community).

38. See Vince Farhat, et al., *supra* note 27 (explaining the Fifth Circuit's application of the materiality standard).

automatically fail for lack of materiality.<sup>39</sup> A bright-line rule such as this would ease the burden on the courts who adjudicate the immense number of suits brought under the FCA. More so, this rule would also ease some of the business community's confusion and concern about accruing liability under the FCA.<sup>40</sup> Furthermore, this bright-line rule would force the federal government to be more mindful of how it spends taxpayer funds, and this rule would provide a reasonable check on the federal government's ability to earn billions from an extremely broad and powerful act.<sup>41</sup> Finally, this bright-line rule would end the current split between the Fifth and Ninth Circuits, providing clarity for all the circuits in the country.<sup>42</sup>

This Comment begins with a brief historical discussion of the FCA to provide background information and context. Next, this Comment discusses the *Escobar* decision and its impact on the FCA. Then, this Comment discusses the Fifth Circuit's position on a violation's immateriality to the government's payment decision when the government has actual knowledge of the contractor's violation and continues to pay the contractor regardless of this knowledge. This Comment will also discuss the positions of a few other federal circuits with similar holdings to the Fifth Circuit. This Comment will then examine the Ninth Circuit's position on the materiality of a claim under the FCA regarding the impact of the government's actual knowledge of a contractor's noncompliance and the government's payment despite this knowledge. Finally, this Comment posits the Fifth Circuit's position as an appropriate bright-line rule regarding materiality of a claim made under the FCA for the reasons stated in the previous paragraph.

## II. HISTORICAL BACKGROUND OF THE FALSE CLAIMS ACT

During the chaos and turmoil of the Civil War, Congress drafted the FCA

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39. See *Universal Health Servs., Inc. v. United States ex rel. Escobar*, 136 S. Ct. 1989, 2003–04 (2016) (describing the government's actual knowledge of noncompliance on a contract and the government's continued payment of the contract provide strong evidence that the noncompliance was immaterial to the government's decision to pay).

40. See Seiden, *supra* note 31 (noting the confusion felt in the circuit courts and business community).

41. See *id.* (validating the confusion and concerns felt by the business community).

42. See *id.* (noting the current split on the materiality standard as applied by the Fifth and Ninth Circuits).



to deter defense contractors from committing fraud.<sup>43</sup> Defense contractor fraud was incredibly rampant and bold during this time, with reports of the United States Army receiving crates of sawdust instead of the weapons needed to end the war.<sup>44</sup> Thus, in 1863, Congress passed the FCA to combat unscrupulous government contractors, and, upon President Lincoln's signature, the Act colloquially became known as "Lincoln's Law."<sup>45</sup>

The FCA remained in its original form until the 1940s with the rise of World War II.<sup>46</sup> During this time, Congress saw fit to limit the substantial power behind the Act.<sup>47</sup> When Congress amended the FCA in 1943, it placed a knowledge limitation on the Act.<sup>48</sup> This "knowledge bar" prevented relators from bringing claims under the FCA if the government agency involved in the dispute had knowledge of the alleged fraud.<sup>49</sup> The 1943 amendment culled the excessive number of FCA cases the government prosecuted until Congress decided to substantially strengthen the Act in 1986.<sup>50</sup>

In 1986, Congress—to once again battle rampant fraud by defense contractors—supercharged the FCA.<sup>51</sup> The 1986 amendment created an easier avenue for individuals to file FCA claims before a court and provided an exemption to the knowledge bar, previously implemented with the 1943

43. See James B. Helmer, Jr. & Robert Clark Neff, Jr., *War Stories: A History of the Qui Tam Provisions of the False Claims Act, the 1986 Amendments to the False Claims Act, and Their Application in the United States* *ex rel. Gravitt v. General Electric Co. Litigation*, 18 OHIO N.U. L. REV. 35, 36 (1991) (providing a history of the creation and application of the False Claims Act).

44. *Id.* at 35.

45. See Christopher L. Martin, Jr., Comment, *Reining in Lincoln's Law: A Call to Limit the Implied Certification Theory of Liability Under the False Claims Act*, 101 CAL. L. REV. 227, 236–37 (2013) (discussing how "Lincoln's Law" came into being).

46. See Christina Parel, Note, *Striving for Consistency: Implied False Certification Theory After Escobar*, 47 PUB. CONT. L.J. 461, 464 (2018) ("In 1943, Congress amended the FCA to bar qui tam actions based on information already in the government's possession.").

47. See *id.* at 464 (describing how Congress weakened the FCA during the 1940s).

48. See Cynthia A. Howell, *Rough Road Ahead for Businesses?—The Impact of the Supreme Court's Ruling in Universal Health Services, Inc. v. United States ex rel. Escobar*, 19 DUQ. BUS. L.J. 97, 99–100 (2017) (discussing the 1943 amendment to the FCA).

49. *Id.*

50. See *id.* at 100 (stating the scope of the FCA "significantly expanded" because of three amendments starting in 1986).

51. See Rachel V. Rose, *Appreciating the Impact of Universal Health Servs. Inc. v. United States ex rel. Escobar in False Claims Act Actions*, 63 FED. LAW. 42, 43 (2016) (summarizing what the 1986 amendment added to the FCA in order to strengthen the Act). See generally S. REP. NO. 99-345, at 2–3 (1986) (discussing the government's need to protect the Department of Defense from being defrauded as the reason for drafting the 1986 amendment to the FCA).

amendment. The 1986 amendment made it easier for FCA claims to be brought in court and provided an exemption to the knowledge bar, previously implemented with the 1943 amendment.<sup>52</sup> Under the 1986 amendment, if the government's knowledge of a contractor's alleged fraud came from a whistleblower, then that knowledge did not bar a suit from being brought against an allegedly fraudulent contractor.<sup>53</sup>

The 2009 and 2010 amendments further increased the power of the FCA.<sup>54</sup> These amendments, combined with the amendment of 1986, turned the FCA into one of the most overpowered statutory weapons at the federal government's disposal.<sup>55</sup> The FCA now covers virtually all transactions between the federal government and independent contractors.<sup>56</sup> More so, the Supreme Court further strengthened the FCA by validating the implied false certification theory in *Escobar*—creating yet another avenue for a company to accrue FCA liability.<sup>57</sup>

### III. THE *ESCOBAR* DECISION AND ITS IMPACT ON THE FALSE CLAIMS ACT'S MATERIALITY ELEMENT

In 2016, the Supreme Court resolved the issue of the implied false certification theory by validating the doctrine in its landmark opinion in *Escobar*.<sup>58</sup> This decision was highly important for two significant reasons. First, the *Escobar* decision ended a long-standing split among the federal circuit courts regarding the validity of implied false certification

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52. S. REP. NO. 99-345, at 4 (1986); False Claims Amendments Act, Pub. L. No. 99-562, 100 Stat. 3153 (1986); see Martin, Jr., *supra* note 45, at 237 (discussing how the 1986 amendment to the FCA expanded the Act's power).

53. Martin, Jr., *supra* note 45, at 237; S. REP. NO. 99-345, at 4 (1986).

54. Fraud Enforcement and Recovery Act of 2009, Pub. L. No. 111-21, 123 Stat. 1617 (2009); Patient Protection and Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119 (2010); see Howell, *supra* note 48, at 100 (discussing how the FCA was expanded by the 1986, 2009, and 2010 amendments).

55. See Howell, *supra* note 48, at 100 (explaining the power's granted to the FCA by the 1986, 2009, and 2010 amendments).

56. See generally *The False Claims Act: A Primer*, U.S. DEP'T OF JUST. (Apr. 22, 2011), [https://www.justice.gov/sites/default/files/civil/legacy/2011/04/22/C-FRAUDS\\_FCA\\_Primer.pdf](https://www.justice.gov/sites/default/files/civil/legacy/2011/04/22/C-FRAUDS_FCA_Primer.pdf) [<https://perma.cc/K84R-ETLP>] (stating FCA liability accrues for anyone "who knowingly submits a false claim to the government or causes another to submit a false claim to the government or knowingly makes a false record or statement to get a false claim paid by the government").

57. See *Universal Health Servs. Inc. v. United States ex rel. Escobar*, 136 S. Ct. 1989, 1999 (2016) (holding, under certain circumstances, cases may be filed using the implied certification theory under the FCA).

58. *Id.* at 1999.

theory.<sup>59</sup> Second, and the main focus of this Comment, the *Escobar* decision created even more confusion between the circuit courts regarding the issue of a claim's materiality.<sup>60</sup> This section will begin with a brief discussion of how the Supreme Court ended the circuit splits regarding the implied false certification theory. This section will then focus on how the materiality standard proffered by the *Escobar* Court impacted the circuit courts' rulings on FCA cases.

#### A. *Ending the Circuit Court's Confusion with the Escobar Decision*

Before the *Escobar* decision, federal circuits debated the validity and scope of the implied false certification theory.<sup>61</sup> This theory allows the government or a whistleblower to bring a complaint under the FCA when a contractor makes a claim for payment, but does not disclose any violations of contractual obligations or statutory regulations that are implied and material to the government's payment.<sup>62</sup> The circuit split prior to *Escobar* was not a simple cut-and-dry split between two circuits; the implied false certification theory split was between virtually all the circuits.<sup>63</sup> Some circuits recognized the theory in full, some only in part or only in certain circumstances, and one outright denied the theory's viability.<sup>64</sup> Due to widespread confusion about the implied false certification theory among the circuits, the Supreme Court granted certiorari to the *Escobar* case.<sup>65</sup>

In *Escobar*, the dispute hinged on two issues: (1) whether a claim under the FCA could be made using the implied false certification theory, and

59. Jacob J. Stephens, *Dicta Me This: Implied False Certification to Materiality Under the False Claims Act Post-Escobar*, 44 U. DAYTON L. REV. 273, 280–83 (2019) (discussing the split between the varying circuits regarding on the implied false certification theory and how the *Escobar* decision resolved the split).

60. See Bergman, *supra* note 4 (noting the circuit courts are not consistent in their rulings regarding materiality of an FCA claim since the *Escobar* decision).

61. See Latoya C. Dawkins, *Not So Fast: Proving Implied False Certification Theory Post-Escobar*, 42 SETON HALL LEGIS. J. 163, 165 (2017) (discussing in brief how the circuits were split on implied false certification theory).

62. See *Escobar*, 136 S. Ct. at 1995 (stating how the misrepresentation made by a defendant falls within the definition of “false and fraudulent” in this explained situation).

63. See Megan E. Italiano, Note, *An Implied Defense: Self-Disclosure Offers A Defense to the Expanded False Claims Liability After Universal Health Services v. Escobar*, 60 WM. & MARY L. REV. 1943, 1951–55 (2019) (noting the history of implied false certification theory and how the theory varied from circuit to circuit); see also Krause, *supra* note 26, at 1820–21 (discussing the split among the circuits about the validity and scope of the implied false certification theory of the FCA).

64. See Krause, *supra* note 26, at 1820–21 (summarizing the circuit split regarding implied false certification theory).

65. *Escobar*, 136 S. Ct. at 1998.

(2) whether FCA liability could only accrue if an express payment provision is violated.<sup>66</sup> The relators who brought the case alleged that Universal Health Services violated the FCA under the implied false certification theory.<sup>67</sup> Specifically, the relators alleged that Universal Health Services did not disclose that some of its employees lacked the proper medical training and licensing required by Medicaid when the company submitted claims for payment.<sup>68</sup>

The United States District Court for the District of Massachusetts granted summary judgment for Universal Health Services, holding none of the statutory regulations the company violated were conditions of payment.<sup>69</sup> The First Circuit Court of Appeals reversed, taking the position that statutory or contractual regulations could be either expressly stated conditions of payment or implied conditions of payment.<sup>70</sup> Upon Universal Health Services' appeal, the Supreme Court granted certiorari to end the conflict among the circuits regarding the validity of the implied false certification theory.<sup>71</sup>

The Court held a claim could be brought under the FCA, in select instances, using the implied false certification theory.<sup>72</sup> The Court also concluded not all conditions for payment are expressly stated.<sup>73</sup> There may be some implied conditions, and violating implied conditions of payment can trigger liability under the FCA.<sup>74</sup> However, the Court carefully noted that not *all* violations of even an express condition of payment can trigger FCA liability.<sup>75</sup> According to the Court, what triggered liability under the FCA was not a violation of just any old contractual provision or statutory

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66. *See id.* at 1995–96 (explaining how claims can be made under the FCA using the implied false certification theory in some circumstances, and FCA liability is not limited to circumstances where there is a violation of express conditions for payment).

67. *Id.* at 1997–98.

68. *Id.*

69. *Id.* at 1998.

70. *United States ex rel. Escobar v. Universal Health Servs.*, 780 F.3d 504, 512–13 (1st Cir. 2015).

71. *See Escobar*, 136 S. Ct. at 1998–99 (discussing the Court's reasoning for granting certiorari).

72. *See id.* at 1999 (holding implied false certification theory is a valid theory under which to bring a claim under the FCA).

73. *Id.* at 2001.

74. *See id.* (holding the FCA does not limit liability to violations of express conditions for payment only).

75. *See id.* (noting not all violations of express conditions will automatically trigger liability under the FCA).

regulation.<sup>76</sup> Rather, what triggers FCA liability is whether the violated provision or regulation was material to the government's decision to pay the contractor.<sup>77</sup>

The Court reasoned that focusing on whether or not a violated provision or regulation was material to the government's decision to pay a contractor was the most efficient and effective method to adjudicate FCA claims.<sup>78</sup> The Court wanted to prevent mass confusion among government contractors, who are desperately trying to abide by both express contractual conditions of payment and implied statutory conditions in order to avoid liability.<sup>79</sup> Furthermore, the Court wanted to avoid providing an avenue for the federal government to turn every mere contractual violation or inconsequential statutory violation into an FCA issue by labeling anything and everything as a condition of payment.<sup>80</sup> Thus, for FCA liability to be triggered, a government contractor must violate an obligation or regulation that is material to the government's decision to pay.<sup>81</sup> As Justice Thomas wrote:

If the Government failed to specify that guns it orders must actually shoot, but the defendant knows that the Government routinely rescinds contracts if the guns do not shoot, the defendant has "actual knowledge." . . . [A] defendant's failure to appreciate the materiality of that condition would amount to "deliberate ignorance" or "reckless disregard" of the "truth or falsity of the information" even if the Government did not spell this out.<sup>82</sup>

The Court's decision allowing claims to be brought under the FCA by the implied false certification theory in limited circumstances cleared up the

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76. *See id.* (stating materiality is key to determining whether a provision or regulation is a condition of payment).

77. *See id.* (determining materiality to be a key factor in determining whether a contractor actually violated the FCA).

78. *See id.* (noting a condition of payment is determined by a materiality determination).

79. *See id.* at 2002 (discussing the complicated web of contractual obligations and statutory regulations that companies must deal with in order to do business with the government).

80. *See id.* (explaining the need to avoid having the government label everything contractual obligation or statutory regulation an express condition of payment).

81. *See id.* (holding a material obligation or regulation must be violated to the decision for the government to pay).

82. *See id.* at 2001–02 (providing Justice Thomas's example of unshootable guns and the ability for the government to rescind such contracts for the knowledge that the contractor has of this material issue).

mass circuit confusion regarding the theory.<sup>83</sup> However, the Court's decision in *Escobar* would again cause as much confusion among the federal circuits as did the validity and scope of implied false certification theory.<sup>84</sup> Only this time, the confusion stemmed from the *Escobar* Court's own materiality standard.<sup>85</sup>

#### B. *The Escobar Decision's Impact on Materiality of an FCA Claim*

The Supreme Court ended one mass circuit split with its decision in *Escobar*, but created a new one regarding the issue of materiality.<sup>86</sup> In *Escobar*, the Court stated the materiality standard of the FCA was "demanding."<sup>87</sup> In the years since the Court's decision in *Escobar*, the federal circuit courts have inconsistently interpreted the Supreme Court's position on the materiality element of an FCA claim.<sup>88</sup> In particular, the Fifth and Ninth Circuits are the most at odds with one another regarding this issue.<sup>89</sup>

As previously stated, the Supreme Court determined the materiality

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83. See Tiphannie Miller, *Materiality and the False Claims Act After Escobar*, 35 DEL. LAW., Spring 2017, at 24, 25 (discussing briefly why the Supreme Court granted certiorari in *Escobar* and the Court's holding stating the implied false certification theory is valid).

84. See Bergman, *supra* note 4 (stating the circuit courts have struggled to come to a consensus on an interpretation of *Escobar*'s materiality standard); see also Seiden, *supra* note 31 (discussing how three years after the decision, the circuit courts are still divided regarding *Escobar*'s materiality standard); Roderick L. Thomas & Michelle B. Bradshaw, *False Claims Act: Escobar's Materiality Language Gets More Bite*, WILEY (Nov. 2017) <https://www.wileyrein.com/newsroom-newsletters-item-False-Claims-Act-Escobars-Materiality-Language-Gets-More-Bite.html> [<https://perma.cc/RL9C-WYZE>] (discussing how courts grapple with how to properly apply *Escobar*'s materiality standard).

85. See Mike Chow, Note, *Payment Is Not Enough: Materiality in Implied False Certifications Under the False Claims Act*, 70 HASTINGS L.J. 573, 576 (2019) (noting how the *Escobar* Court ended the circuit split regarding implied false claims theory, but created another one based on its very own holding on materiality).

86. See Bergman, *supra* note 4 (stating courts are divided in interpreting the Supreme Court's holding on materiality of a claim made under the FCA); see also Seiden, *supra* note 31 ("The high court's refusal to further detail what a valid complaint must say to sufficiently allege falsity and materiality, . . . arguably leaves two significant federal circuit splits in place on those issues.").

87. See *Universal Health Servs., Inc. v. United States ex rel. Escobar*, 136 S. Ct. 1989, 2003 (2016) ("The materiality standard is demanding.").

88. See Farringer, *supra* note 20, at 1254 (explaining how the lower courts have trouble in interpreting the materiality standard the Supreme Court set out in *Escobar*); see also Boyadzieva, *supra* note 8, at 13 (discussing how the Supreme Court in *Escobar* did not lay out a bright line rule regarding materiality of an FCA claim).

89. See Seiden, *supra* note 31 (noting the existence of a circuit split between the Fifth and Ninth Circuits surrounding the issue of materiality of FCA claims post-*Escobar*).

standard of an FCA claim to be “demanding.”<sup>90</sup> The Court laid out some guidelines to help explain just how demanding the materiality standard is.<sup>91</sup> However, these guidelines were not bright-line rules, leading to variations in circuit court interpretations. Currently, the materiality standard requires an intensive examination of the facts involved in each complaint, and no one factor is completely dispositive in the determination process.<sup>92</sup>

In *Escobar*, the Court observed that the FCA requires a contractor’s misrepresentation or fraud to be “material to the other party’s course of action.”<sup>93</sup> To make this determination, the Court—as one should—first looked to the FCA’s definition of materiality.<sup>94</sup> The statute defines materiality as “having a natural tendency to influence, or be capable of influencing, the payment or receipt of money or property.”<sup>95</sup> The Court noted this definition was rooted in common law traditions.<sup>96</sup> The Court pointed out, across various rulings, there could be no existence of fraud where the fraud was *not material* to induce a party to act.<sup>97</sup>

However, the Court declined to specifically establish whether the FCA is directly governed by § 3729(b)(4)—the statute’s actual definition of materiality—or if common law traditions govern the statute.<sup>98</sup> Today, clear direction on the materiality aspect of an FCA claim would be very beneficial for both the courts adjudicating FCA cases and businesses that regularly contract with the government.<sup>99</sup> Nevertheless, the *Escobar* Court decided in its wisdom to not establish a bright-line rule just yet. Instead, it attempted to take a middle path to the concept of materiality.<sup>100</sup> The Court reiterated

90. See *Escobar*, 136 S. Ct. at 2003 (describing the materiality standard of an FCA claim as “demanding”).

91. See *id.* at 2001–04 (discussing the materiality standard of an FCA claim).

92. See Miller, *supra* note 83, at 25 (describing the materiality standard as set down in the *Escobar* decision).

93. See *Escobar*, 136 S. Ct. at 2001 (explaining the materiality standard of an FCA claim).

94. See *id.* at 2002 (noting the definition of materiality in the FCA).

95. 31 U.S.C. § 3729(b)(4) (2018).

96. See *Escobar*, 136 S. Ct. at 2002 (citing *Neder v. United States*, 527 U.S. 1, 22 (1999)) (providing the Court preserved the common law meaning of materiality in various rulings regarding fraud and misrepresentation).

97. See *id.* (stating the Court preserved the common law meaning of materiality in various rulings regarding fraud and misrepresentation).

98. *Id.*

99. See generally Seiden, *supra* note 31 (discussing the existence of a circuit split regarding the *Escobar* materiality standard, and discussing how the business community would like some clear direction on the issue as well).

100. See *Escobar*, 136 S. Ct. at 2002 (discussing why the Court was not establishing whether common law or the FCA’s direct definition govern the materiality of an FCA claim).

that materiality is determined by the misrepresentation of a party's decision to pay and such a position on materiality was held across varying areas of law.<sup>101</sup>

The Court continued to expound its position on materiality by laying out some base guidelines for the lower courts to follow. First, the government cannot just label any "statutory, regulatory, or contractual requirement as a condition of payment."<sup>102</sup> Next, the Court stated that an FCA claim lacks materiality even if the government might have an option to not pay a contractor upon learning of an instance of noncompliance.<sup>103</sup> The Court further noted that if a contractor's noncompliance was "minor or insubstantial," then the noncompliance was also not material.<sup>104</sup> Just because the government claims something is material to its decision to pay does not mean that it is necessarily so. The Court pointed out that, though not dispositive, the government's identification of a provision as a condition of payment is highly relevant to a materiality determination.<sup>105</sup>

The Court then discussed what would be material in a claim made under the FCA. The materiality of an FCA claim, according to the Court, includes situations where a contractor knows the government never pays when a specific statute or contractual obligation is violated.<sup>106</sup> For example, a company contracts with the federal government to provide gently used, pre-owned vehicles for government agencies. The company knows the federal government never pays on these contracts when a licensed mechanic does not service the used vehicles. However, the company merely hires self-taught mechanics to work on the vehicles. When the company delivers the vehicles and requests payment from the federal government, the company's omission that non-licensed mechanics worked on the vehicles instead of licensed ones would be material in determining of liability under the FCA.

Notably, the Court did include a knowledge limitation on the government regarding the materiality of an FCA claim. In instances where the government actually knows about a contractor's noncompliance and pays

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101. See *id.* at 2002–03 (evidencing a similar position taken by both the Restatement of Contracts and the Restatement of Torts).

102. *Id.* at 2003.

103. See *id.* (discussing the Court's position on materiality).

104. *Id.*

105. See *id.* (noting the government's position that a statute or contractual regulation as a condition of payment is not automatically dispositive).

106. *Id.*



the contractor in full for their work, said knowledge provides a strong presumption that the noncompliance was not material to the government's decision to pay.<sup>107</sup> Furthermore, if the government typically pays on certain contracts despite its knowledge of noncompliance, such payment also provides a strong presumption that the noncompliance was immaterial to the government's decision to pay.<sup>108</sup>

However, the Court, continuing down its middle road position, did not provide this knowledge limitation with a very powerful bite.<sup>109</sup> This is because, although the government's decision to pay or continue to pay a contractor despite the government's knowledge of noncompliance is strong evidence that the noncompliance is immaterial, that evidence is not completely dispositive.<sup>110</sup> In other words, even though the government completely knows about a contractor's noncompliance and still pays the contractor in full—which would imply to a reasonable person that the noncompliance was immaterial—a court could still determine that the contractor's noncompliance was indeed material. Thus, a court could impose FCA liability on a company the government's knowledge about the company's noncompliance and payment to the company. This stance seems self-contradictory. However, attempting to maintain common law traditions, the Court did not directly establish any of the materiality factors set out in *Escobar* as bright-line rules.<sup>111</sup>

The Supreme Court's refusal to establish any bright-line rules regarding the issue of materiality of an FCA claim caused variances in the circuit courts' decisions on FCA cases in the three years since the *Escobar* decision.<sup>112</sup> Nearly every circuit has a different stance on the materiality of a claim made under the FCA, and thus there is no clear consensus throughout the country on what is and what is not material in an FCA

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107. See *id.* (stating the government's actual knowledge of a contractor's noncompliance and the government's decision to pay provides a presumption of the noncompliance's non-materiality).

108. *Id.* at 2003–04.

109. See *id.* (providing the government's actual knowledge of a contractor's noncompliance can show that the noncompliance was immaterial).

110. See *id.* (noting the government's actual knowledge is not completely dispositive in a materiality determination of an FCA claim).

111. See *id.* at 2002–04 (stating common law traditions do influence a materiality analysis of an FCA materiality claim, but not directly deciding whether it governs, and stating factors courts could use to analyze the materiality element).

112. See Chow, *supra* note 85, at 576 (stating the Supreme Court set the stage for new circuit splits involving materiality when it implied false certification theory).

claim.<sup>113</sup> In particular, the Fifth and the Ninth Circuits have the most comprehensive split on the issue.<sup>114</sup> So, in sum, the *Escobar* decision's impact on the issue of materiality of an FCA claim was a negative one that caused confusion between the circuit courts and for the business that regularly contracts with the government.<sup>115</sup> This confusion has led both businesses and attorneys alike to call for some bright-line rules to guide their understanding of the FCA.<sup>116</sup> To date, the Supreme Court has been deaf to these calls.<sup>117</sup>

#### IV. THE FIFTH CIRCUIT'S STRICT POSITION ON MATERIALITY AND SIMILAR STRICT POSITIONS OF OTHER CIRCUITS

Since *Escobar*, the federal circuit courts have inconsistently interpreted the Supreme Court's materiality factors of an FCA claim.<sup>118</sup> Some circuits, such as the Fifth Circuit, have strictly interpreted one facet of the Court's position on materiality, while others, such as the Ninth Circuit, interpret this facet of the Court's position more loosely.<sup>119</sup> Specifically, when it is shown that the government had actual knowledge of alleged noncompliance and continued to pay or paid the defendant in full, that evidence overwhelmingly, not just strongly, shows that noncompliance was immaterial.<sup>120</sup> The Fifth Circuit promulgated this reasonable avenue of a potential bright-line rule for materiality in FCA claims. This reasonable avenue of a potential bright-line rule for materiality in FCA claims was promulgated by the Fifth Circuit after *Escobar* was

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113. See Bergman, *supra* note 4 (discussing "there appears to be a deepening circuit split developing regarding how plaintiffs must plead and prove materiality after *Escobar*").

114. Seiden, *supra* note 31.

115. See *id.* (noting the existence of a clear circuit split between the Fifth and Ninth Circuits surrounding the issue of materiality of FCA claims post-*Escobar*).

116. See *id.* (interviewing Robert Rhoad about the current state of the FCA).

117. See *id.* (providing illustrating how the Supreme Court again rejected to hear cases regarding the FCA's materiality standard).

118. See Alex Hontos & Lauren Roso, *False Claims Act: New Developments for an Old Law*, DORSEY & WHITENY LLP (Aug. 23, 2019, 9:20 AM), <https://dorseyfca.com/false-claims-act-new-developments-for-an-old-law/> [<https://perma.cc/6SW5-9GD8>] (discussing the lack of Supreme Court guidance about the materiality of an FCA claim post-*Escobar*).

119. See Jacklyn N. DeMar, *From the Editor*, 87 FALSE CLAIMS ACT & QUI TAM Q. REV. NL 1, 1 (2017) (discussing the differing interpretations of the Supreme Court's materiality holding in *Escobar* held by the circuit courts).

120. See *id.* at 1 (explaining the Fifth Circuit's dismissal of an FCA claim when the government had actual knowledge of noncompliance and continued payment despite noncompliance).

decided.<sup>121</sup> The Fifth Circuit's position on materiality of an FCA claim's materiality is echoed by several other circuits, which in turn created a split among the circuits taking a strict position and the Ninth Circuit's more relaxed position on the materiality of an FCA claim.<sup>122</sup>

This section will first discuss the Fifth Circuit's position regarding FCA claims, where the government had actual knowledge of an alleged noncompliance and yet continued to pay or paid the contractor despite this knowledge. Specifically, this section will look at two cases from the Fifth Circuit—*Abbot v. BP Exploration & Production*,<sup>123</sup> and *United States ex rel. Harman v. Trinity Industries*,<sup>124</sup> respectively. Next, this section will discuss other federal circuit courts that have taken a similarly strict stance to the Supreme Court's materiality holding from *Escobar*.<sup>125</sup> Specifically, it will examine cases from the First, Third, and Seventh Circuits and discuss how the position of these circuits' position is similar to that of the Fifth Circuit.<sup>126</sup>

#### A. *The Fifth Circuit's Strict Position on Materiality*

Shortly after the Supreme Court's decision in *Escobar*, the Fifth Circuit was presented with two cases involving the FCA. First in *Abbott*, and then more conclusively in *Harman*, the Fifth Circuit held in favor of an allegedly fraudulent contractor when the government had actual knowledge of the contractor's noncompliance and continued to pay the contractor.<sup>127</sup> These two cases, most notably *Harman*, highlight the strict interpretation of the

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121. See *United States ex rel. Harman v. Trinity Indus. Inc.*, 872 F.3d 645, 663 (5th Cir. 2017) (drawing the lesson that “continued payment by the federal government after it learns of the alleged fraud substantially increases the burden on the relator in establishing materiality”).

122. See Bergman, *supra* note 4 (discussing the continuing circuit split stemming from *Escobar*'s materiality holding); see also Seiden, *supra* note 31 (noting the continuance of a circuit split regarding materiality three years after the *Escobar* decision).

123. *Abbott v. BP Expl. & Prod., Inc.*, 851 F.3d 384 (5th Cir. 2017).

124. *Harman*, 872 F.3d at 645.

125. Bergman, *supra* note 4.

126. *Id.*

127. See *Harman* 872 F.3d at 667–68 (holding in favor of Trinity Industries due to a lack of materiality in the whistleblower's FCA claim because the government had actual knowledge of Trinity's noncompliance and continued to use Trinity's products and pay Trinity); see also *Abbott*, 851 F.3d at 388 (holding in favor of BP because of a lack of materiality in the whistleblower's FCA claim due to the government's knowledge of BP alleged noncompliance and continued payment to BP).

FCA's demanding materiality standard.<sup>128</sup>

In *Abbott*, a whistleblower brought a case against British Petroleum (BP), claiming BP made false assertions of compliance with regulatory requirements to the United States Department of the Interior (DOI).<sup>129</sup> The whistleblower claimed BP did not possess all the government-required documentation and engineer approval for its operation of an oil production facility in the Gulf of Mexico.<sup>130</sup> The whistleblower alerted the DOI of BP's potential fraud, which prompted the DOI to investigate the allegations.<sup>131</sup> Upon completing its investigation, the DOI deemed the whistleblower's complaint to lack merit and declined to revoke BP's license to operate the oil production facility.<sup>132</sup> The United States District Court for the Southern District of Texas upheld BP's motion to dismiss after initially denying the motion pre-discovery, and the whistleblower appealed.<sup>133</sup>

The Fifth Circuit reviewed the case and focused on the materiality of the claim.<sup>134</sup> The Fifth Circuit reiterated the Supreme Court's declaration that the FCA's materiality standard is demanding.<sup>135</sup> Furthermore, case's facts drew the Fifth Circuit's attention to the *Escobar* Court's statements regarding instances when the government has actual knowledge of a contractor's

128. See *Harman*, 872 F.3d at 660–61 (noting the Supreme Court stated the materiality standard of an FCA case is demanding and to look at the government's actual knowledge and behavior in determining materiality); see also *Abbott*, 851 F.3d at 388 (noting the *Escobar* decision described the government's actual knowledge and continued payment to an allegedly fraudulent contractor as substantial evidence that the noncompliance was immaterial to the government's decision to pay).

129. See *Abbott*, 851 F.3d at 386 (“Abbott subsequently filed . . . a complaint pursuant to 31 U.S.C. § 3730(b)(2) of the False Claims Act (“FCA”) on April 21, 2009, claiming, inter alia, that BP falsely certified compliance with various regulatory requirements.”).

130. *Id.* at 386 (“During his employment, Abbott came to believe that BP did not have all of the necessary documentation for the Atlantis and that many of the Atlantis documents that BP did have were not approved by engineers as required by applicable regulations.”).

131. See *id.* (“As a result of his lawsuit, the Department of the Interior (“DOI”) began reviewing BP's compliance with those regulatory requirements in May 2009.”).

132. See *id.* (“DOI's investigation culminated in a 2011 report . . . that concluded that ‘Abbott's allegations that Atlantis operations personnel lacked access to critical, engineer-approved drawings are without merit,’ and that ‘Abbott's allegations about false submissions by BP to [DOI] are unfounded.’”).

133. See *id.* (“The district court ultimately granted summary judgment in favor of BP on all claims.”).

134. See *id.* at 387–88 (discussing the Supreme Court's holding on materiality in *Escobar*).

135. See *id.* (quoting *Universal Health Servs., Inc. v. United States ex rel. Escobar*, 136 S. Ct. 1989, 2001 (2016)).

noncompliance and continues to pay the contractor.<sup>136</sup> In this case, the DOI knew of BP's noncompliance with certain regulations.<sup>137</sup> Despite this knowledge, the DOI found no reason to suspend or terminate BP's operation of the oil production facility operation.<sup>138</sup> The Fifth Circuit rightfully observed how these facts presented strong evidence BP allegedly violated the regulations was immaterial to the government's decision to allow BP to continue operations.<sup>139</sup> Thus, the whistleblower's complaint did not meet the demanding materiality standard *Escobar* imposed, and the district court did not err in granting summary judgment for BP.<sup>140</sup>

The Fifth Circuit's ruling on the materiality issue in *Abbott*'s materiality issue seems to be a strict, textualist interpretation of the materiality standard set out in *Escobar*.<sup>141</sup> The Fifth Circuit continued to strictly interpret the Supreme Court's stance on materiality in its decision in *Harman*, when that case was brought before it several months after deciding *Abbott*.<sup>142</sup> The *Harman* decision clarified and firmly set the Fifth Circuit's position on the materiality of FCA claims when the government has actual knowledge of the alleged noncompliance and yet continues to pay despite of this

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136. See *id.* at 387–88 (noting the Supreme Court stated the government's actual knowledge of noncompliance and the government's continued payment despite of this knowledge presents a strong showing that the noncompliance was immaterial to the government's payment).

137. See *id.* at 386 (describing how the whistleblower's complaint triggered an investigation of the allegations by the DOI allegations).

138. See *id.* ("The DOI Report also 'found no grounds for suspending the operations of the Atlantis . . . or revoking BP's designation as an operator . . .'").

139. See *id.* at 388 (noting the DOI's knowledge of BP's noncompliance with certain regulations and its immateriality in the DOI's decision to allow BP to continue operations).

140. See *id.* ("The district court therefore correctly granted summary judgment on the FCA claims in favor of BP.").

141. Compare *Escobar*, 136 S. Ct. 1989, 2003 (finding it to be strong evidence that a violation was immaterial to the government's payment decision when the government continued to pay an allegedly fraudulent contractor despite having actual knowledge of the contractor's violation), with *Abbott* 851 F.3d at 387–88 (stating the DOI's knowledge of BP's noncompliance with certain regulatory statutes combined with the DOI's decision to allow BP to continue operating in the Gulf of Mexico created a substantial showing of evidence that compliance with those statutes was not material in the DOI's decision, and the whistleblower had no evidence to beat this substantial evidence).

142. See *United States ex rel. Harman v. Trinity Indus. Inc.*, 872 F.3d 645, 660–61 (5th Cir. 2017) (explaining the Supreme Court's position on the materiality of FCA claims as laid out in *Escobar*).

noncompliance.<sup>143</sup> In these instances, claims fail for lack of materiality.<sup>144</sup>

In *Harman*, a whistleblower brought an FCA claim against Trinity Industries Inc. (Trinity), a manufacturer of highway guardrails for sale and use by state governments throughout the United States.<sup>145</sup> Since the Federal Highway Administration (FHWA) reimbursed the states which purchased Trinity's guardrails, Trinity was in effect paid by the federal government and, thus, fell within the scope of the FCA.<sup>146</sup> The whistleblower, a customer and former competitor, alleged Trinity did not inform the FHWA of some changes made to the guardrails and these changes led to an increase in car accidents.<sup>147</sup> In other words, the whistleblower claimed that Trinity defrauded the federal government of funds.<sup>148</sup>

The FHWA investigated the whistleblower's allegations.<sup>149</sup> Following the investigation, the FHWA stated, despite Trinity's omission of the changes it made to the guardrails, it would continue to reimburse states which purchased these products.<sup>150</sup> Furthermore, the government declined to intervene in the case, leaving the whistleblower to continue the litigation on its behalf.<sup>151</sup> Based on the FHWA's investigation and decision to continue payment, and because the government would not prosecute the case itself, Trinity moved for summary judgment.<sup>152</sup> The district court denied this motion, as well as a writ of mandamus following a mistrial.<sup>153</sup> Interestingly, though the district court stated it was not prepared to make a ruling as a matter of law, the court did note the evidence substantially did

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143. See *id.* at 663–65 (holding the whistleblower's claim failed for lack of materiality in this case because the government knew about the alleged noncompliance and still reimbursed the contractor despite this knowledge).

144. See *United States ex rel. Patel v. Catholic Health Initiatives*, 312 F. Supp. 3d 584, 605 (S.D. Tex. 2018) (determining an FCA complaint to lack materiality when the government would have the option to decline payment when it knew of the contractor's noncompliance based on the *Escobar* materiality standard and the Fifth Circuit's ruling in *Harman*).

145. *Harman*, 872 F.3d at 649–50.

146. *Id.* at 648.

147. *Id.* at 649–50.

148. *Id.*

149. *Id.* at 650.

150. *Id.*

151. *Id.*

152. *Id.*

153. *Id.* at 650–51.

allude to immateriality of Trinity's omission.<sup>154</sup> However, the jury did not see it that way and rendered a verdict in favor of the whistleblower.<sup>155</sup>

Following the verdict, the FHWA ordered independent testing of the guardrails.<sup>156</sup> When the results of the testing the guardrails were safe, the FHWA stated it would continue to reimburse states for purchasing them.<sup>157</sup> Based upon the independent testing and the FHWA's announcement, Trinity sought post-judgment relief, but was denied by the district court.<sup>158</sup> Trinity then appealed to the Fifth Circuit seeking the post-judgment relief denied to it by the district court.<sup>159</sup>

The Fifth Circuit, however, did not grant Trinity its sought-after post-judgment relief.<sup>160</sup> Instead, it reversed the whole decision.<sup>161</sup> The Fifth Circuit interpreted the facts of the case to show that the whistleblower's claim did not meet the materiality standard set out in *Escobar*.<sup>162</sup> Specifically, the Fifth Circuit focused on the government's actual knowledge and actual behavior based on this knowledge.<sup>163</sup> In other words, because the FHWA knew about Trinity's omission of the changes made to its highway guardrails, and continued to reimburse states for purchasing the guardrails, Trinity's omission was immaterial to the FHWA's decision to pay.<sup>164</sup>

The Fifth Circuit reached its decision by not only strictly interpreting *Escobar*'s materiality standard, but also by examining similar cases from other federal circuits.<sup>165</sup> The Fifth Circuit even examined the position of the Ninth Circuit—which did not immediately find a lack of materiality in these

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154. *See id.* at 651 (referencing the district court reprimanding the parties for the mistrial and stating, “a strong argument can be made that the defendant’s actions were neither material nor were any false claims based on false certifications presented to the government”).

155. *Id.* at 651.

156. *Id.*

157. *Id.* at 651 (5th Cir. 2017).

158. *Id.* at 651–52.

159. *Id.*

160. *Id.* at 652 (“[W]e need not consider the question of post-judgment relief . . .”).

161. *See id.* at 652, 670 (finding *Trinity* to be “entitled to judgment as a matter of law on the issue of materiality,” and reversing and remanding the case in favor of *Trinity*).

162. *See id.* at 660–62 (discussing the Supreme Court’s holding on materiality of FCA claims in the *Escobar* decision).

163. *See id.* at 663–67 (examining the FHWA’s decision to continue to reimburse states for use of Trinity’s guardrails, despite the FHWA’s actual knowledge of Trinity’s omission).

164. *See id.* at 665 (“[T]he ‘very strong evidence’ here of FHWA’s continued payment remains un rebutted.”).

165. *See id.* at 661–63 (examining FCA cases involving similar situations from the First, Seventh, and Ninth Circuits).

instances—but found its sister-circuit’s interpretation to be unpersuasive.<sup>166</sup> The Fifth Circuit determined, though these circuits did not hold any one materiality factor to be dispositive, several circuits held that when the government continues to pay a contractor despite an issue of noncompliance it is very strong evidence that the noncompliance is immaterial.<sup>167</sup>

To date, the Fifth Circuit has yet to take another case involving the FCA’s materiality standard when the government has actual knowledge of a noncompliance and continues to pay the contractor.<sup>168</sup> So, as it stands, the Fifth Circuit’s position regarding materiality of an FCA claim is a showing by the defendant of the government’s actual knowledge of an alleged noncompliance and its continued payment in spite of this knowledge creates a virtually insurmountable burden for the plaintiff.<sup>169</sup> This burden is so substantial that it, in effect, defeats the materiality element of an FCA claim.<sup>170</sup>

Furthermore, this substantial burden for the plaintiff only occurs in instances when the government has actual knowledge and has made payments or paid in full.<sup>171</sup> In any other scenario, such as when the government stops payment when it gains the required knowledge or does not gain actual knowledge of the alleged noncompliance, the FCA claim is

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166. See *id.* at 664–68 (determining the Ninth Circuit’s interpretation of the *Escobar* materiality standard to be unpersuasive).

167. See *id.* at 661–63 (explaining how the First, Seventh, and Ninth Circuits provided the Fifth Circuit with the lesson that continued payment by the government after it learns of a contractor’s noncompliance is highly strong evidence of the noncompliance’s immateriality and that said evidence had not been rebutted in this case).

168. See Taylor Sample, *With Widening Circuit Splits and Mounting Pressure Will 2019 See a Post-Escobar Decision from the Supreme Court*, JD SUPRA (Jan. 23, 2019), <https://www.jdsupra.com/legalnews/with-widening-circuit-splits-and-33647/> [https://perma.cc/ZPZ5-LT2R] (pointing out how the Supreme Court’s denial of certiorari for the *Harman* case leaves as precedent the Fifth Circuit’s position on materiality of an FCA claim when the government has knowledge of the alleged noncompliance and continues to pay or pays the contract in full).

169. *Id.*

170. See *id.* at 665 (discussing how the plaintiff’s complaint should fail for lack of materiality because of the strong evidence of the government’s knowledge of the noncompliance and its continued reimbursement for states that used Trinity’s guardrails).

171. Compare *United States ex rel. Lemon v. Nurses To Go, Inc.*, 924 F.3d 155, 161–62 (5th Cir. 2019) (determining an FCA claim to meet the *Escobar* material standard because the government did not have actual knowledge of the alleged noncompliance when it made payments to the contractor), with *Harman*, 872 F.3d 645, 665 (5th Cir. 2017) (determining the evidence of a complaint’s immateriality to be virtually insurmountable when the government has actual knowledge of the contractor’s alleged noncompliance and pays the contractor in full or continues to make payments).



not so easily defeated for lack of materiality.<sup>172</sup> The specific required circumstances that would trigger this heavy burden on the plaintiff are limited—the government must pay with full knowledge of the alleged fraud that is actually occurring.<sup>173</sup> Thus, this limitation makes it very difficult for businesses to abuse the Fifth Circuit's FCA materiality position, and makes the position an efficient and effective method to quickly and reasonably end an FCA dispute.<sup>174</sup>

#### B. *Similar Strict Positions of Other Federal Circuit Courts*

A few other federal circuit courts hold a similar position to that of the Fifth Circuit regarding the immateriality of an FCA complaint when the government actually knows of an alleged noncompliance and continues to make payments on a contract.<sup>175</sup> Most notably, the First, Third, and Seventh Circuits virtually mirror the position of the Fifth Circuit.<sup>176</sup> Those circuit courts, like the Fifth Circuit, strictly interpret the *Escobar* Court's materiality guidelines, and in doing so highlight the efficiency and effectiveness of such an interpretation on FCA cases.<sup>177</sup>

##### 1. The First Circuit's Position

The First Circuit, in *United States ex rel. Nargol v. DePuy Orthopaedics, Inc.*,<sup>178</sup> held akin to the Fifth Circuit when it encountered a case in which the government had actual knowledge of noncompliance and still reimbursed a contractor.<sup>179</sup> *Nargol* involved alleged Medicare fraud based on a contractor's omission of potential design flaws in metal hip replacements.<sup>180</sup> However, the government continued approving the designs and purchasing the metal hip replacements despite learning of these

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172. See *United States ex rel. Broadnax v. Sand Lake Ctr., P.A.*, No. 8:13-cv-2724-T-27MAP, slip op. at \*5 (M.D. Fla. Feb. 04, 2019) (limiting *Harman* to instances where the government has actual knowledge of a contractor's noncompliance and continues to pay the contractor or pays the contractor in full despite this actual knowledge).

173. See *id.* at \*4–5 (noting the circumstances when the *Harman* precedent would be triggered).

174. *Id.* at 5.

175. See Bergman, *supra* note 4 (listing and summarizing the differing federal circuit court positions on the materiality of an FCA complaint).

176. *Id.*

177. *Id.*

178. *United States ex rel. Nargol v. DePuy Orthopaedics, Inc.*, 865 F.3d 29 (1st Cir. 2017).

179. See *id.* at 35–37 (determining the whistleblower's complaint did not meet the FCA's demanding materiality standard as set out by the *Escobar* Court).

180. *Id.* at 31–34.

potential flaws from the whistleblower.<sup>181</sup> The United States District Court for the District of Massachusetts ruled for the defendant, leading to the whistleblower's appeal.<sup>182</sup>

The First Circuit took note of the *Escobar* Court's determination that the FCA's materiality standard is demanding.<sup>183</sup> The First Circuit specifically looked to the factor stating that when the government has actual knowledge of an alleged contractual violation and yet continues to pay on the contract, then the government's knowledge is strong evidence of the violation's immateriality to the government's decision to pay.<sup>184</sup> The record in *Nargol* presented the First Circuit with evidence that the government gained actual knowledge of the defendant's alleged violation, but did not withdraw approval of or cease reimbursement for the defendant's metal hip replacements.<sup>185</sup> To the First Circuit, because the government did not change its position once learning of the defendant's alleged violations, it was evidence that the alleged violations were immaterial to the government's decision to pay.<sup>186</sup> In the end, the First Circuit dismissed all but one of the whistleblower's complaints because it found the misstatements in these dismissed complaints to be immaterial to the government's decision to pay due to the government's actual knowledge of the alleged violations.<sup>187</sup>

## 2. The Third Circuit's Position

The Third Circuit holding in *United States ex rel. Petratos v. Genentech Inc.*,<sup>188</sup> was similar to the First Circuit's position.<sup>189</sup> In *Petratos*, the whistleblower alleged Genentech committed fraud under the FCA by omitting some potential side effects of a cancer drug in its submissions for Medicare

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181. *See id.* at 35 (noting how the record showed the FDA continued to reimburse healthcare providers who purchased and used the defendant's products, after the FDA learned of the alleged violations).

182. *Id.* at 34.

183. *Id.* at 34–35.

184. *Id.*

185. *Id.* at 35.

186. *See id.* at 35–36 (noting the *Escobar* materiality factors and the evidence of the government maintaining its normal position with the defendant after learning of the alleged violations).

187. *See id.* at 36, 43 (affirming the district court's dismissal of all but one of the whistleblower's complaints because they could not meet the exacting standards of a complaint made under the FCA).

188. *United States ex rel. Petratos v. Genentech Inc.*, 855 F.3d 481 (3d Cir. 2017).

189. *See id.* at 490–93 (holding the whistleblower's complaint to lack the materiality element required of an FCA complaint due to evidence of the FDA's continued approval of Genentech's cancer drug for reimbursement).

reimbursements.<sup>190</sup> The United States District Court for the District of New Jersey first held that the whistleblower's claim failed because the claim could not meet the falsity element of an FCA.<sup>191</sup> Predictably, the whistleblower appealed but the Third Circuit affirmed the decision.<sup>192</sup> However, the Third Circuit did not affirm the ruling based on the district court's reasoning.<sup>193</sup> Rather than deciding this case by looking at the falsity element, the Third Circuit determined that the complaint did not meet the FCA's demanding materiality standard.<sup>194</sup>

In *Petratos*, the Third Circuit examined the record under the lenses of the FCA's demanding materiality standard.<sup>195</sup> The Third Circuit specifically noted that it is strong evidence of immateriality when the government continues payment regardless of having actual knowledge of a noncompliance.<sup>196</sup> Interestingly, the Third Circuit interpreted this materiality factor to also mean an omission was immaterial to the government's payment decision when a relator admits the "[g]overnment would have paid the claims with full knowledge of the alleged noncompliance."<sup>197</sup> The Third Circuit even posited that if a relator did not plead that the government's actual knowledge of the noncompliance would influence its decision to pay, then the alleged noncompliance was immaterial as well.<sup>198</sup>

### 3. The Seventh Circuit's Position

The rollercoaster ride that was *United States v. Sanford-Brown, Limited*<sup>199</sup>

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190. *Id.* at 485.

191. *Id.* at 486.

192. *Id.* at 494.

193. *See id.* at 489 (describing how appellate courts may affirm a case based upon reasoning different than that of the district court and affirming the district court's decision because the claim did not meet the demanding materiality requirement of an FCA complaint).

194. *Id.*

195. *See id.* at 489–90 (examining the case record based on *Escobar* materiality).

196. *See id.* at 481, 489 (discussing the *Escobar* materiality factors).

197. *Id.* at 481–90.

198. *See id.* at 490 (noting the Third Circuit's belief that the FCA's demanding materiality standard should be implemented at the pleading stage and highlighting how the federal circuit courts are becoming split on whether to implement the FCA's demanding materiality standard at the pleading or trial stages of an action—which provides the basis of this argument for the bright-line rule to implemented at the trial stage).

199. *United States v. Sanford-Brown, Ltd.*, 840 F.3d 445 (7th Cir. 2016).

also brought the Seventh Circuit to a similar position.<sup>200</sup> *Sanford-Brown* was originally decided in 2015 by the Seventh Circuit in favor of the defendant, because the complaint was made utilizing the implied false certification theory, which the Seventh Circuit did not recognize at the time.<sup>201</sup> Granting the writ of certiorari, the Supreme Court took the case.<sup>202</sup> But, the Court quickly remanded *Sanford-Brown* back to the Seventh Circuit, having ruled on a similar issue in the *Escobar* decision just eleven days prior.<sup>203</sup> On remand, however, the Seventh Circuit again held for the defendant.<sup>204</sup>

The Seventh Circuit reached its final decision in *Sanford-Brown* based on the Supreme Court's holding in *Escobar*.<sup>205</sup> The Seventh Circuit first determined that the relator did not present a proper FCA complaint under implied false certification theory.<sup>206</sup> More importantly though, the Seventh Circuit determined that because the government—even with knowledge of the alleged noncompliance—continued to do business with the defendant, the alleged noncompliance was immaterial to the government's decision to make payments.<sup>207</sup> According to the Seventh Circuit, this evidence entitled the defendant to summary judgment.<sup>208</sup>

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200. See *id.* at 447 (holding summary judgment proper for the defendant because the plaintiff-relator could not meet the FCA's demanding materiality standard based off evidence of the government's actual knowledge of the alleged violation and its continued payment despite this knowledge).

201. See *United States v. Sanford-Brown, Ltd.*, 788 F.3d 696, 714 (7th Cir. 2015) (ruling in favor of the defendant because the plaintiff did not adequately prove an FCA violation).

202. See *United States ex rel. Nelson v. Sanford-Brown, Ltd.*, 136 S. Ct. 2506 (mem.) (2016) (granting writ of certiorari).

203. See *id.* ("Judgment vacated, and case remanded to the United States Court of Appeals for the Seventh Circuit for further consideration in light of [*Escobar*].") (citation omitted).

204. See *Sanford-Brown, Ltd.*, 840 F.3d, at 447–48 (holding for the defendant because the plaintiff-relator did not properly make a claim based on implied false certification theory and because the plaintiff-relator could not meet the FCA's demanding materiality standard).

205. See *id.* at 447 ("This matter is before us on remand from the United States Supreme Court for reconsideration in light of its recent decision in [*Escobar*].") (citation omitted).

206. See *id.* (concluding the conditions of "the implied false certification theory" were not met by the plaintiff-relator).

207. See *id.* (discussing how evidence of the Government's continued business with the defendant shows evidence of the alleged noncompliance's immateriality).

208. See *id.* (determining "summary judgment [to be proper] because Nelson failed to establish the independent element of materiality . . .").

The position taken by the First, Third, and Seventh Circuits vary subtly from the Fifth Circuit's position, but all these circuits strictly interpreted the *Escobar* Court's ruling on the materiality of an FCA claim. In each of these cases, the respective federal circuit court based its decision not solely just on the government's actual knowledge, but also on the government's actual behavior based on its knowledge.<sup>209</sup> In each case, the circuit courts reasonably determined that when the government learned of an alleged noncompliance and did nothing to stop paying the violating contractor, then the contractor did nothing to defraud the government.<sup>210</sup>

This common theme shows that, contrary to the Supreme Court's belief, a bright-line rule for the materiality element of an FCA claim is possible.<sup>211</sup> Specifically, a rule making just one of the *Escobar* materiality factors dispositive. Stated another way, when the government has actual knowledge of an alleged violation or noncompliance and continues to pay or pays the contract in full despite this actual knowledge, then that alleged violation or noncompliance is not material to the government's decision to pay. In these limited circumstances, an FCA claim should be dismissed for lack of materiality.

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209. See *United States ex rel. Nargol v. DePuy Orthopaedics, Inc.*, 865 F.3d 29, 34–35 (1st Cir. 2017) (noting the Government's actions upon gaining actual knowledge of the defendant's alleged violations showed the defendant's alleged violations did not materially affect the Government's decision to pay); see also *United States ex rel. Petratos v. Genentech Inc.*, 855 F.3d 481, 492 (3d Cir. 2017) (explaining how under the FCA “it is the Government's materiality decision that ultimately matters.”); see also *Sanford-Brown, Ltd.*, 840 F.3d at 447 (determining, based on *Escobar*, that the government's behavior is key to a materiality determination in an FCA case).

210. See *United States ex rel. Harman v. Trinity Indus. Inc.*, 872 F.3d 645, 660–61 (5th Cir. 2017) (indicating a strong showing of the immateriality of a violation when the Government decides to pay, having actual knowledge of a contractor's alleged misrepresentation, noncompliance, or violation and still continues to pay the contractor despite this actual knowledge); see also *Nargol*, 865 F.3d at 34–35 (determining the Government's continued business with the defendant, despite its knowledge of noncompliance, to show noncompliance was immaterial to the government's decision to pay the defendant); see also *Petratos*, 855 F.3d at 489–90 (finding the Government would have continued payment had it learned of Genentech's omissions and showing the omission would “not [be] material to the Government's payment decision”); see also *Sanford-Brown, Ltd.*, 840 F.3d at 447 (examining the record to find that despite gaining knowledge of the noncompliance, the Government chose to not penalize the defendant in any way).

211. See generally Krause, *supra* note 26, at 1813–14 (noting how, in an attempt to keep with “common-law concepts,” the Supreme Court in *Escobar* “declined to set brightline rules” for any of the materiality factors it laid out).

## V. THE NINTH CIRCUIT'S BROAD POSITION ON MATERIALITY AND A POTENTIAL SHIFT IN ITS POSITION

The strict interpretation of the *Escobar* Court's materiality factors is not shared by every federal circuit however.<sup>212</sup> The Ninth Circuit, for example, holds a looser interpretation of the FCA's demanding materiality standard. In the Ninth Circuit, even if the government has actual knowledge of a contractor's noncompliance and pays the contractor despite this knowledge, the courts may still find the noncompliance to meet the materiality element of an FCA claim.<sup>213</sup> Thus, in the Ninth Circuit, a contractor can accrue FCA liability more easily than in those federal circuits which strictly interpret the *Escobar* Court's materiality standard.

### A. *The Ninth Circuit's Broad Position on Materiality*

The Ninth Circuit first took this broad position in *United States ex rel. Campie v. Gilead Sciences*.<sup>214</sup> However, it has recently shown a shift in its position on the materiality of an FCA claim.<sup>215</sup> Furthermore, as will be

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212. See Matthew K. Organ & Takayuki Ono, *Escobar Decision Continues to Affect Major FCA Cases*, THE ATTORNEYS OF GOLDBERG KOHN (Mar. 22, 2018), <https://www.whistleblowersattorneys.com/blogs-whistleblowerblog/escobar-affects-major-fca-cases> [<https://perma.cc/HMA9-9F48>] (discussing how the *Escobar* decision created splits regarding the materiality of a claim when the government has actual knowledge of an instance of noncompliance and still continues to pay the contract, and how some federal circuits find the aforementioned government knowledge and payment to meet the FCA's materiality standard and other federal circuits do not); see also Matt Curley, *FCA Deeper Dive: Escobar and Its Aftermath—Part II*, INSIDE THE FCA (May 23, 2017), <https://www.insidethefca.com/fca-deeper-dive-escobar-and-its-aftermath-part-ii/> [<https://perma.cc/G5U5-GPXY>] (explaining how the federal circuits are split on the issue of whether an FCA claim should automatically fail for lack of materiality when the government has actual knowledge of the contractor's noncompliance and continues to pay the contractor or does not change its position in any way).

213. See Anne K. Walsh, *Ninth Circuit Revives False Claims Act Case Applying Escobar Materiality Standard*, HYMAN, PHELPS & MCNAMARA: FDA L. BLOG (June 17, 2017), <http://www.fdalawblog.net/2017/07/ninth-circuit-revives-false-claims-act-case-applying-escobar-materiality-standard/> [<https://perma.cc/AN6L-CQZB>] (examining the *Campie* case and discussing the Ninth Circuit's position that evidence of a noncompliance's materiality is shown when the government has actual knowledge of the noncompliance and continues to make payments to the contractor).

214. See *United States ex rel. Campie v. Gilead Scis., Inc.*, 862 F.3d 890, 899 (9th Cir. 2017) ("We construe the Act broadly . . .").

215. See Craig D. Margolis, Tirzah S. Lollar, & Michael E. Sammuels, *Ninth Circuit Finds Continued Government Payments Show that Alleged False Statements Are Not Material*, ARNOLD & PORTER (July 11, 2018), <https://www.arnoldporter.com/en/perspectives/publications/2018/07/ninth-circuit-finds-continued-government-payments> [<https://perma.cc/R6E5-TFSH>] (noting how a recent Ninth Circuit case may be signaling change regarding the materiality of an FCA claim when the government continues to make payments despite having actual knowledge of a contractor's noncompliance).

explained in this section, the Ninth Circuit in *Campie* did not need to rule that it is still evidence of a noncompliance's materiality when the government actually knows of the noncompliance and continues to pay despite this knowledge. The Ninth Circuit's position on the materiality of an FCA claim is based, in part, on prior Ninth Circuit precedent calling for a broad interpretation of the Act.<sup>216</sup> This precedent, stemming from *United States ex rel. Hendow v. University of Phoenix*,<sup>217</sup> still controls the Ninth Circuit's judgment on FCA cases, despite being possibly preempted by the *Escobar* Court's ruling.<sup>218</sup>

In *Campie*, two relators alleged Gilead Sciences, Inc. (Gilead) violated the FCA by making false claims about the quality of its HIV drugs in its compliance forms submitted to the Food and Drug Administration (FDA).<sup>219</sup> Furthermore, the relators alleged that because of these false claims, Gilead received billions of dollars in Medicare and Medicaid reimbursements.<sup>220</sup> Specifically, the relators alleged Gilead used chemicals from unapproved manufacturers in China, and hid or altered this fact in its compliance communications with the FDA.<sup>221</sup> Gilead did eventually seek the FDA's approval for its Chinese source though.<sup>222</sup> However, according to the relators, the company used the Chinese chemicals prior to seeking this approval.<sup>223</sup> More so, the relators alleged that Gilead falsified its records in order to gain the FDA's approval of the Chinese source.<sup>224</sup>

To make matters worse, Gilead retaliated against one of the whistleblowers, Jeff Campie, by terminating his employment after he brought up concerns of Gilead's alleged misrepresentations to the government.<sup>225</sup> Adding to its suspicious behavior, Gilead then requested the whistleblower to sign an agreement barring him from bringing an action against the company under the FCA.<sup>226</sup> Upon refusing, the two relators

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216. See *Campie*, 862 F.3d at 899 (9th Cir. 2017) (maintaining the Ninth Circuit's precedent of broadly construing the FCA in order to combat any and all forms of fraud against the government).

217. See generally *Hendow*, 461 F.3d at 1170 ("The False Claims Act . . . is not limited to such facially false or fraudulent claims for payment.").

218. See *United States ex rel. Rose v. Stephens Inst.*, 909 F.3d 1012, 1023 (9th Cir. 2018) (Smith, J., dissenting) (holding *Hendow* was overruled by the *Escobar* materiality standard).

219. *Campie*, 862 F.3d at 895–98.

220. *Id.* at 897.

221. *Id.* at 896.

222. *Id.*

223. *Id.*

224. *Id.*

225. *Id.* at 897–98.

226. *Id.* at 898.

brought this case in the United States District Court for the Northern District of California.<sup>227</sup>

The district court twice dismissed the relators' complaint for failure to state a claim.<sup>228</sup> According to the district court, the relators' FCA claims did not show that Gilead's misrepresentations were material to the government's decision to pay.<sup>229</sup> However, the Ninth Circuit granted appeal because of the *Escobar* Court's ruling on the materiality of an FCA claim occurring shortly after the district court rendered its decision.<sup>230</sup> The Ninth Circuit determined the district court had erred when it ruled against the relators' FCA claims.<sup>231</sup> And, in a stunning reversal, the Ninth Circuit found for the relators.<sup>232</sup>

To reach its decision, the Ninth Circuit first looked to precedent within its own jurisdiction.<sup>233</sup> The *Hendow* case holds that the Ninth Circuit should construe the FCA very broadly in order to protect the government from fraud.<sup>234</sup> Specifically, in regards to materiality, the court in *Hendow* held all that mattered was that a causal chain between the false statement and the government's payment.<sup>235</sup> Relying on this precedent, the Ninth Circuit proceeded to examine not only the FCA broadly, but the FCA materiality factors posited by the *Escobar* Court as well.<sup>236</sup>

The Ninth Circuit heavily relied on the *Hendow* precedent because the district court determined the payor agency, the Center for Medicare and

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227. *Id.*

228. *Id.*

229. *Id.* at 899.

230. *See id.* at 895–96 (noting the recency of the *Escobar* decision following the district court's ruling in *Campie* as a reason for the Ninth Circuit to hear the case).

231. *See id.* at 907 (“[R]elators allege more than the mere possibility that the government would be entitled to refuse payment if it were aware of the violations . . .”).

232. *See id.* at 909 (reversing the holding of the United States District Court for the Northern District of California and finding for the relators).

233. *See id.* at 898–99 (stating the *Hendow* precedent governs the analysis of FCA complaints in the Ninth Circuit).

234. *See Hendow*, 461 F.3d at 1170 (determining the FCA was designed to protect the government from any and all types of fraud and was given a broad scope by Congress in 1986).

235. *See id.* at 1174 (finding a causal chain of connection between the alleged violation and the government's decision to pay on a contract is necessary for a claim to meet the materiality element of the FCA).

236. *See Campie*, 862 F.3d at 904–05 (discussing the *Escobar* materiality factors of an FCA claim and construing them to find evidence of materiality even when the “[g]overnment pays a particular claim in full despite its actual knowledge that certain requirements were violated”).



Medicaid Services (CMS), technically was not defrauded for payment.<sup>237</sup> Furthermore, Gilead claimed the FDA approved its HIV drugs, providing evidence that its claims for payment to Medicare and Medicaid were not false.<sup>238</sup> According to Gilead, the FDA became aware of its noncompliance after approving the Chinese source but still continued to approve Gilead's HIV drugs despite knowing of the noncompliance.<sup>239</sup> Gilead further claimed that the FDA's approval shielded the company from FCA liability, utilizing a case from the Fourth Circuit to in an attempt to persuade the Ninth Circuit.<sup>240</sup> However, because of the *Hendon* precedent, the Ninth Circuit was neither impressed nor persuaded.<sup>241</sup>

The Ninth Circuit thought it insignificant that the payor agency was not technically the agency to which Gilead made misrepresentations.<sup>242</sup> It first observed that both the FDA and CMS were overseen by the Secretary of Health and Human Services.<sup>243</sup> From this basic connection, the Ninth Circuit deduced that essentially Gilead committed fraud against the Department of Health and Human Services.<sup>244</sup>

Next, the Ninth Circuit, mirroring the Third Circuit in *Petratos*, held that it was not the difference in federal agency that mattered, but whether or not the defendant induced the government to pay based on a misrepresentation.<sup>245</sup> In other words, what were the government's actions

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237. See *id.* at 903 (discussing why the district court dismissed the relators' complaint and how it erred according to *Hendon*).

238. See *id.* at 903–04 (noting Gilead's defense to the relators' FCA claims).

239. *Id.* at 906.

240. See *id.* at 903–04 (describing Gilead's defense to the relators' FCA claims based on Fourth Circuit precedent). See generally *United States ex rel. Rostholder v. Omnicare, Inc.*, 745 F.3d 694, 701–02 (4th Cir. 2014) (determining FCA cases are barred when the payment submissions are made to Medicare and Medicaid, and the FDA has already approved the drug).

241. See *Campie*, 862 F.3d at 904 (holding the Fourth Circuit's ruling, and thus the defense's argument, to be unpersuasive based on prior Ninth Circuit precedent).

242. See *id.* at 903 (asserting the distinction between the government agencies do not matter, only that a false statement was made to the government for payment).

243. *Id.* at 903.

244. *Id.*

245. See *id.* at 903 (holding the government's actions based on a contractor's misrepresentations in a statement for payment mattered, rather than what individual agency paid and the one to which the misrepresentations were made); see also *United States ex rel. Petratos v. Genentech Inc.*, 855 F.3d 481, 492 (3d Cir. 2017) (discussing the importance of the government's actions in determining the materiality of an FCA claim and holding the government's actions to control in the materiality analysis).

based on the misrepresentation?<sup>246</sup> Based on this logic, a reasonable person would believe that the Ninth Circuit would then find a misrepresentation to be immaterial when the government had knowledge of the misrepresentation and continued to pay despite knowing. However, the Ninth Circuit held otherwise.<sup>247</sup>

When examining the materiality element of the relator's FCA claim, the Ninth Circuit did utilize the materiality factors laid out by the *Escobar* Court.<sup>248</sup> However, the Ninth Circuit examined these factors broadly.<sup>249</sup> The Ninth Circuit evidenced this broad interpretation by holding that the government's continued payment despite having actual knowledge of a contractor's noncompliance was the inverse of what the Supreme Court reasoned this action to be.<sup>250</sup>

In *Campie*, the Ninth Circuit held "proof of materiality can include" situations where the government makes continued payments to a contractor despite it having actual knowledge of the contractor's violation of certain requirements.<sup>251</sup> This is contrary to the Supreme Court's holding in *Escobar*, which held this type of scenario to be evidence of the violation's immateriality.<sup>252</sup> Furthermore, this line of reasoning goes against the Ninth Circuit's logic that it should be the government's actions that dictate whether or not a violation was material to its payment decision.<sup>253</sup> More importantly, however, the Ninth Circuit did not have to stretch the *Escobar* materiality factors to find against Gilead.

The Ninth Circuit found that Gilead made misrepresentations to the

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246. See *Campie*, 862 F.3d at 903 (utilizing *Hendow* to hold that it matters not which federal agency was misled, but only that evidence can be shown to connect the false statement for payment to the government's action of payment).

247. See *id.* at 905 (determining evidence of an FCA claim's materiality where the government pays a claim in spite of its actual knowledge of a violation by the contractor).

248. *Id.*

249. *Id.* at 905–06.

250. Compare *id.* at 905 (finding proof of materiality to be in situations where the government continues to pay a claim in spite of having actual knowledge of a contractor's violation), with *Escobar*, 136 S. Ct. 1989, 2003 (determining the government's payment, despite its actual knowledge of a contractor's violation or noncompliance with an obligation, to be a factor showing the violation or noncompliance's immateriality).

251. *Campie*, 862 F.3d at 905.

252. *Escobar*, 136 S. Ct. at 2003.

253. See *Campie*, 862 F.3d at 903 (determining the focus should be on whether the government was fraudulently induced to pay based on the contractor's false statement).

FDA in order to obtain the approval of its Chinese source.<sup>254</sup> In other words, the government did not have actual knowledge of Gilead's violations.<sup>255</sup> Any payment made by CMS to Gilead were fraudulently induced by Gilead's initial misrepresentations to the FDA.<sup>256</sup> Gilead actively covered up its Chinese source to gain FDA approval of its HIV drugs—so, from the beginning it was virtually impossible for the government to have actual knowledge.<sup>257</sup> Thus, the Ninth Circuit did not need to hold the government's continued payments after gaining actual knowledge of a violation to be evidence of the violation's materiality in an FCA claim.<sup>258</sup> The government in *Campie* did not have actual knowledge, and so its continued payments to Gilead did not constitute a scenario similar to the *Escobar* Court's materiality factor showing immateriality.<sup>259</sup>

Gilead did try to use the government's continued purchases of the drugs after the FDA learned of Gilead's violations as a defense.<sup>260</sup> However, Gilead's defense was terminally flawed because upon learning of these violations the FDA materially changed its position, ultimately calling for a recall of Gilead's drugs.<sup>261</sup> And, Gilead eventually stopped using its Chinese source, making any later payments by the government after the stoppage insignificant to the issue in the case.<sup>262</sup> Moreover, Gilead used the Chinese source well before gaining FDA approval, and made misrepresentations to the FDA in order to gain the ability to be paid by the CMS.<sup>263</sup> Gilead's initial use of the Chinese source and its misrepresentations destroy any chance of the government having actual knowledge.<sup>264</sup> This is

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254. *See id.* at 905 (noting Gilead's alleged false claims were made to the FDA in order to gain its approval for Gilead's HIV drugs).

255. *Id.*

256. *Id.*

257. *See id.* at 906–07 (discussing how it is unclear exactly when or if the government gained actual knowledge of Gilead's violations).

258. *Id.*

259. *See id.* at 906–07 (noting, from the record and from the positions of the parties in contention, it is very unclear whether the government had actual knowledge of Gilead's alleged violations).

260. *Id.* at 906.

261. *See id.* at 906 (examining the evidence to find instances of the FDA warning Gilead of impurities, sending Gilead a letter of noncompliance, and of two recalls of Gilead's drugs).

262. *Id.*

263. *Id.* at 896.

264. *See id.* at 905 (“Mere FDA approval cannot preclude [FCA] liability, especially where . . . the alleged false claims procured certain approvals in the first instance.”).

because the payor agency was paying Gilead based on government approval gained through fraud.<sup>265</sup>

In the end, the Ninth Circuit determined a genuine question of fact existed regarding whether or not the government had actual knowledge of Gilead's noncompliance—justifying its reversal of the district court's dismissal.<sup>266</sup> As to Gilead's defense, the Ninth Circuit found that there might be other reasons why the FDA continued its approval of Gilead's drugs—though these other reasons were not stated in the opinion.<sup>267</sup> Thus, the government's continued payments after learning of Gilead's violations could still be evidence of the violation's materiality on its decision to continue payment.<sup>268</sup>

The Ninth Circuit made the correct ruling in *Campie*.<sup>269</sup> It is clear from the record in this case that Gilead intentionally defrauded the government of billions of dollars by making misrepresentations to the FDA in order to be reimbursed by the CMS.<sup>270</sup> However, the Ninth Circuit did not have to reach this decision by finding evidence of the government's actual knowledge of a contractor's noncompliance and its continued payment to the contractor to be material in triggering FCA liability. Gilead utilized an unapproved source in China for its HIV drugs and then made false statements to eventually gain approval for this source.<sup>271</sup> From the very beginning, Gilead concealed its source from the government until a couple of relators brought this to the attention of authorities.<sup>272</sup> Gilead clearly committed a violation under the FCA, and the Ninth Circuit was correct in reversing the district court's dismissal. But, the Ninth Circuit did not need to broadly interpret the *Escobar* materiality factors of an FCA claim to achieve its result.

Without actual knowledge, the government's continued payment to a noncompliant contractor is not evidence of the noncompliance's materiality

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265. *Id.*

266. *See id.* at 906–07 (discussing whether or not the government had actual knowledge of Gilead's violations and when it gained said knowledge).

267. *See id.* at 906 (holding there are many possible reasons why the FDA continued to approve Gilead's HIV medication after gaining actual knowledge).

268. *Id.*

269. *Id.*

270. *See id.* at 895–99 (detailing the allegations against Gilead).

271. *Id.* at 895–99, 906 (discussing how Gilead defrauded the government and finding that it obtained its FDA approval fraudulently).

272. *Id.* at 895–99.

on the government's decision to pay.<sup>273</sup> With actual knowledge, it is.<sup>274</sup> In the Ninth Circuit, however, the government's actual knowledge and its continued payment in spite of this knowledge is clearly not dispositive.<sup>275</sup>

The Ninth Circuit may have so broadly interpreted the *Escobar* materiality factors in *Campie* because of the *Hendon* precedent.<sup>276</sup> After all, the Circuit did shirk off a common theme among the federal circuits, which provided the makers of medications approved by the FDA with a shield from FCA liability in its pursuit of a reversal.<sup>277</sup> However, as previously stated, the record showed Gilead intentionally defrauded the government to gain approval for its drugs, making both the FDA shield and the continued payment with actual knowledge defenses moot.<sup>278</sup>

#### B. *A Potential Shift in the Ninth Circuit's Position*

In the two years since *Campie*, the Ninth Circuit has signaled that its position on the materiality of an FCA claim may be changing.<sup>279</sup> A dynamic duo of cases lit the signal in 2018—*United States ex rel. Berg v. Honeywell International, Inc.*<sup>280</sup> and *United States ex rel. Rose v. Stephens Institute*,<sup>281</sup> respectively. It may now actually be that *Campie* is an outlier case in the post-*Escobar* world.

273. See *Escobar*, 136 S. Ct. at 2003 (finding it to be evidence of a noncompliance or violation's immateriality when the government knows of said noncompliance or violation and continues to pay or pays the contract in full despite of this knowledge).

274. See *id.* (stating actual knowledge is evidence of noncompliance's materiality).

275. See *Campie*, 862 F.3d at 905 (finding proof of materiality in an FCA claim to include situations where the government has actual knowledge of a contractor's noncompliance and still makes payments to the contractor in spite of this knowledge).

276. See *id.* (determining, based on precedent from *Hendon*, that the Ninth Circuit should interpret the FCA broadly to encompass all forms of fraud, and holding it to be evidence of a violation's FCA materiality even when the government continues to pay on a contract despite actually knowing of said violation).

277. See *id.* at 906 (noting how other federal circuits are hesitant to rule on FCA claims involving drug manufacturers when the FDA has approved of the manufacturer's drug); see *D'Agostino v. Ev3, Inc.*, 845 F.3d 1, 9 (1st Cir. 2016) (discussing how FDA approval shielded a drug manufacturer from FCA liability); see *Petratos*, 855 F.3d at 490 (explaining the impact of FDA on FCA claims).

278. See *Campie*, 862 F.3d at 895–99, 904–08 (discussing Gilead's alleged actions and finding Gilead made fraudulent misrepresentations in order to gain the FDA's approval).

279. See generally Margolis, et al., *supra* note 215 (discussing the potential impact of *Berg* on other Ninth Circuit cases, based on the Ninth Circuit in *Berg* finding evidence of immateriality when it was shown the government had actual knowledge of a contractor's noncompliance and continued to pay the contractor in spite of this knowledge).

280. *United States ex rel. Berg v. Honeywell Int'l, Inc.*, 740 F. App'x 535 (9th Cir. 2018).

281. *Rose*, 909 F.3d 1012 (9th Cir. 2018).

The first case to signal the Ninth Circuit's new position on the materiality of an FCA claim was *Berg*.<sup>282</sup> In *Berg*, the issue was not specifically about the materiality of an FCA claim.<sup>283</sup> Rather, the case turned on whether the relators stated any part of an FCA claim.<sup>284</sup> The relators alleged that Honeywell International, Inc. (Honeywell), made false claims regarding the installation of equipment to the United States Army for payment.<sup>285</sup> The United States District Court for the District of Alaska granted summary judgment for Honeywell, ruling the relators failed to meet any element of an FCA claim.<sup>286</sup> On appeal, the Ninth Circuit affirmed the district court's ruling.<sup>287</sup>

Regarding the materiality of an FCA claim, the court in *Berg* correctly interpreted the *Escobar* materiality factors as intended by the Supreme Court.<sup>288</sup> The Ninth Circuit found the Army to have actual knowledge of Honeywell's allegedly fraudulent activity for an extended period of years.<sup>289</sup> Furthermore, the record showed that the Army continued to pay Honeywell for its services during this period of actual knowledge.<sup>290</sup>

The Ninth Circuit determined this evidence to show Honeywell's alleged fraud to be immaterial to the Army's decision to continue payment.<sup>291</sup> Thus, because the relators could not meet the FCA's demanding materiality element—and because they could not meet any of the elements at all—the Ninth Circuit affirmed summary judgment in favor of Honeywell.<sup>292</sup>

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282. See *Berg*, 740 F. App'x at 538 (holding the Army's actual knowledge of Honeywell's alleged noncompliance and its continued payment to Honeywell for a period of years to provide evidence that the alleged noncompliance was immaterial to the government's decision to pay).

283. *Id.* at 537.

284. See *id.* at 537 (noting the relators are appealing a motion of summary judgment against them).

285. *Id.*

286. See *id.* at 537–39 (9th Cir. 2018) (discussing the district court's reasoning for finding that the relators failed to meet any required element of an FCA claim).

287. See *id.* (agreeing with the district court's findings that the relators failed to meet any element of an FCA claim).

288. See *id.* at 538 (acknowledging the immateriality of an alleged violation on the government's decision to pay when the government has actual knowledge of said violation and still continues to pay on a contract in spite of its actual knowledge).

289. *Id.*

290. *Id.*

291. See *id.* (finding evidence of the Army's actual knowledge of Honeywell's alleged noncompliance and the Army's continued payment to Honeywell to show Honeywell's alleged noncompliance to be immaterial to the Army's continued payment).

292. See *id.* at 537–39 (finding the relator's presented no triable fact for any of the required elements for an FCA claim and affirming summary judgment in favor of Honeywell).

However, the Ninth Circuit in *Berg* did not expressly overrule its prior holding from *Campie* regarding an FCA claim's materiality.<sup>293</sup>

The Ninth Circuit next revisited the issue of an FCA claim's materiality in *Rose*.<sup>294</sup> In *Rose*, a group of relators alleged the Stephens Institute violated an incentive compensation ban in the conditions for its federal funding.<sup>295</sup> That case was originally dismissed by the district court, but found new life thanks to the *Escobar* decision.<sup>296</sup> The Ninth Circuit then heard the case to provide clarification on *Escobar*'s impact on Ninth Circuit precedent, affirming the district court's ruling.<sup>297</sup>

Providing some clarification, the Ninth Circuit determined that the *Hendow* precedent still controlled in the Ninth Circuit's analysis of an FCA claim, with *Escobar* merely creating a "gloss" over the *Hendow* precedent.<sup>298</sup> In other words, the Ninth Circuit would continue to broadly interpret the FCA.<sup>299</sup> Essentially, all that is required for a violation to be material is just some form of a causal connection between a contractor's violation and the government's decision to pay.<sup>300</sup>

The Ninth Circuit did acknowledge that evidence of the government's actual knowledge of a violation and its continued payment to a contractor despite this knowledge was strong evidence of the violation's immateriality.<sup>301</sup> However, upon examination of the record, the Ninth Circuit found no evidence showing the government had actual knowledge of the Stephens Institute's alleged violation.<sup>302</sup> Thus, the

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293. See *id.* at 538–39 (discussing the *Escobar* materiality factors and finding evidence of the Army's actual knowledge of Honeywell's noncompliance and the Army's continued payment to Honeywell to show the noncompliance to immaterial in its payment decision, but not mentioning its prior ruling to the contrary in *Campie*).

294. See *Rose*, 909 F.3d at 1018–23 (examining the *Escobar* materiality factors and comparing these factors to the record in *Rose*).

295. *Id.* at 1016.

296. *Id.*

297. See *id.* at 1017–23 (discussing the application of the *Escobar* standard for FCA claims and affirming the district court's granting of summary judgment for Honeywell).

298. See *id.* at 1020 (viewing *Escobar* "as creating a 'gloss' on the analysis of materiality").

299. *Id.*

300. See *United States ex rel. Hendow v. Univ. of Phoenix*, 461 F.3d 1166, 1174 (9th Cir. 2006) (noting the requirement of a causal chain between the alleged false statement for payment and the government's decision to make the payment).

301. *Rose*, 909 F.3d at 1019.

302. *Id.* at 1021.

Ninth Circuit did not directly revisit this issue or expressly overrule *Campie*.<sup>303</sup>

It is worth noting that the dissent in *Rose* staunchly argued *Escobar* overruled *Hendow*.<sup>304</sup> In his dissent, Judge Smith determined that *Hendow* no longer held control over the Ninth Circuit's analysis of FCA claims.<sup>305</sup> Judge Smith rightfully pointed out that the *Hendow* precedent heavily relies on express conditions of payment to be determinative in a materiality analysis.<sup>306</sup> This is contrary to the Supreme Court's holding in *Escobar*, which declared express conditions of payment to be relevant in a materiality analysis, but not dispositive.<sup>307</sup>

The dissent argued the *Hendow* precedent requires the question of materiality to be, “*whether* payment is conditioned on compliance . . . .”<sup>308</sup> however, the correct question as determined from the *Escobar* dissent's understanding of the materiality factors, is “*whether* the [g]overnment would truly find such noncompliance material to a payment decision.”<sup>309</sup> Because the Supreme Court in *Escobar* determined the materiality question to be based off the government's actions instead of what it labels as a condition of payment, the *Hendow* precedent regarding materiality has been overruled.<sup>310</sup>

The Ninth Circuit is potentially shifting the position it took on the materiality of an FCA claim in *Campie*.<sup>311</sup> This is evidenced by the Circuit's

303. See *id.* (noting the record's lack of evidence regarding the government's actual knowledge of the alleged violation, and thus the Ninth Circuit could not analyze the case based on this materiality factor).

304. See *id.* at 1023–24 (Smith, J., dissenting) (arguing *Escobar* overruled *Hendow*'s materiality analysis because the *Escobar* analysis focuses on whether the government found the alleged violation to be material to its decision to pay, rather than a mere a condition of payment).

305. See *id.* at 1023 (“*Hendow*'s materiality holding is no longer good law after *Escobar*.”).

306. See *id.* (discussing how *Hendow* held express conditions of payment to be evidence of materiality).

307. See *id.* (citing *Universal Health Servs. v. United States ex rel. Escobar*, 136 S. Ct. 1989, 1996 (2016)).

308. *Id.* at 1024.

309. *Id.* (emphasis added).

310. See *id.* (noting the majority erred in finding *Escobar* did not overrule the *Hendow* precedent controlling the materiality analysis of an FCA claim in the Ninth Circuit, because the *Hendow* analysis runs contrary to how the Supreme Court determined the materiality of analysis to be in *Escobar*).

311. See Carolyn Pearce, *Why Escobar Materiality Rule Applies to California FCA*, LAW360 (Sept. 5, 2018), <https://www.law360.com/articles/1079561/print?section=california> [https://perma.cc/NE6S-NRD4] (discussing the increasing influence of the Supreme Court's ruling on an FCA claim's materiality in *Escobar* on both the federal circuit level and on the state level in California); see Margolis,



acknowledgment in *Berg* and *Rose* that the government's actions based on its actual knowledge of a contractor's noncompliance should determine an FCA claim's materiality.<sup>312</sup> Also, the *Hendow* precedent is starting to lose its grip on the Ninth Circuit, as is shown by the majority's stretch to keep it alive<sup>313</sup> and the dissent's well-reasoned argument against it.<sup>314</sup> The only thing holding the Ninth Circuit back might be that it is waiting for a case similar to *Campie* in order to officially change its position, as the result of the Ninth Circuit's holdings in *Berg* and *Rose* support the argument that *Campie* is an outlier.<sup>315</sup>

#### VI. WHY THE FIFTH CIRCUIT'S STRICT POSITION SHOULD BE THE BRIGHT-LINE RULE FOR MATERIALITY OF AN FCA CLAIM

The section argues why the federal circuits—or the Supreme Court, if it decides to take another FCA case on the issue<sup>316</sup>—should adopt a position

et al., *supra* note 215 (describing the Ninth Circuit's ruling in *Berg*, in which the Circuit determined evidence of the Army's continued payments to Honeywell, despite the Army's knowledge of Honeywell's alleged violation for years, to be evidence of the violation's immateriality to the Army's decision of continued payment).

312. See *United States ex rel. Berg v. Honeywell Int'l, Inc.*, 740 F. App'x 535, 538 (9th Cir. 2018) (determining it to be strong evidence of a violations immateriality to the government's decision to pay a contractor when the Army had actual knowledge of Honeywell's alleged violations for years and continued to pay Honeywell despite this knowledge); see also *Rose*, 909 F.3d at 1019–21 (acknowledging it to be strong evidence of a violations immateriality to the government's decision to pay a contractor when the government has actual knowledge of the contractor's alleged violations and continues to pay despite this knowledge, but not finding this situation in the case record).

313. See *Rose*, 909 F.3d at 1019–20 (believing *Hendow* was “not clearly irreconcilable” with *Escobar*, despite admitting *Hendow* only explicitly considered express conditions for payment, but considering that *Hendow* might have been decided differently in light of *Escobar*) (quoting *Miller v. Gammie*, 335 F.3d 889, 893 (9th Cir. 2003)).

314. See *id.* at 1023–24 (arguing *Escobar* overruled *Hendow*'s materiality analysis because *Hendow* focuses the analysis on express conditions of payment, but *Escobar* holds that the focus should be on the government's action based on the alleged violation, noncompliance, or misrepresentation).

315. See *Berg*, 740 F. App'x at 538 (acknowledging the Army's continued payments to Honeywell, and its knowledge that Honeywell was allegedly noncompliant with its contract for years, to be evidence of the noncompliance's immateriality on the Army's decision to pay Honeywell); see also *Rose*, 909 F.3d at 1019 (finding immateriality to be shown when the government has actual knowledge of a violation and continues to pay on a contract regardless of this actual knowledge); *United States ex rel. Campie v. Gilead Scis., Inc.*, 862 F.3d 890, 905 (deeming it possible for the government's actual knowledge of a contractor's noncompliance or violation to still be evidence of the noncompliance or violation's materiality to the government's decision to pay the contractor).

316. See generally Brian P. Dunphy & Nicole E. Henry, *Third Time's Not the Charm: Supreme Court Again Declines to Weigh in on Escobar's "Materiality" Standard*, NAT'L L. REV. (Mar. 25, 2019), <https://www.natlawreview.com/article/third-time-s-not-charm-supreme-court-again-declines-to-wei>

on the materiality of an FCA claim similar to that of the Fifth Circuit.<sup>317</sup> Specifically, FCA claims should fail for lack of materiality when the record shows the government had actual knowledge of a contractor's noncompliance with an obligation and, despite this knowledge, continued to pay the contractor. This bright-line rule is limited, reasonable, and would efficiently ease the burden on the courts in deciding FCA cases.

This section will first discuss how this bright-line rule is in line with the Supreme Court's holding in *Escobar*.<sup>318</sup> Next, the section will posit the potential benefits such a simple bright-line rule would provide to the federal courts and business which regularly contract with the government. Lastly, this section will discuss the potential public policy implications such a bright-line rule could promote.

#### A. *This Bright-Line Rule Aligns with the Supreme Court's Holding in Escobar*

The Supreme Court in *Escobar* held the FCA's materiality standard to be a demanding one.<sup>319</sup> That is because across many areas of the law, materiality focuses on the actions of the recipient of the misrepresentation.<sup>320</sup> For example, in contracts law, misrepresentations are material if they are likely to cause a reasonable person to act.<sup>321</sup> Similarly, in the law of torts, misrepresentations are material if a reasonably prudent person would find the misrepresentation to be influential in making his or her decision.<sup>322</sup> Furthermore, *Black's Law Dictionary* defines material to be "[o]f such a nature that knowledge of the item would affect a person's decision-making . . . ."<sup>323</sup> A bright-line rule automatically ending an FCA claim when it is shown that the government had actual knowledge of a

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gh-escobar-s-materiality [<https://perma.cc/5G7B-LZQ6>] (discussing how the Supreme Court has declined to build upon or clear up the confusion caused by the *Escobar* ruling for a third time).

317. See *United States ex rel. Harman v. Trinity Indus. Inc.*, 872 F.3d 645, 670 (5th Cir. 2017) (holding the government's continued payments to a contractor despite knowledge of violations creates a presumption of immateriality; see also *United States ex rel. Lemon v. Nurses To Go, Inc.*, 924 F.3d 155, 156 (5th Cir. 2019) ("[I]f the Government regularly pays a particular claim in full despite actual knowledge that certain requirements were violated, . . . that is very strong evidence that those requirements are not material.") (quoting *Universal Health Services, Inc. v. U.S. ex rel. Escobar*, 136 S. Ct. 1989, 2003–04 (2016)).

318. See *Escobar*, 136 S. Ct. at 2003 (holding the government's payment of a claim is evidence that certain requirements are not material).

319. *Id.*

320. See *id.* at 2002 (noting materiality is virtually the same across varying areas of law).

321. RESTATEMENT (SECOND) OF CONTRACTS § 162(b) (AM. LAW INST. 1981).

322. RESTATEMENT (SECOND) OF TORTS § 538(2)(a)–(b) (AM. LAW INST. 1977).

323. *Material*, BLACK'S LAW DICTIONARY (11th ed. 2019).

contractor's noncompliance with an express or implied obligation and continued to pay the contractor regardless of this knowledge is aligned with the *Escobar* Court's holding and the varying legal definitions of materiality.

This bright-line rule emphasizes the government's actual knowledge and its actions based off its actual knowledge. It does not heavily focus on conditions of payment as the *Hendow* precedent does,<sup>324</sup> but instead focuses on whether the government was induced to act based on the contractor's alleged noncompliance or violation. After all, the *Escobar* Court did state conditions of payment were relevant, but not dispositive in an FCA materiality analysis.<sup>325</sup>

Furthermore, this bright-line rule is limited. The rule requires the government to actually have knowledge of a contractor's noncompliance, and the government's continued payment despite this knowledge, for it to be triggered. This limitation is shown by the Fifth Circuit in *Harman*, in which the court held it was clear and reasonable that the alleged noncompliance was in fact immaterial to the government's payment decision because said payment was given after the government gained actual knowledge of a contractor's noncompliance; it was clear and reasonable that the alleged noncompliance was in fact immaterial to the government's payment decision.<sup>326</sup> However, as the Fifth Circuit has also demonstrated, if it is found that the government did not have actual knowledge of a contractor's noncompliance and made payments, then such lack of actual knowledge of the noncompliance is evidence of the noncompliance's materiality.<sup>327</sup>

Moreover, the Court in *Escobar* noted the FCA's materiality analysis, while rigorous, was not so fact intensive that it could automatically survive

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324. See *United States ex rel. Rose v. Stephens Inst.*, 909 F.3d 1012, 1023 (9th Cir. 2018) (discussing how *Hendow* heavily relied on conditions of payment in the FCA materiality analysis it posited, and arguing that *Hendow* does not align with the Supreme Court's ruling in *Escobar*).

325. See *Escobar*, 136 S. Ct. at 2003–04 (determining the government's conditions of payment to be relevant in a materiality analysis of an FCA claim, but not dispositive because not all conditions of payment are actually material to the government's decision to pay a contractor).

326. See *United States ex rel. Harman v. Trinity Indus. Inc.*, 872 F.3d 645, 665 (5th Cir. 2017) (finding evidence of the government's continued payment to Trinity, despite having actual knowledge of Trinity's misrepresentations, to be evidence that the misrepresentations were immaterial to the government's decision to pay).

327. See *United States ex rel. Lemon v. Nurses To Go, Inc.*, 924 F.3d 155, 161–62 (5th Cir. 2019) (deciding a contractor's violation of an obligation to be material to the government's decision to pay the contractor when it was found that the government did not have actual knowledge of the contractor's violation).

summary judgment.<sup>328</sup> This means a bright-line rule making one of the *Escobar* materiality factors dispositive, is possible. And, as the *Escobar* Court held, there are multiple methods under which the government or relators can bring an FCA claim in court.<sup>329</sup> This bright-line rule, by focusing on whether the noncompliance was influential or induced the government to act, may be used either if express claims are violated or if the claim was brought under the implied false certification theory.

B. *This Bright-Line Rule Would Benefit Federal Courts and Government Contractors Alike*

Currently, there is a split among the federal circuits regarding the materiality of an FCA claim when the government has actual knowledge of a contractor's alleged noncompliance with a statutory, regulatory, or contractual obligation and continues to pay the contractor regardless of this knowledge.<sup>330</sup> Increasingly, federal courts are finding the government's continued payment, despite having actual knowledge of a contractor's noncompliance with an obligation, is evidence the noncompliance was immaterial to the government's decision to pay.<sup>331</sup> In other words, a

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328. See *Escobar*, 136 S. Ct. at 2004 n.6 (rejecting the contractor's argument that the materiality analysis is "too fact intensive" to allow for summary judgment or motions to dismiss in FCA cases).

329. See Johan H. Krause, *Holes in the Triple Canopy: What the Fourth Circuit Got Wrong*, 68 S.C.L. REV. 845, 847–48 (discussing how an FCA claim may be brought by a contractor's violation of an express condition of payment, and how the implied false certification theory evolved and became another theory under which an FCA claim may be brought).

330. See Chow, *supra* note 85, at 581–82 (discussing the split among the circuits regarding the materiality of an FCA claim); see also Scott Roybal & Joseph Barton, *Feature Comment: 2017 Civil False Claims Act Update*, GOV'T CONTRACTOR, Nov. 15, 2017, at 1, [https://www.sheppardmullin.com/media/publication/1681\\_TGC%2059-42-345.pdf](https://www.sheppardmullin.com/media/publication/1681_TGC%2059-42-345.pdf) [<https://perma.cc/HR7S-MFN5>] (discussing the potential circuit split the Ninth Circuit created by holding the government's continued payment to a contractor regardless of its actual knowledge of the contractor's violation of an obligation to be evidence of the violation's materiality to the government's decision to pay).

331. See Bergman, *supra* note 4 (noting a majority of federal courts are taking "a more stringent" stance toward the *Escobar* materiality factor's impact on the materiality analysis of an FCA claim); Steven A. Neeley & Brian Wagner, *After Escobar, Materiality Matters*, THE CONTRACTOR'S PERSPECTIVE (Jan. 31, 2018), <https://www.contractorsperspective.com/false-claims-act/after-escobar-materiality-matters/> [<https://perma.cc/7BX4-DBSN>] (explaining the *Escobar* decision's materiality position and its impact on businesses); J. Andrew Jackson & Ryan P. McGovern, *Judge Cites Escobar Materiality Standard, Vacates \$350 Million False Claims Act Judgment*, JONES DAY (Jan. 2018), <https://www.jonesday.com/en/insights/2018/01/judge-cites-iescobari-materiality-standard-vacates> [<https://perma.cc/5H KJ-DEZV>] (discussing how a federal district court strictly interpreted the *Escobar* materiality factors to find against the relators due to the relators' failure to prove the government did not have actual knowledge of the alleged violations by a nursing home operators despite its continued payment, which showed the violations to be immaterial).

growing number of federal circuits are showing one of the *Escobar* materiality factors to be dispositive. The Ninth Circuit's contrary holding in *Campie*, however, has not been directly overturned.<sup>332</sup> Meaning, the Ninth Circuit continues to ignore the Supreme Court's determination that strong evidence of a noncompliance's immateriality to the government's payment decision exists when the government has actual knowledge of the noncompliance and continues payment.<sup>333</sup>

Moreover, since the *Escobar* decision, businesses which regularly contract with the federal government have also experienced confusion in trying to understand the FCA and how to avoid accruing liability under it.<sup>334</sup> Right now, a defense utilizing the government's knowledge of the contractor's alleged violation and its continued payment to the contractor to show the violation was immaterial to the government's decision, is not viable depending on where an FCA claim is filed.<sup>335</sup> Thus, government contractors are robbed of a common defense throughout the country to a federal law—the law we all must commonly follow<sup>336</sup>—if an FCA claim against them is filed in a federal district court in California instead of in Texas.<sup>337</sup>

Even though the *Escobar* Court thought none of the materiality factors it posited were dispositive, a growing number of federal circuits seem to hold otherwise.<sup>338</sup> These circuits, such as the Fifth Circuit, hold so by placing the onus of the materiality analysis on the government's actions that were

332. *Campie*, 862 F.3d at 905; see also Daniel Wilson, 9th Cir. Won't Revisit FCA Materiality Dispute, LAW360 (Nov. 26, 2018, 10:23 PM), <https://www.law360.com/articles/1104764/9th-circ-won-t-revisit-fca-materiality-dispute> [<https://perma.cc/8GBF-PS4D>] (stating the Ninth Circuit did not directly revisit the issue of FCA materiality it was confronted with in *Campie*, and thus did not alter its position regarding FCA materiality).

333. See Italiano, *supra* note 63, at 1960 (discussing how the Ninth Circuit's holding in *Gilead* runs contrary to the Supreme Court's holding in *Escobar*).

334. See Seiden, *supra* note 31 (discussing how businesses regularly contracting with the government have been confused about how to properly avoid liability under the FCA since *Escobar*).

335. Compare *United States ex rel. Harman v. Trinity Indus. Inc.*, 872 F.3d 645, 667–68 (5th Cir. 2017) (determining the government's actual knowledge of Trinity's alleged fraud to be evidence of the alleged fraud's immateriality for the government's decision to continue contracting with Trinity), with *Campie*, 862 F.3d at 905 (finding proof of a noncompliance's materiality to the government's decision to pay in situations when the government has actual knowledge of a contractor's noncompliance, even though the government continues to pay or pays the contractor in full despite this knowledge).

336. See U.S. CONST. art. VI, cl. 2 (establishing federal law as the supreme law of the land and essentially making it the general law all must follow within the borders of the United States).

337. See *supra* note 335 and accompanying text.

338. See Krause, *supra* note 26, at 1813–14 (discussing the weaknesses of the *Escobar* decision because it did not fully or clearly define materiality and did not hold any factor to be dispositive).

based on the contractor's alleged violation of an obligation.<sup>339</sup> Due to this growing trend, both businesses and the federal courts would benefit from making this one materiality factor a dispositive bright-line rule. For when it is determined the government had actual knowledge of a contractor's alleged noncompliance with an express or implied obligation and continued to pay the contractor, the claim should fail for lack of materiality.

By having a reasonable and limited method to dismiss frivolous or insufficient FCA claims, federal courts could easily clear up some of their dockets.<sup>340</sup> Furthermore, this rule would enable government contractors to more easily plan out a defense to FCA liability.<sup>341</sup> During discovery, contractors would know to specifically look for evidence of the government's actual knowledge of the alleged violation and the government's continued payment or inaction despite this knowledge. Thus, the bright-line rule is consistent with the *Escobar* Court noting that FCA claims must meet the heightened standard of Federal Rule of Civil Procedure (9)(b).<sup>342</sup> Courts would then be able to easily rule on motions to dismiss or for summary judgment in instances when the government had actual knowledge of a violation and, despite its knowledge, continued to pay the contractor.

### C. Public Policies This Bright-Line Rule Would Promote

It is obvious that the general public policy behind the FCA is to prevent contractors from defrauding the federal treasury.<sup>343</sup> It is smart the

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339. See Italiano, *supra* note 63, at 1960 (discussing an emerging trend among federal courts to focus on the government's conduct once it is determined the government had knowledge of a contractor's noncompliance or violation of an obligation).

340. See generally Robert T. Rhoad & David Robbins, *Fraud, Debarment and Suspension—Part I: Fraud*, 2019 GOV'T CONT. YEAR IN REV. BRIEFS 25, 25 (charting the total number of cases by fiscal year and showing 767 new FCA cases filed in 2018).

341. See G. Christian Roux & John D. Hanover, *Implied False Certification Liability Under the False Claims Act: How the Materiality Standard Offers Protection After Escobar*, 38 CONSTR. LAW. 16, 21 (2018) (concluding an "effective defense" to an FCA complaint to be a showing of the alleged violations immateriality on the government's decision to pay the contractor).

342. See *Universal Health Services, Inc. v. United States ex rel Escobar*, 136 S. Ct. 1989, 2004 n.6 (2016), (noting the materiality analysis is not "too fact intensive," allowing for summary judgment in FCA cases, and noting that FCA cases must meet the heightened standard of Rule 9(b) of the Federal Rules of Civil Procedure); see also FED. R. CIV. P. (9)(b) (describing what a party must plead when the party is stating a claim involving fraud).

343. See Douglas K. Rosenblum & John A. Schwab, *FCA 101 A Practitioner's Guide to the False Claims Act*, CRIM. JUST. 26, 28–29 (discussing how the history of the FCA shows the intention behind the Act is to protect the government coffers from fraudulent government contractors).

government protects taxpayer funds. Keeping with the public policy behind the FCA, the bright-line rule posited by this Comment would promote a few public policies which would help prevent future FCA violations. First, the rule would incentivize contractors to disclose any noncompliance of express or implied obligations to the government. Second, the rule would ensure the government is more careful in paying potentially noncompliant contractors. And third, this bright-line rule would provide a limited and reasonable but necessary check on an incredibly powerful and broad federal statute.

This rule would incentivize contractors to disclose violations to the government because as soon as the government has actual knowledge of the alleged fraud and does not cease paying the contractor, the contractor has a viable defense to FCA liability.<sup>344</sup> With this guaranteed defense to incentivize them, contractors would likely be more open and honest in their business dealings with the government. This incentivized reporting by contractors would also diminish the government's heavy reliance on whistleblowers—who are economically incentivized—to report to the government any misdeeds of a contracting company.<sup>345</sup> By having a rule incentivizing contractors to self-report their own violations, the government becomes better equipped with knowledge to protect taxpayer funds. Moreover, the federal government has openly called for contractors to voluntarily disclose instances of violations or noncompliance and to assist the government in investigating FCA claims.<sup>346</sup>

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344. See Italiano, *supra* note 63, at 1969–77 (discussing the *Escobar* decision's impact on the health care industry as well as benefits and defenses to FCA liability provided by acts of self-disclosure).

345. See *Justice Department Recovers Over \$2.8 Billion from False Claims Act Cases in Fiscal Year 2018*, U.S. DEP'T OF JUST. (Dec. 21, 2018), <https://www.justice.gov/opa/pr/justice-department-recovers-over-28-billion-false-claims-act-cases-fiscal-year-2018> [https://perma.cc/Y7A8-EW6K] (describing how much money the Justice Department recovered in 2018, and noting that whistleblowers filed 645 FCA claims in 2018); *Justice Department Recovers Over \$3.7 Billion From False Claims Act in Fiscal Year 2017*, *supra* note 1 (describing how much money the Justice Department recovered from FCA claims in 2017, and pointing out that whistleblowers filed 669 FCA claims and earned a total of \$392 million that year); *Justice Department Recovers Over \$4.7 Billion from False Claims Act Cases in Fiscal Year 2016*, U.S. DEP'T OF JUST. (Dec. 14, 2016), <https://www.justice.gov/opa/pr/justice-department-recovers-over-47-billion-false-claims-act-cases-fiscal-year-2016> [https://perma.cc/8T2G-JUJE] (discussing how much money the Justice Department recovered from FCA cases in 2016, and noting that, in 2016, whistleblowers brought 702 FCA claims and earned a total of \$519 million).

346. U.S. DEP'T OF JUSTICE, DEPARTMENT OF JUSTICE ISSUES GUIDANCE ON FALSE CLAIMS ACT MATTERS AND UPDATES JUSTICE MANUAL, (2019), <https://www.justice.gov/opa/pr/departments-justice-issues-guidance-false-claims-act-matters-and-updates-justice-manual> [https://perma.cc/79BC-TNDZ] (promoting the Justice Department's guidance and incentives for contractors to voluntarily disclose information about potential violations or instances of noncompliance).

Even the FCA itself allows for reduced damages when contractors self-report violations under the Act.<sup>347</sup> The bright-line rule offered in this Comment, however, would likely prevent many FCA violations from happening at all. By incentivizing contractors to report any noncompliance with an express or implied obligation, the government and contractor would have more time to remedy the situation before the contractor actually violates the FCA.

As the Supreme Court held in *Escobar*, the FCA was never intended to prosecute garden variety contractual disputes.<sup>348</sup> The FCA is very broad and powerful. The Act's penalties are seemingly merciless.<sup>349</sup> However, despite the Court's check on the scope of the Act, numerous FCA claims are filed each year.<sup>350</sup> Not all of these claims are victorious for the government or relator.<sup>351</sup> This means the FCA is being used to, or at least is being used in an attempt to, prosecute inconsequential or insubstantial contract disputes.

The bright-line rule posited here, making one of the *Escobar* materiality factors dispositive, would provide a reasonable and limited check on the Act. The rule would protect government contractors from facing costly FCA litigation in instances when their alleged violations were not actually material to the government's payment decision. The claim would automatically fail because the government already knew about the alleged violation and has shown through its actions that it does not care about the violation in rendering its payment decision. Thus, a bright-line rule as posited here would ensure the FCA is utilized properly while promoting public policy.

## VII. CONCLUSION

The Fifth Circuit correctly held when the government has actual knowledge of a contractor's alleged violation and continues to pay the contractor, the continued payment is substantial evidence that the violation

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347. False Claims Act, 31 U.S.C. § 3729(a)(2) (2009).

348. *Escobar*, 136 S. Ct. at 2003.

349. See Margolis, *supra* note 1, at 27 (describing the severity of the FCA's punishments).

350. See generally *Fraud Statistics - Overview*, U.S. DEP'T OF JUST., [https://www.justice.gov/civil/page/file/1080696/download?utm\\_medium=email&utm\\_source=govdelivery](https://www.justice.gov/civil/page/file/1080696/download?utm_medium=email&utm_source=govdelivery) [<https://perma.cc/9YZL-SWC8>] (listing the total number of cases brought by the government and relators from October 1, 1987 to September 30, 2018, which shows that a total of 2,448 FCA cases were brought between 2016 and 2018).

351. See *United States ex rel. Harman v. Trinity Indus. Inc.*, 872 F.3d 645, 669–70 (5th Cir. 2017) (holding against the relator).



was immaterial to the government's payment decision.<sup>352</sup> The Ninth Circuit held to the contrary based off precedent overruled by *Escobar*.<sup>353</sup> The bright-line rule posited in this Comment mirrors the Fifth Circuit's position. It makes just one of the *Escobar* materiality factors dispositive. The rule offered here advances public policy in a limited and reasonable manner and eases the burden courts face in presiding over the numerous FCA cases each year.

Overall, the bright-line rule offered in this Comment is a perfect fit for the post-*Escobar* landscape because it would promote sound public policies for both contractors and the government. The rule is only applicable in limited circumstances. The rule is reasonably based on an almost universal legal principal that for fraud or misrepresentation to be material it must be influential on the recipient's actions. More so, a growing number of federal circuits are interpreting the *Escobar* materiality factors in a manner that is similar to this offered bright-line rule. And, most importantly, the rule is in line with the *Escobar* Court's holding on the materiality of an FCA claim.

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352. See *id.* at 665–70 (holding the government's actual knowledge of the contractor's alleged omission and its continued payment to the contractor showed overwhelming evidence that the alleged omission was not in any way material to the government's payment decision).

353. See *United States ex rel. Campie v. Gilead Scis., Inc.*, 862 F.3d 890, 905 (9th Cir. 2017) (holding materiality can be found when the government has actual knowledge of the contractor's alleged violation and continues payment to the contractor).