



# Legal Briefs

Cases, statutes and legal issues of interest to AGC members

## AGC Cal. LEGAL BRIEF

March 2014

### Hoping for Summary Judgment on California False Claims? *Au Contreras*

*By Aaron P. Silberman and Dennis J. Callahan*

Like a recurring nightmare for public contractors in the state, the California Court of Appeal recently issued a second opinion in the case of *San Francisco Unified School District ex rel. Contreras v. Laidlaw Transit, Inc.* that, like the first one, broadly construes the California False Claims Act (CFCA). The first decision (*Contreras I*) made clear that a whistleblower may state a viable CFCA claim, and subject the defendant to potentially costly and distracting discovery, even where she cannot allege that any express statement in the contractor's requests for payment was false. Now, in a decision filed on March 11, 2014 (*Contreras II*), the court has established very difficult standards for a contractor to meet when asserting after discovery that there is no need for a trial either because the alleged false claims were immaterial to the government's decision to pay or because the contractor lacked the required intent to be liable under the CFCA. More than ever, contractors on public contracts in California should take extreme care to avoid requesting payment without making sure they have complied with all material contract requirements, regardless of whether they expressly certify that compliance in their invoices.

In the *Contreras* case, several whistleblowers, or *qui tam* relators, filed a lawsuit against a school bus services contractor, First Student, alleging that it violated the CFCA by "knowingly" presenting false claims for payment to the San Francisco Unified School District. The contract in the *Contreras* case required, among other things, that First Student meet state and federal safety standards and that it "maintain its buses in 'excellent mechanical condition and appearance.'" The complaint alleged that First Student presented invoices to the District while in knowing breach of the contract's maintenance provisions and that doing so violated the CFCA.

In 2010, First Student successfully requested that the trial court dismiss the relators' complaint for failing to allege that any express representations in its invoices were false. The relators appealed, and, in *Contreras I*, the Court of Appeal reversed. The court held that a contractor that fails to comply with a material contract term, and submits invoices without informing the procuring agency of the non-compliance, may be liable under the CFCA. The panel in *Contreras I* became the first California court to embrace the doctrine of implied certification under the CFCA.

AGC member attorneys provide, from time to time, reviews and analyses of cases, statutes and legal issues of general interest to AGC members. This bulletin is intended to provide the reader with general information regarding current legal issues. It is not to be construed as specific legal advice or as a substitute for the need to seek competent legal advice on specific legal matters. For more information on AGC's Legal Advisory Committee, whose members contribute Legal Briefs, please contact John Hakel at 626/608-5800 or check AGC's website at [www.agc-ca.org](http://www.agc-ca.org).



# Legal Briefs

Cases, statutes and legal issues of interest to AGC members

Having survived First Student’s attack on the complaint, the parties continued the litigation back in the trial court. After completing extensive (and no doubt expensive) discovery, First Student moved for summary judgment, arguing that the undisputed evidence showed that the relators could not prove two required elements of their false claims case – materiality and “scienter” (actual knowledge, deliberate ignorance or reckless disregard as to the truth of the alleged false claim). The trial court granted the motion, finding both that the false certifications alleged by the relators were not material to the school district’s decision to pay the invoices and that the busing company did not have the required knowledge of its noncompliance with the contract’s maintenance obligations. The relators appealed for a second time, and, as with the first appeal (in *Contreras I*), the Court of Appeal reversed the trial court.

**Materiality.** Unlike other violations listed in the CFCA (like submitting false statements), the type of violation alleged by the relators in the *Contreras* case – submitting a false request for payment – does not explicitly state that materiality is an element of the plaintiff’s proof. Materiality under that CFCA provision is a judge-made doctrine that requires, as a condition of false claims liability, that the alleged falsity of the claim be material to the public entity’s decision to pay the contractor. The purpose of the materiality requirement is to reject false claims lawsuits based on insignificant contract breaches.

In the proceedings below, the trial court accepted First Student’s argument that the maintenance deficiencies alleged by the relators – such as using buses with substandard tire tread depths and brake pad thicknesses, and delaying or skipping periodic mechanical safety inspections – were not material because the school district continued to pay invoices after the allegations came to light. The appeals court rejected this ruling for two principal reasons. First, the court distinguished between the *allegations* that the contractor ignored its maintenance failures and *evidence* that it did so. The court noted that First Student presented no evidence that the school district ever paid invoices at a time when it *knew* the allegations were true.

Second, and more troubling for contractors, *Contreras II* adopted the California Attorney General’s view, presented in an amicus (“friend of the court”) filing on the issue, that a public agency’s decision to pay does not control the materiality question. The court held that, even if the District had been aware of First Student’s maintenance failures but still continued to pay the invoices, this would not prove that the failures were immaterial. Rather, the court concluded that the materiality inquiry is “not whether [the falsity] actually influenced the government not to pay a particular claim,” but whether it has a “natural tendency to influence or is capable of influencing the government funding decision.”



# Legal Briefs

Cases, statutes and legal issues of interest to AGC members

Although it was not presented in this case, because it was disputed whether the government actually knew of the contractual failures at the time it paid the invoices, this second rationale would seem to render the government's actual knowledge inconsequential. For lots of reasons, the government might pay invoices even where it knew information that could justify a decision to withhold payment. Perhaps the government does not want to risk an interruption in service, or perhaps the contracting officer believes that the contractor's failure deserves some sanction short of a full denial of payment. At the most fundamental level, when the controlling materiality inquiry concerns all of the inputs into the authorizing official's payment decision, and what is "capable of influencing" it, plaintiffs in CFCA actions should have little difficulty in raising a disputed issue of material fact to survive summary judgment, and send the case to trial (or give the plaintiffs significant leverage in settlement discussions).

Where the government knew of the falsity and still paid, a meaningful materiality requirement would put the onus on the whistleblower to overcome that important fact with evidence that the authorizing official made the decision to pay for a reason unrelated to contractor's noncompliance with contract requirements. Such evidence could be in the form of internal emails or discussions deliberating the payment decision,

or correspondence with the contractor regarding the reasons payment was being made despite the noncompliance. As it stands, however, the "capable of influencing" standard applied by the court in *Contreras II* largely vitiates the materiality requirement.

**Contractor's Knowledge.** The CFCA holds liable only those contractors who "knowingly" submit false claims, a standard that includes acting in deliberate ignorance or with reckless disregard of the truth or falsity of the information presented to the government. In support of its contention that it did not knowingly violate the contractual maintenance requirements, First Student argued that throughout the contract it had been subject to annual California Highway Patrol inspections that invariably assigned First Student the CHP's highest "compliance rating" of "satisfactory," meaning that the contractor's facilities did not jeopardize highway safety.

While the *Contreras II* panel acknowledged that this evidence may have satisfied First Student's initial showing in support of summary judgment, the court considered it insufficient to resolve the knowledge issue as a matter of law because the plaintiff had presented countering "evidence of widespread and persistent violations of contractual maintenance requirements." In this regard, the court found particularly persuasive deposition testimony from the contractor's maintenance manager that the company did not adhere to its audit policies, and documentation of hundreds of instances of First Student's use of buses with illegally thin

AGC member attorneys provide, from time to time, reviews and analyses of cases, statutes and legal issues of general interest to AGC members. This bulletin is intended to provide the reader with general information regarding current legal issues. It is not to be construed as specific legal advice or as a substitute for the need to seek competent legal advice on specific legal matters. For more information on AGC's Legal Advisory Committee, whose members contribute Legal Briefs, please contact John Hakel at 626/608-5800 or check AGC's website at [www.agc-ca.org](http://www.agc-ca.org).



# Legal Briefs

Cases, statutes and legal issues of interest to AGC members

brake linings. The court concluded that the frequency of these maintenance failures gave rise to a “reasonable inference that defendants acted in reckless disregard of the truth of its implied certifications of compliance with the Contract.”

## Conclusion

*Contreras II* will make it nearly impossible in most CFCA cases for defendants to get out of cases on summary judgment based on materiality or contractor knowledge defenses, even where the weight of evidence strongly favors the defendants. As a result, unless and until this decision is overturned by the California Supreme Court, plaintiffs will have a smoother road to trial on their CFCA claims. This in turn likely will force significant settlements from contractors daunted by the specter of the CFCA’s treble damages and penalties provisions and other consequences of being subject to a CFCA judgment, like its impact on a contractor’s past performance and the potential for debarment from public contracting.

The California Supreme Court refused the defendant’s request to review *Contreras I*. If, as expected, First Student petitions the Court to review the *Contreras II* decision, the Supreme Court likely will decide early this summer whether to hear the appeal.

*Aaron Silberman and Dennis Callahan are shareholders at Rogers Joseph O’Donnell, PC, where they focus on construction and government contracts. Aaron is the current Chair of the San Francisco Bay Area District and former chair of the Legal Advisory Committee. For more information, visit the RJO website at [www.rjo.com](http://www.rjo.com).*