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THE CALIFORNIA FALSE CLAIMS ACT: A POWERFUL WEAPON AGAINST CONTRACTORS GETS MORE POWERFUL

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If the California False Claims Act ("Cal. FCA"), starting at Section 12650 of the Government Code, were a gun, then the Legislature just coated the bullets with teflon and a state appeals court just informed contractors that their bulletproof vests are full of holes. If this analogy leaves you feeling less than secure, as intended, then read on.

Effective January 1, 2010, the Cal. FCA was amended not only to expand the bases for liability under the Act but also to increase dramatically the penalties that may be imposed for violations. Some other changes were also made, though it is unclear what their impact will be.

More False Statements May Subject Contractors to Cal. FCA Liability

First, the Legislature amended the portion of Act (at Section 12651(a)(2)) describing liability for submitting, or causing submission of, false statements in support of a request for payment, property or services. The Cal. FCA used to provide that, among violations under the Act, was knowingly making or using a false record or statement "to get a false claim paid or approved" by the government. Now, the language "to get" has been replaced with "material to payment." The effect is to substantially broaden the conduct that will violate the Act.

In 2008, the U.S. Supreme Court determined that the language "to get" in the federal FCA (on which the Cal. FCA is modeled) meant that, in order for a party responsible for a false statement to be liable under the Act, that party had to intend that the statement would result in payment by the government. *Allison Engine Co. v. United States ex rel. Sanders*, 128 S. Ct. 2123 (2008). For example, if a party not in contract with the government (i.e., a subcontractor or supplier) made a knowingly false statement in connection with a government funded project but did not know that government funds were involved, it could not be liable for false statements.

In direct response to the *Allison Engine* decision, the Congress in 2009 passed the federal Fraud Enforcement and Recovery Act ("FERA"), amending the federal FCA by replacing "to get" in the federal FCA with "material to payment." By making precisely the same change to the Cal. FCA (in Section 12651(a)(2)), the California Legislature clearly intended the same expanded false statements liability. This language is consistent with a California appeals court decision, issued years before *Allison Engine*, the FERA, or the Cal. FCA amendments – *City of Pomona v. Superior Court*, 89 Cal. App. 4th 793 (2001). In that case, the court held that a pipe supplier could be liable under the Cal. FCA for false statements in its catalog about the lead content of one of its pipe models, even though the supplier had no knowledge that any of its pipe would be used on a public project or paid for with public funds.

More Cal. FCA Violations May Subject Contractors to Cal. FCA Penalties

A second major change made to the Cal. FCA in the 2010 amendments also involves false statements liability and deprives contractors of a rare bit of good news they received in 2007. Section 12651(a) used to provide that a party may be liable for civil penalties for each "false claim." Now, it provides for a penalty for each "violation." Again, this expands contractors' potential liability under the Act.

In 2007, a California Court of Appeal in *Fassberg Construction Co. v. Housing Auth. of the City of Los Angeles*, 152 Cal. App. 4th 720 (2007), ruled that the Cal. FCA, by limiting liability for penalties to "false claims," excluded them from other violations, such as false statements. Thus, while false statements could result in liability for damages they caused (and which could be proven), they could not result in penalties. In many cases, Cal. FCA damages are minimal or non-existent, and, in many more, they are at least very difficult to prove. Penalties, in contrast, are usually easy to prove and can be substantial. For example in *Fassberg*, the court reversed millions of dollars in penalties against a contractor, primarily for false change order requests and weekly payroll reports.

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By replacing "false claims" with "violations" in the Cal. FCA, the 2010 amendments effectively overrule *Fassberg*. Now every false statement may subject a contractor to a civil penalty, in addition to damages liability.

Penalties Are Now Clearly Mandatory Under the Cal. FCA

To make matters worse, the 2010 amendments now make clear that courts must assess a penalty for every Cal. FCA violation by a contractor. A previous amendment, passed in 2007, may have already accomplished this when it raised the floor on penalties. Prior to the 2007 amendment, the Act (in Section 12651(a)) provided that violators "may" be liable for penalties of "up to $10,000." The 2007 amendment changed that language to provide for penalties from $5,000 to $10,000. That may have eliminated the courts' discretion to assess penalties of less than $5,000 per violation (decisions interpreting language in the federal FCA identical to that in the amended Cal. FCA have held it to require courts to impose at least a $5,000 penalty for each violation), but this was unclear, since the word "may" remained in this section. The 2010 amendments remove all doubt, replacing "may" with "shall." Thus, the statute now requires courts to assess a penalty of at least $5,000 for each and every Cal. FCA violation they find.

It Is Now Clear that Facially "True" Claims May Nevertheless Subject Contractors to Cal. FCA Liability

Finally, in *San Francisco Unified School District ex rel. Contreras v. Laidlaw Transit, Inc.*, 182 Cal. App. 4th 438 (2010), a California appeals court expressly recognized for the first time that contractors may be liable under the Cal. FCA under the so-called "implied certification theory."

Under this theory, a claim may be "false," and so subject a contractor to liability, even if every express statement in the claim is true, where it requests payment to which the contractor is not entitled. The idea is that the claim *implies* that the contractor is entitled to the payment requested, that is that the work has been performed completely and in accordance with all contract, legal and regulatory requirements material to payment.

Prior to *Laidlaw*, it had not been decided whether contractors could be liable for implied certifications under the Cal. FCA, though there was always the risk that California courts would follow the decisions applying the theory to the federal FCA. Now, thanks to *Laidlaw*, there is no room for doubt.

Conclusion

For a long time, State and local governments and whistleblowers have had a powerful weapon against contractors in the Cal. FCA. Some have used it appropriately to ferret out and remedy fraud; some have used it improperly to extort high dollar settlements or to coerce contractors to abandon valid contract claims. With the recent developments discussed above, this weapon has become even more powerful. Contractors beware.

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