

Legislative Analysis



FALSE CLAIMS ACT

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House Bill 4117

Sponsor: Rep. Gino Polidori

Committee: Judiciary

First Analysis (3-11-09)

BRIEF SUMMARY: The bill would create the False Claims Act by which private citizens, the state attorney general, or authorized persons representing local governments could bring an action against a person or entity who committed fraud against the state or a local government.

FISCAL IMPACT: The bill would have an indeterminate but likely positive fiscal impact on state and local government. Although the bill would create a new cause of action, costs associated with prosecuting the case would be reimbursed by the defendant to the action if they were found liable. Also, a person who violates the provisions of the act would be liable to the state or political subdivision for three times the amount of damages the state or political subdivision incurred and for a civil penalty of not less than \$5,000 and not more than \$10,000. Both the treble damages and civil penalty would be deposited in the General Fund of the state or political subdivision.

THE APPARENT PROBLEM:

In 2005, the Legislature enacted the Medicaid False Claims Act (Public Act 337). The new act allowed individuals, as well as the state attorney general, to initiate a civil suit in the name of the state against another person or business believed to have filed false or fraudulent claims for Medicaid payments. The act allows the attorney general to intervene and take over the prosecution of a case with merit, though the citizen who initiated the claim shares in the recovery of the award. The act also protects those citizens, sometimes referred to as "whistleblowers," who often are employees of the person or business charged with fraud, from retaliation by their employers.

On the federal level, whistleblower laws are not limited just to Medicare or Medicaid, but apply to any situation involving fraud against the government. Reportedly, actions brought under the whistleblower laws are very successfully litigated, and return almost \$15 for each dollar spent on prosecuting a case. Twenty-three states, the District of Columbia, and several large cities now have False Claims Act laws to go after those who would defraud state entities.

In light of the anticipation of federal stimulus dollars expected to be used by state and local governmental entities on various infrastructure projects, it has been suggested that Michigan enact a broader false claims law that would encompass fraudulent acts against not just the state, but also local governments.

THE CONTENT OF THE BILL:

The bill would create a new act known as the False Claims Act to establish remedies and sanctions against an individual or entity who presents a false or fraudulent claim to obtain money, property, or services from the state or a political subdivision (i.e., a local unit of government). It allows for enforcement by a "prosecuting authority" or by a private party. The bill would prohibit retaliation against someone who pursues a remedy under this new act.

(A "prosecuting authority" would be defined to mean the attorney general or an official charged with investigating, filing, and conducting civil legal proceedings on behalf of a political subdivision. A "political subdivision" includes a county, city, township, village, district, metropolitan government or authority, political body with the legal power or authority to levy taxes, or other legally authorized local governmental body, or a combination of such subdivisions.)

Damages and Penalties for False Claims. A person who commits any of the offenses described below, regardless of specific intent to defraud, is liable to the state or a political subdivision for three times the amount of damages sustained because of the offense, the costs of an action brought to recover damages or a penalty, and for a civil penalty of not less than \$5,000 or more than \$10,000 for each act.

The bill would apply to a person (individual or entity) who:

- * Knowingly presents or causes to be presented a false claim for payment or approval to an officer or employee of the state or a political subdivision.
- * Knowingly makes or uses, or causes to be made or used, a false record or statement to get a false claim paid or approved.
- * Conspires to defraud by getting a false claim allowed or paid.
- * Has possession, custody, or control of public property or money used or to be used by the state or political subdivision and knowingly delivers or causes to be delivered less property than the amount for which the person receives a certificate or receipt.
- * Is authorized to make or deliver a document certifying receipt of property used or to be used by the state or a political subdivision and knowingly makes or delivers a receipt that falsely represents the property used.
- * Knowingly buys, or receives as a pledge of an obligation or debt, public property from any person who lawfully could not sell or pledge the property.
- * Knowingly makes, uses, or causes to be made a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the state or a political subdivision.

* Is a beneficiary of the inadvertent submission of a false claim to an employee, officer, or agent of the state or political subdivision or other recipient of money of this state or political subdivision who subsequently discovers that the claim submitted was false, but fails to disclose the false claim as applicable within a reasonable amount of time after discovery.

This act would not apply to claims, records, or statements that were made under the state's Income Tax Act or statements subject to recovery in a civil action under the Medicaid False Claim Act of 1977.

Prosecuting Authority Investigative Power. If, before beginning an action, a prosecuting authority has reasonable cause to believe that a person has information or is in possession, custody, or control of a document relevant to an investigation of conduct, the prosecuting authority may serve on the person a written demand to do one or more of the following: (a) appear and be examined under oath, (b) produce the document or object for inspection and copying, or (c) answer written interrogatories.

A prosecuting authority could file an action to enforce a demand in the circuit court of the county where the person resides or maintains a principal place of business. A notice of hearing and a copy of all pleadings would have to be served on the person on whom the demand was served. The person could appear in opposition to the action.

If the court finds that the demand is proper and there is reasonable cause to believe that conduct prohibited under the bill may have occurred (or is presently occurring) and the information sought is relevant to an investigation of the conduct, the court would have to order the person to comply with the demand, subject to any modification prescribed by the court. On motion by the person and for good cause shown, the court could enter any order to protect the person from unreasonable annoyance, embarrassment, oppression, burden, or expense.

Any testimony taken, document produced, or answers provided would have to be kept confidential by the prosecuting authority before beginning an action against a person for the conduct under investigation unless federal law requires the disclosure, confidentiality is waived by the person being investigated and the person who testified produced a document or answered interrogatories, or disclosure is authorized by the court.

Private Actions to Recover Losses/Intervention by Prosecuting Authority. Any person could bring an action in the name of the state or a political subdivision to recover losses sustained by the state or political subdivision by any of the prohibited conduct. A court could not dismiss such an action unless the prosecuting authority had been notified and had an opportunity to appear and oppose dismissal. If the opportunity to oppose dismissal is not exercised within 28 days, the opportunity would be considered waived.

If a person other than the prosecuting authority initiates an action, the complaint would be sealed and the clerk could not issue a summons for service on the defendant until the prosecuting authority decides whether or not to take over the action. When the complaint

is filed, a copy must be served on the prosecuting authority, along with disclosure in writing of substantially all material evidence and information supporting the complaint.

Within 90 days after receiving the complaint and disclosure, the prosecuting authority would be required to notify the court and the person initiating the action of one of the following: (1) that he or she will take over the action and have primary responsibility for proceeding with the action or (2) that he or she declines to take over the case and the person initiating the action has the right to proceed.

A person other than the prosecuting authority could not intervene in the action or bring another action on behalf of the state or the political subdivision based on the underlying facts of the action.

A prosecuting authority who elects to proceed with an action through initiation or intervention would have primary responsibility for prosecuting the action and could do all of the following:

- * Agree to dismiss the action, notwithstanding the objection of the person initiating the action, but only if that person has been notified of and offered the opportunity to participate in a hearing on a motion to dismiss.

- * Settle the action, notwithstanding the objection of the person initiating the action, but only if that person has been notified of and offered the opportunity to participate in a hearing on the settlement and if the court determines that the settlement is fair, adequate, and reasonable under the circumstances. On a showing of good cause, the settlement hearing may be heard in camera (in the judge's chambers).

- * Request that the court limit the participation of the person initiating the action. If the prosecuting authority demonstrates that unrestricted participation by the person initiating the action would interfere with or unduly delay the prosecution of the case, or it would be repetitious, irrelevant, or unduly harassing, the court could limit the number of the person's witnesses, limit the length of witness testimony, limit the person's cross-examination of witnesses, or otherwise limit the person's participation in the litigation.

If the prosecuting authority notifies the court that he or she declines to take over the action, the person who initiated the action could proceed with it. However, the prosecuting authority, at his or her request and expense, could be provided with copies of all pleadings filed in the action and copies of all deposition transcripts. In spite of an election not to take over the action, the court may permit the prosecuting authority to intervene at any time on a showing of good cause without affecting the rights or status of the person initiating the claim.

However, if the court determines, after a hearing in camera, that the actions of the person initiating the claim during discovery would interfere with the prosecuting authority's investigation or prosecution of a criminal or civil matter, the court could stay the discovery for not more than 90 days. The court could extend the stay on a further

showing that the prosecuting authority is pursuing the investigation or proceeding with reasonable diligence and that the discovery would interfere with the ongoing investigation.

Alternative Action by Prosecuting Authority. As an alternative, the prosecuting authority could instead pursue damages or a penalty for a prohibited act through any proceeding available, including an administrative proceeding. If the prosecuting authority pursues an alternative proceeding, a person who initiates an action has rights in that proceeding equivalent to the rights the person would have had if the original action had continued, to the extent that those rights are consistent with the law governing the proceeding. Findings of fact and conclusions of law that become final in an alternative proceeding are conclusive on the parties to an action. For purposes of this provision, a finding or conclusion is final if it has been finally determined on appeal, if the time for filing an appeal has expired, or if the finding or conclusion is not subject to judicial review.

Private Party Intervention. A person could bring a civil action in any county in which venue is proper. If the attorney general elects to intervene in an action and the court grants the request, on motion by the attorney general, the court would be required to transfer the action to the Ingham County circuit court. If the prosecuting authority for a political subdivision elects to intervene in an action pending in a judicial circuit or district that is not located in the political subdivision and the court grants the request, on motion of the prosecuting authority, the court must transfer the action to the circuit or district in which the political subdivision is located, as applicable.

Burden of Proof. In actions to reclaim losses, the plaintiff would have the burden of proving all essential elements of the cause of action, including damages, by a preponderance of the evidence. The defendant would be estopped from denying the essential elements of a criminal offense of which the defendant was found guilty, whether by verdict after trial or by plea of guilty or nolo contendere, if the criminal offense included elements of false statement or fraud and if the action involves the same transaction.

Award to Prevailing Private Party. If a person other than the prosecuting authority prevails in an action that person initiates, the court would be required to award the person necessary expenses, costs, reasonable attorney fees, and the following percentages of monetary proceeds resulting from the action or settlement of the claim: if the prosecuting authority intervenes, 15 to 25 percent; if the prosecuting authority does not intervene, 25 to 30 percent.

However, if the court finds an action to be based primarily on disclosure of specific information that was not provided by the person bringing the action, such as information from a criminal, civil, or administrative hearing; a legislative report, an audit, or investigation; or from the news media, and the prosecuting authority proceeds with the action, the court could award the person bringing the action no more than 10 percent of the monetary recovery in addition to reasonable attorney fees, necessary expenses and costs.

Reduction of Award to Complicit Private Party. If the court finds that the person bringing the action planned or initiated the conduct on which the action is brought, the court could reduce or eliminate the share of the proceeds the person otherwise would be entitled to receive. A person who is convicted of criminal conduct arising from a violation of this act could not initiate or remain a party to an action under the act and is not entitled to share in the monetary proceeds resulting from the action or any settlement of the claim.

A person other than the prosecuting authority could not bring an action based on allegations or transactions that are already the subject of a civil action, a criminal investigation or prosecution, or an administrative proceeding to which the state or federal government is already a party. The court would be required to dismiss an action brought in violation of this provision.

No Private Action Based on Public Disclosure. Unless that person is the original source of the information, a person other than the prosecuting authority could not initiate an action based on the public disclosure of allegations or transactions in a criminal, civil, or administrative hearing; in a state or federal legislative, investigative, or administrative report, hearing, audit, or investigation; or from the news media. The person is the original source if he or she had direct and independent knowledge of the information on which the allegations are based and voluntarily provided the information to the prosecuting authority before filing an action based on the information.

State Not Liable for Fees of Private Parties. The state or a political subdivision and the prosecuting authority are not liable for any expenses, costs, or attorney fees that a person incurs in bringing an action under the bill. Any amount awarded to a person initiating an action to enforce this act would be payable solely from the proceeds of the action or settlement.

Award to Defendant. If a person proceeds with an action after being notified that the prosecuting authority has declined to intervene, and the court subsequently finds the claim to be frivolous, the court must award the prevailing defendant actual and reasonable attorney fees and expenses and, in addition, must impose a civil fine of up to \$10,000 on the person who initiated the action. The civil fine would be deposited in the General Fund of the state or political subdivision, as applicable.

Recovery of Costs by the State or Political Subdivision. The prosecuting authority could recover all costs the state or a political subdivision incurs in the litigation and recovery of restitution under the act, including the cost of investigation and attorney fees. The prosecuting authority would deposit the amount recovered into the General Fund of the state or political subdivision, excluding amounts for restitution, court and investigation costs, and fines.

Employer Prohibitions and Sanctions. An employer could not discharge, demote, suspend, threaten, harass, or otherwise discriminate against an employee in terms and conditions of employment because the employee initiates, assists in, or participates in a

proceeding or court action or because the employee cooperates with or assists in an investigation. This prohibition does not apply to an employment action against an employee if the court finds one or more of the following apply: (1) the employee brought a frivolous claim; (2) the employee planned or initiated the conduct on which the action is brought; or (3) the employee is convicted of criminal conduct.

An employer who violates this provision is liable to the employee for all of the following: (1) reinstatement without loss of seniority, (2) two times the amount of lost back pay, (3) interest on the back pay, (4) compensation for any special damages, and (5) any other relief necessary to make the employee whole.

Civil Action Limitations. A civil action could not be filed more than three years after the official of the state or political subdivision charged with responsibility to act in the circumstances discovers the act on which the action is based, or more than 10 years after the act was committed, whichever is later.

An action may be brought for conduct that occurred prior to the effective date of the bill, if the action is filed within the time specified above. An action brought by an employee against an employer for prohibited conduct against the employee could not be filed more than three years after the last act on which the action was based.

Remedies. The remedies provided by the new act are not exclusive and are provided in addition to any other remedies provided in any other law or available under common law. The new act is to be liberally construed and applied to promote the public interest.

BACKGROUND INFORMATION:

The bill is almost identical to House Bill 4773 of last session. The bill passed the House, but failed to see Senate action.

ARGUMENTS:

For:

According to information supplied by Frank, Haron, Weiner and Navarro, a law practice that litigates false claims and whistleblower actions, the bill would allow whistleblowers to bring suits under seal in the name of the state or a local unit of government (known as *qui tam* actions) against parties who have committed fraud against a state or local unit program, agency, and so on. The attorney general or local prosecuting authority (e.g., city attorney or county prosecutor) would retain the right to take control of the case; if they decline to intervene, the person initiating the action can continue on his or her own. The state or local unit can also initiate an action under the bill. If successful, the remedies include triple damages and civil penalties that in effect make the state or local unit "whole" for the costs of investigation, lost interest, and whistleblower awards on top of what was taken by fraud. The bill would also provide an award to the whistleblower who initiated an action of between 15 and 30 percent, depending on the circumstances of

the case, for instance, the value of the information provided by the whistleblower in successfully litigating the case.

The bill would provide valuable protections to whistleblowers. This is needed as often only insiders have access to the types of documentation that can prove fraud. These brave individuals need to know that their jobs and seniority will be protected from employer retaliation. On the other hand, the bill would also discourage frivolous claims by disgruntled employees; false claims attorneys only take a case if they believe the case is winnable (which means a substantial body of evidence pointing to fraud must be presented to the attorney), and, if the case is dismissed by a court as frivolous, the whistleblower (or governmental entity) bringing the action has to pay the defendant's reasonable attorney's fees and expenses.

The bill is important as the state and local units of government contract out millions of dollars a year on various public services. Though most contractors and vendors are honest and reputable, fraud happens. The bill is especially needed now, as federal stimulus dollars will soon arrive and public projects will ramp up quickly so to get state residents working again. Quick enactment of the bill would discourage potential bidders on those public jobs from taking advantage of the situation to pad their own pockets. In addition, because the bill would provide a retroactivity clause that would apply to conduct occurring before the bill's enactment within the specified limitation, a private citizen, the state, or local prosecuting authority could take on those who do.

In short, the bill represents good governance by protecting taxpayers' money from fraud and abuse and gives important protections to employees who expose their employers' fraudulent business practices against public agencies.

POSITIONS:

The Office of Attorney General indicated support for the bill. (3-11-09)

A representative of Frank, Haron, Weiner and Navarro, Attorneys at Law, testified in support of the bill. (3-11-09)

The Michigan Association for Justice indicated support for the bill. (3-11-09)

The Michigan Infrastructure and Transportation Association indicated opposition to the bill. (3-11-09)

Legislative Analyst: Susan Stutzky
Fiscal Analyst: Ben Gielczyk

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.