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LEGAL REMEDIES FOR GRAND CORRUPTION

Lessons from Qui Tam Litigation in the United States

David Kwok
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This paper is the third in a series examining the challenges and opportunities facing civil society groups that seek to develop innovative legal approaches to expose and punish grand corruption. The series has been developed from a day of discussions on the worldwide legal fight against high-level corruption organized by the Justice Initiative and Oxford University's Institute for Ethics, Law and Armed Conflict, held in June 2014.

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Introduction

Qui tam litigation is a distinctive form of private litigation, allowing a private party (known as a "relator") to sue "on behalf of the king,"[1] or the government. In the United States, qui tam litigation today exists primarily under the False Claims Act, a statute forbidding fraud against the federal government. If a private party discovers that a company has been defrauding the federal government, the private party can litigate against the company and receive a share of the penalties. Qui tam actions have been credited with tremendous growth in prosecutions for fraud.

As this chapter will lay out, the history of qui tam in the United States reveals that the overall success of the legislation rests on a few key ingredients. First, the U.S. system relies heavily upon a well-developed, responsible executive branch of government to handle prosecution. The fate of private litigation, in which whistleblowers bring litigation in cases where the government has not decided to pursue public prosecution, suggests the crucial importance of this role. Second, it relies on a cooperative private bar. Third, the independent and predictable U.S. judiciary maintains the division of responsibility between federal prosecutors and private litigants and provides an independent check on government behavior.

The chapter will go on to propose improvements over the U.S. system that would be likely to support the success of a qui tam system in the absence of the ingredients that have been crucial in the United States. These largely consist of supporting whistleblowers by reducing the uncertainty they face and providing them greater anti-retaliation protection.

History also suggests that countries should have modest expectations for growth in qui tam litigation, once instituted; even with a prior well-established civil litigation system, it may take five to ten years to see a substantial volume of qui tam cases.

The History of Qui Tam in the United States

Reflecting the influence of British common law, the United States has a long history of private enforcement of law, and qui tam litigation is one of the set of tools.[2] The early British common law system focused almost exclusively on private litigation—there was no public prosecutor or government police force. For example, if a shopkeeper found herself the victim of a robbery, she would have to investigate and pursue the robber herself. This reliance on private litigation resulted in under-

[1] "Qui tam" is short for a longer Latin phrase, "qui tam pro domino rege quam pro se ipso in hac parte sequitur," which translates to "who as well for the king as for himself sues in this matter." Black's Law Dictionary (10th ed. 2014).

[2] For historical background, see J. Randy Beck, *The False Claims Act and the English Eradication of Qui Tam Legislation*, 78 N.C. L. Rev. 539 (2000); John Langbein, *The Origins of Adversary Criminal Trial* (2003).

enforcement; victims were either ineffective or insufficiently motivated to pursue offenders. The presence of unpunished offenders was an ongoing risk to the public. One response to this under-enforcement was qui tam litigation, rewarding private parties who would aid the king by pursuing offenders. Qui tam litigation was available in both courts of "law" and courts of "equity"—what would today be known as criminal and civil litigation.

The United States did not adopt qui tam litigation as broadly as the British. Most of the modern U.S. experience stems from the False Claims Act (FCA), a statute addressing fraud against the federal government. The False Claims Act was originally passed in 1863 during the American Civil War, when concerns about private companies selling sawdust labeled as gunpowder to the Union army prompted passage. The provision gives relators incentive to act as private enforcers, because they receive a minimum percentage of the penalty fraudulent military suppliers paid to the federal government. The guidelines for imposing penalties in the statute put them at treble the damages.

The FCA permits both civil and criminal sanctions, but the qui tam provisions apply only to civil sanctions; a relator cannot file criminal charges. If the government intervenes in a qui tam case, however, it may choose to bring criminal charges in addition to the civil sanctions.

Modern FCA Procedure

Today, any person can file a qui tam suit against a defendant; the courts stay and seal all qui tam actions immediately upon initial filing. Neither the public nor the defendant knows of the filing, and the lawsuit cannot progress until the federal government reviews it. By statute, the government has sixty days to investigate and make a decision regarding intervention. As a practical matter, courts routinely grant the government time extensions. The government typically requires over a year to investigate.

If the federal government chooses to intervene, it takes over the lawsuit and handles the litigation. The government intervenes in roughly a quarter of qui tam cases. The relator receives a portion of the final penalties against the defendant but has the sole role of witness in the case.

If the federal government declines to intervene, the statute permits it to unilaterally dismiss the lawsuit and foreclose any relator action, but it rarely exercises that power. In the absence of either action by the federal government, the relator can proceed with her lawsuit against the defendant. If she attempts to settle or dismiss the action, she must obtain government consent.

The original FCA did not give the federal government as much power as it has now. This primacy of Department of Justice (DOJ) choice came about because the U.S.

Congress became suspicious of abusive qui tam tactics. In the mid-twentieth century, a relator filed a qui tam action based on information that the DOJ already knew and was utilizing in a criminal action. The relator was not disclosing new allegations or information against the particular defendant. Congress revised the FCA to foreclose such parasitic cases, requiring relators to provide information that the government did not already know.

The FCA fell into disuse. The revisions made it too difficult for relators to file qui tam actions. The federal government possessed a tremendous amount of information, and it was easy for defendants to secure dismissals of qui tam actions based on evidence that someone within the federal government had prior knowledge of the alleged fraud. Congress amended the FCA to help address some of these problems by reducing the restrictions on relators.

The present system still follows the primacy of provision of information. First, the FCA still prohibits qui tam actions based solely on information that the government is already using in litigation against a defendant, and it also prohibits qui tam actions based upon publicly disclosed information. For example, an individual learning about corporate wrongdoing on a public news program cannot file a qui tam action against that corporation. It also prohibits qui tam actions based upon government reports or hearings, except if the relator herself discovered the wrongdoing and informed the government report or media.

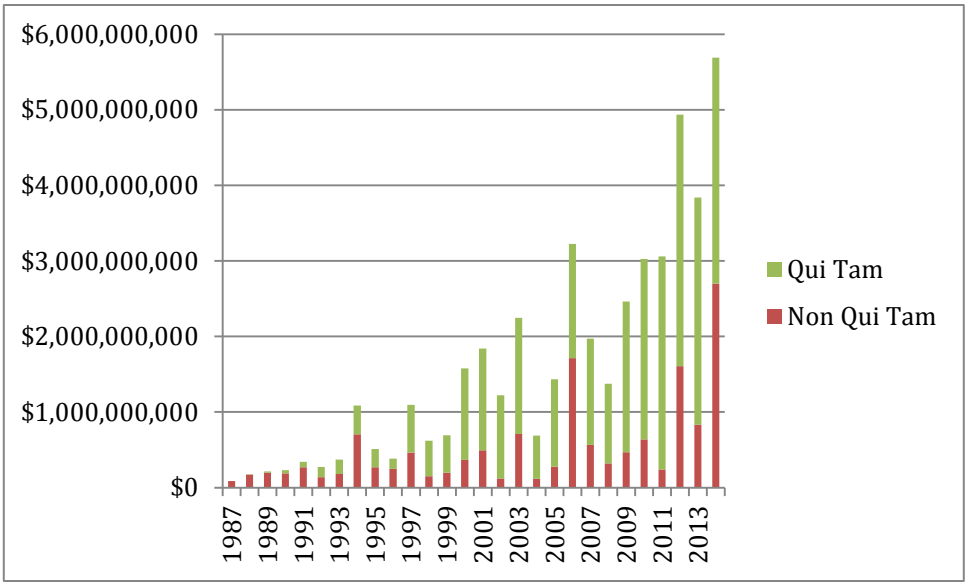
Relators can receive as much as 30% of the civil recovery, which can be substantial given the treble damages provisions in the statute. Civil penalties also include $5,500 to $11,000 in fines per false claim. So, if a court determines that a defendant's fraud resulted in $3 million in damages, which trebled is $9 million, and levied $1 million in fines for a total of $10 million, the relator could receive as much as $3 million. Contrary to qui tam's beginnings in defense contractor fraud cases, the majority of qui tam cases today center on government-provided health insurance—that is, Medicare and Medicaid fraud. One possible explanation is that government healthcare spending has grown tremendously, thus increasing the opportunity for fraud. A separate potential explanation is that the healthcare industry is more fragmented and competitive than the defense industry. Consolidation in the defense industry may make defense employees more cautious in becoming a whistleblower or relator, as they may fear an inability to obtain future related employment. In contrast, the fragmented healthcare industry has numerous potential employers, and whistleblowers may be more confident in their ability to find future employment.

Effectiveness of the U.S. System

Measured by dollar recoveries, U.S qui tam litigation under the FCA appears successful. In the past few fiscal years, qui tam litigation has led to approximately $3

billion in FCA recoveries per year, generally dwarfing non–qui tam recoveries under the FCA.[3]

FCA Settlements and Judgments in USD (non–inflation adjusted) by fiscal year



The FCA qui tam process also appears to be a success from a cooperation perspective. One concern about private enforcement is the possibility that public enforcement could decline in response—government agents might slack or be reassigned. However, the evidence suggests that government agents are heavily invested in successful cases and are not reducing efforts to identify fraud in response to relator efforts.

The fact that roughly 95% of non-intervened cases fail to obtain any recovery suggests the important role of the federal government in making qui tam legislation successful. Private, independent litigation against defendants is in fact highly unsuccessful.

The reasons for this disparity in effectiveness have not been resolved. Relators' attorneys often advise clients to dismiss a case if they are unsuccessful in obtaining government intervention, so no jury looks at the facts, leaving us with virtually no evidence as to case quality. One possibility is that the government intervenes in all of the good cases; thus, the remaining cases are of poor quality and we should not be surprised that most of those remaining cases fail to recover anything. A second possibility is the remaining cases are of good quality, but they are more difficult and

[3] See http://www.justice.gov/civil/pages/attachments/2014/11/21/fcastats.pdf. For more empirical evaluation, see David Kwok, *Does Private Enforcement Attract Excessive Litigation? Evidence from the False Claims Act*, 42 Pub. Cont. L. J. 225 (2013); David Engstrom, *Harnessing the Private Attorney General: Evidence from Qui Tam Litigation*, 112 Colum. L. Rev. 1244 (2012).

the government as well as the relator's attorney recognize this and do not litigate the case. Another possibility is that the negotiating power of the federal government is driving the success—because the federal government has such great leverage against private businesses, businesses feel compelled to settle cases in which it has intervened. Therefore, government intervention itself, rather than case quality or difficulty, determines outcomes. The private cases may have merit, but the defendants do not fear private litigants and therefore refuse to settle. A fourth possibility is that courts draw strong negative inferences from the fact that the government did not intervene, thus making non-intervened cases more difficult procedurally, even if their factual basis is still strong.

Apart from the known problem that private cases find little success, the evidence of success is limited in many ways. As with most white-collar offenses, there is little information available regarding underlying offense levels. For example, if the overall levels of fraud against the federal government have been rising since 1986, the rise in FCA actions since 1986 might follow that trend. We therefore have little insight as to whether the FCA is successfully reducing levels of fraud against the federal government under a deterrence theory.

Moreover, nearly all FCA cases involve settlements or dismissals; only a few go to trial each year, even if the government intervenes. As a result, we have very little independent evidence of the quality of most qui tam cases. There have been allegations that some settlements are actually sweetheart deals in which the government levies a light fine against serious fraud because of the importance of the company. There is also evidence that the government does not make intervention decisions based solely on the merits of the case.

Without independent evaluation, perhaps the largest empirical challenge involves the legitimacy of non-intervened cases. These cases constitute the majority of qui tam cases. If most of the cases concern real wrongdoing, the qui tam system is failing to address those cases. If most of the cases are meritless, relators may be causing the government to spend substantial time and resources on wasteful investigations. Overall, the qui tam provisions of the FCA appear to be successful in encouraging relators to bring information to the government, and the government has been extracting increasingly more settlement dollars from defendants based on such information.

Conditions Leading to the U.S. Success

I. A Strong Executive Branch

Any enforcement regime allowing multiple potential enforcement paths generates the potential for conflict. What determines whether private or government enforcement takes precedence?The U.S. qui tam system gives government absolute precedence. The Department of Justice (DOJ) has the right of first refusal over any

qui tam action. It can halt any action, and must approve any settlement reached between the relator and the defendant, a measure that reduces the potential for collusive settlements that are not in the public interest. This system would not work if the DOJ could not be trusted to pursue the public interest; thus, it rests on a strong and incorrupt executive branch. As the U.S. has not recently followed any alternative rule, it is difficult to evaluate whether any other system would be superior. For example, if federal prosecutors may fail to prosecute wrongdoing, the present primacy of DOJ decisions is likely to be unhelpful. Alternatives include a system with greater trust in the judicial system, which would allow courts to decide the merits of a relator's case rather than emphasizing executive branch oversight of the case. Another option would be a first-to-file rule: whichever party first brought litigation against a particular defendant would be in charge. Relators could also have greater flexibility. Thus, if a government report reveals wrongdoing, but the executive branch fails to prosecute the wrongdoer, the legislature could rely on relators to prosecute.

II. A Cooperative Private Bar

Attorneys specializing in representing relators have been vital in ensuring that meritorious cases reach the federal government. While these attorneys do not independently prosecute cases, the U.S. federal government relies on these private attorneys to investigate and filter them. People who learn of wrongdoing by their employer may feel moral indignation, but attorneys are critical in translating the indignation or suspicion into a legal claim that the government and courts will recognize. Attorneys are also important in helping relators understand the types of evidence needed to convince a court or government prosecutor to take action. Some U.S. courts have permitted relators to file qui tam actions without the benefit of attorneys, and those relators' efforts have been particularly unhelpful and unsuccessful.

Cooperative private attorneys are also important because of their ability to help shape the boundaries of proscribed behavior through judicial decisions. For example, under the FCA, fraud is not a fully defined concept. Some forms of fraud are readily known: for example, a healthcare provider defrauds the federal government when it bills the federal government without providing any actual treatment. But when a healthcare provider bills the federal government and provides effective medical treatment, but an unauthorized physician supervises the treatment, the question of fraud is less clear. Private attorneys help identify unclear cases.

Relators have responded to the complications in identifying fraud by filing claims that apply pressure upon courts to determine the proper boundary between regulatory violations and fraud under the FCA. Large companies commit a variety of regulatory violations, and due to qui tam litigation, courts must decide when a regulatory violation constitutes fraud against the federal government. For example, relators helped increase the scope of the FCA by bringing a case against a pharmaceutical company for its marketing efforts to physicians, successfully claiming

that such improper marketing eventually led to fraudulent government payment for drugs.[4] Relator litigation has also narrowed the scope of the FCA (e.g., the determination that deliberate false identification of an unapproved physician supervisor in a Medicare bill does not constitute fraud under the FCA).[5] Private attorneys thus have a key role in determining how the lawsuits brought to trial shape such precedents. While the government might make strategic decisions about difficult cases, refusing to intervene in cases that have an untested theory of fraud because of other facts that might cause a court or jury to hesitate, private attorneys can nonetheless press such cases. Losing such a case might establish negative precedent undesirable to the government, but private attorneys and relators nonetheless have the ability to press them.

A cooperative private qui tam bar is also important to the success of the U.S. system in that the FCA grants the reward to the first to file in federal court. Subsequent relators who make similar allegations against the defendant are not entitled to any reward. As a practical matter, however, the attorneys who specialize in representing relators recognize the added value of subsequent relators who can strengthen the case against the common defendant. These attorneys have been known to make side agreements to cooperate and share rewards even though they are not the first to file. This produces better results than filing mill behavior in which relators' attorneys pursue a high volume of low-quality cases, betting on the odds that they will be first. The statute could permit such behavior; the cooperation of the public bar has been crucial in preventing it.

III. An Independent, Procedural Judiciary

The FCA qui tam system, at least early in any individual case, requires little involvement from the judiciary. Courts must be sufficiently independent and reliable in reporting new qui tam actions to the DOJ, but courts do not conduct initial evaluation of a claim's merits. Given that the executive branch handles the merits of qui tam claims first, and most cases settle out of court if the relator doesn't drop them, the judiciary has a modest role in the U.S. system. Many defendants claim that the executive branch's unilateral power to cut off suspected fraudsters from further government contracts or payments, in itself, is sufficient to pressure defendants into settlements. If a defendant's ongoing business is highly dependent upon government business, loss or delays of potential future government revenue may be catastrophic. Of course, settlements are made in the shadow of judicial decision-making; parties consider what courts would otherwise do before reaching a settlement agreement. Nonetheless, perhaps the immediate power of the executive branch in negotiation is sufficient to offset at least mild levels of potential judicial bias in favor of defendants. Evidence suggests the judiciary may be playing a negative role in the failure of non-intervened U.S. qui tam cases. For example, U.S. civil litigation is generally known for

[4] *See* U.S. ex rel. Franklin v. Parke-Davis, Div. of Warner- Lambert Co., 147 F. Supp. 2d 39 (D. Mass. 2001).

[5] *See* U.S. ex rel. Hobbs v. MedQuest Assocs., Inc., 711 F.3d 707 (6th Cir. 2013).

expansive discovery powers in which plaintiffs can force testimony and evidence from defendants. But courts have upheld higher pleading standards for qui tam cases, making it more difficult for non-intervened relators to move past the initial stage and obtain discovery. The DOJ has powers similar to discovery that it can exercise prior to the court's application of initial pleading standards, so this judicial requirement only applies to private cases. Thus, the U.S. judiciary may not be as impartial and independent as would be ideal for a successful system, but a country with a significantly less effective judiciary could expect less success than the United States has had.

Alternative Qui Tam Models

Any country considering the adoption of qui tam should consider a number of potential improvements over the U.S. system, especially if it may lack some of the attributes that have contributed to the success of the U.S. system. This section draws on protections in whistleblower programs, not least because the U.S. system functions in a way that largely resembles such programs. The suggestions are aimed at addressing relator uncertainty: about payment for their efforts, and about retaliation after their decision to litigate.

I. Compensating Criminals Who Come Forward

The FCA does not permit anyone convicted of criminal wrongdoing to receive a percentage of the reward. This law certainly speaks to the public's distaste for rewarding a wrongdoer—especially one who has already benefited from criminal acts. But many potential whistleblowers may have some level of culpability for the wrongdoing they would otherwise report. In addition to encouraging wrongdoers to come forward with information, such rewards would deter crime among individuals who recognize their co-conspirators' incentive to report. In cases where no parties aware of the wrongdoing have fully clean hands, society may benefit from a qui tam program that does not prohibit rewards to criminals. The benefits of offering leniency in antitrust/cartel conspiracies are well known.[6] Given the difficulty in breaking up secret conspiracies, allowing a reward in addition to non-prosecution may be in society's best interest.

I. Setting Reward Amounts

Establishing optimal compensation under a qui tam system is a complex question that is beyond the scope of this paper. Policymakers have competing values and purposes that make such a calculation challenging at best: how harmful is the offense, and how much effort should society put into combating the offense? Does a high payout provide incentive for difficult cases, or does it attract frivolous litigation?

[6] See OECD Policy Brief, *Using Leniency to Fight Hard Core Cartels*, *OECD Observer* (September 2001), available online at http://www.oecd.org/daf/competition/1890449.pdf.

That being said, the U.S. FCA experience helps illustrate some basic parameters. First, establishing a minimum percentage appears to have some importance in a functional qui tam regime. Prior to 1986 when the minimum was set at 15%, a relator could receive a 0% reward. While other challenges were eliminated in 1986 as well, this possibility may well have significantly discouraged. While, as noted above, those convicted of a crime can still receive nothing, most relators receive 15–25%. This example suggests that 15% may be a useful minimum.

Countries creating new systems may also want to look beyond the percentage payment system, which also creates challenges as to proper valuation of the offense. The FCA is crafted to award compensation in two forms. The first is compensation as damages: determining the loss to the government due to the fraud, and having the defendant pay a corresponding amount. This calculation can be difficult when evaluating the proper harm resulting from some types of fraud. For example, a court agreed that a government contractor defrauded the government by claiming to be a qualifying small business when it was not. Nonetheless, the defendant contractor otherwise successfully produced the contracted data-processing facility, and the court was challenged as to proper damages, because the government "got essentially what it paid for."[7] Separately, the FCA provides for a "per claim" penalty: for every false claim a defendant makes, there is a fixed-dollar penalty. This system raises concerns about whether such fixed amounts properly correspond to the harm.
A more general concern with qui tam litigation is the availability of funds for a reward. Under the FCA, while the government "pays" the relator, in reality, the government delivers a share of its recovery from the defendant. Thus, if the defendant does not pay, the relator does not receive anything from the government. This creates a strong incentive for relators to target defendants that actually have the capability to pay ("deep pockets"), and there is little incentive to go after wrongdoers that do not have assets or other capacity to pay fines. This differs from many other information-reward programs in which informants receive a fixed payout from the government regardless of the defendant's own ability to pay. Other countries may wish to create systems that circumvent this problem.

II. Determining the Timing of Payment to Relators

Under the FCA model, payment to the relator is not established until after the primary litigation is resolved. Thus, the relator and the government first work together to prosecute the defendant. Once there is a successful resolution with the defendant, the relator proceeds to negotiate with the government for payment. Some relators have alleged that defendants and the government work together to minimize the relator's payment.

This model allows the government to fully evaluate the relator's role in litigation before determining her reward. If a relator has been helpful throughout the litigation

[7] *See* Ab-Tech Const., Inc. v. United States, 31 Fed. Cl. 429, 434 (1994).

process, the government has the full opportunity to observe and then reward the relator for her assistance. It also allows the government to fully evaluate the harm and the wrongfulness of the defendant's behavior. To the extent that evaluation should come to bear on the relator's share, this can be useful.

The tradeoff, however, is that the relator essentially relies upon the goodwill of the government throughout the litigation process. After a lengthy litigation process, it may be difficult for the relator to suddenly take on an adversarial role against the government in negotiating or litigating for a larger share of the recovery. Moreover, lack of prior certainty about the percentage reward may make it difficult for attorneys and relators to decide whether a case is worthwhile before filing. Uncertainty may depress reporting as well.

III. Prevention of Retaliation

Relators have private information about wrongdoing; in the U.S. context, relators typically have information about their employer's wrongdoing. Revealing this wrongdoing places them at direct risk of retaliation by the employer. The FCA has an anti-retaliation provision, but relators must sue their employers to enforce this provision. The government typically does not intervene to provide aid. Countries creating their own qui tam systems could have government prosecutors prioritize litigation against companies that retaliate. We have little systematic data as to the success of the FCA's anti-retaliation provisions, but anecdotal evidence suggests that significant numbers of qui tam actions come from former employees rather than current employees, suggesting that current employees fear retaliation too much to come forward.

A qui tam system could also protect relators by hiding their identities. Disclosure is likely inevitable if the government decides to pursue litigation, since companies can similarly conduct investigation to determine who had access to incriminating evidence. If, however, the government chooses not to intervene in a case, its present policy is still to unseal and disclose the identity of the relator even if she does not want to proceed with litigation. At least one state, New York, does not follow such a policy and instead protects the relator's identity if so desired. Protecting the relator's identity, at least in a case that does not go forward, would encourage whistleblowers to come forward.

Conclusion

Qui tam litigation has been successful as a whistleblower program in the United States, but it has been unsuccessful as an independent private enforcement system. Countries without strong, effective public prosecution and independent courts should be wary of drawing any lessons from the success of the U.S. model.
If countries with good public prosecution and independent courts choose to use the U.S. qui tam system as a model, they might consider providing greater reward

certainty and protections for whistleblowers in comparison to the U.S. system: private whistleblowers can offer useful information to public prosecutors, and they can use courts to provide accountability over public enforcement efforts. Finally, countries experimenting with qui tam should have modest expectations about results. Measuring the volume and proportion of litigation that results in convictions and/or penalties is a reasonable method of evaluating success, but the results of a system will not be available for at least five years, not least because cases take more than a year to resolve. The mature system in the United States only achieves penalties in roughly 25% of cases, and countries implementing new systems should expect more modest results for a period.

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