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The Tar Heel State Steps Up Its Fight Against Fraud

Since the passage of the North Carolina False Claims Act in 2009, which became effective Jan. 1, 2010, North Carolinians have had a powerful weapon to combat fraud against their tax dollars and to return these funds to the state coffers. At the time it was passed, North Carolina joined 25 other states and the District of Columbia by enacting its own False Claims Act.

Marc S. Raspanti, Pamela C. Brecht and James F. Wyatt

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Editor's note: This is the first of two articles about North Carolina's False Claims Act.

Since the passage of the North Carolina False Claims Act in 2009, which became effective Jan. 1, 2010, North Carolinians have had a powerful weapon to combat fraud against their tax dollars and to return these funds to the state coffers. At the time it was passed, North Carolina joined 25 other states and the District of Columbia by enacting its own False Claims Act.

The North Carolina Medical Assistance Provider False Claims Act, a narrower predecessor to the N.C. FCA that specifically applies to the presentation of false claims by providers of medical assistance under the North Carolina Medical Assistance Program, is still in effect.

Like the Federal False Claims Act upon which it is modeled, the North Carolina False Claims Act is designed to deter and punish those who make false or fraudulent claims for payment by the state and to provide powerful incentives for whistleblowers. In addition to imposing penalties of $5,500 to $11,000 for each false claim submitted to the state and treble damages against wrongdoers, the N.C. FCA contains a qui tam provision allowing private citizens with knowledge of fraud against the state to file suit on behalf of the state and to receive between 15 and 30 percent of the amount recovered from the fraudster as a reward.

The federal FCA has been the federal government's single most powerful tool to combat fraud and waste against the public fisc. Since the federal FCA was amended in 1986, more than $30 billion has been recovered from those who sought to fraudulently profit from taxpayer dollars. It has been used to expose every type of scheme affecting federal funds, including health care, contracting, defense, disaster relief and education fraud.

The federal FCA was strengthened in 2009 by the Fraud Enforcement and Recovery Act (FERA) and again in 2010 by the Patient Protection and Affordable Care Act (PPACA). These acts include amendments that expanded qui tam relators' rights and clarified often-conflicting circuit court interpretations of many of the federal FCA's key provisions. This emboldened federal FCA has resulted in greater recoveries of taxpayer funds.

According to the Department of Justice, in 2010 alone, the U.S. government recovered $3 billion under the qui tam provisions of the FCA. Overall, the public-private partnership embedded in the federal FCA to combat the rampant fraud, waste and abuse against federal taxpayers has ensured this unprecedented success.

The purpose of this article is to guide practitioners concerning some of the key similarities and differences between the federal FCA and the N.C. FCA. While the N.C. FCA can also be used as a very powerful weapon to combat fraud committed on the state of North Carolina, practitioners should, however, be mindful of the differences between the two statutes that are discussed herein.

Given the effectiveness of the federal FCA in both deterring fraud and recovering taxpayer funds from wrongdoers, various states followed suit in enacting their own false claims statutes, many with qui tam provisions. In 2005, Congress provided states with an added incentive to pass their own versions of the FCA — a 10 percent bonus. The Deficit Reduction Act included provisions aimed at incentivizing state governments to pass false claims acts with robust qui tam provisions. Through the DRA, Congress pledged that when a state has a false claims act that was "at least as effective" as the federal FCA in facilitating and rewarding qui tam actions, the federal government would share 10 percent of any federal Medicaid false claims recovery with the state.

Additionally, to receive this bonus, the state FCA must also establish liability to the state for fraudulent claims with respect to Medicaid spending, contain a civil penalty that is not less than the penalty under the federal FCA, and contain a requirement for filing a case "under seal for 60 days with review by the state attorney general." This DRA bonus serves as a powerful incentive for states to pass their own qui tam false claims acts.

In keeping with the state movement toward robust false claims acts, the North Carolina Legislature passed a false claims statute in 2009. Unfortunately, on March 21, 2011, the Department of Health and Human Services (HHS) found the current N.C. FCA to be "not as effective in rewarding and facilitating" potential whistleblowers as the federal FCA. This article analyzes the rationale for this decision, as well as other differences and similarities between the federal FCA and the N.C. FCA.

The North Carolina False Claims Act

While the N.C. FCA mirrors the federal FCA in many respects, there are important differences that lawyers should be aware of that have significant implications for bringing a case under the N.C. FCA. The N.C. FCA mirrors the federal FCA in many respects. The language of the liability provisions for the federal FCA and the N.C. FCA are virtually identical, and both laws provide for the same measure of damages. In addition, the award structures for qui tam relators and key definitions (i.e., "knowing," "material" and "obligation") are the same under both statutes. Like the federal FCA, the N.C. FCA also contains a strong anti-retaliation provision, which affords redress for North Carolina whistleblowers who are fired, demoted or otherwise retaliated against for blowing the whistle on their employer or a government contractor. Additionally, the N.C. FCA specifically states that it should be interpreted in a manner consistent with the federal FCA, including its amendments.

Despite the great similarities between the federal FCA and its North Carolina counterpart, there are differences between these statutes in a number of significant areas. Through two letters issued to the director of the Medicaid Investigations Unit of North Carolina's Department of Justice, the HHS has highlighted five provisions of the N.C. FCA thought not to be as effective at incentivizing qui tam suits as the federal FCA: the public disclosure bar; the original-source exception; the first-to-file provision; the public employee limitation on qui tam suits; and the lack of a clear statute of limitations on anti-retaliation actions. Additionally, several other provisions, though not raised by HHS, may also impact the overall strength of the N.C. FCA. These will be addressed in greater detail below.

The Public Disclosure Bar

The N.C. FCA's public disclosure provision is both broader and more stringent than the federal version. Under the federal FCA, a court shall dismiss an action or claim, unless opposed by the government, if substantially the same allegations or transactions as alleged in the claim were publicly disclosed: (1) in a federal criminal, civil or administrative hearing in which the government or its agent is a party; (2) in a congressional, Government Accountability Office or other federal report, hearing, audit or investigation; or (3) by the news media, unless the action is brought by the attorney general or a person who is an original source of the information.

By contrast, the N.C. FCA does not allow the state of North Carolina to oppose a defendant or court's dismissal of a case based on its public disclosure bar. It also includes a broader definition of what constitutes a public disclosure.

More specifically, the N.C. FCA includes as public disclosures hearings in which the government was not a party. In qui tam litigation, the public disclosure bar was intended to block parasitic lawsuits based on public information obtained by those who contributed nothing to exposing the so-called fraud, but should also allow meritorious suits to continue. To achieve this important balance, the federal FCA specifically delineates what constitutes a public disclosure and allows the government to oppose a court's dismissal of a case based on the public disclosure bar. Thus, North Carolina's public disclosure bar may prove to be a roadblock to potential whistleblowers, and therefore, a deterrent to the filing of meritorious qui tam suits.

The Original-Source Exception

The original-source exception to the public disclosure bar permits a relator to proceed, even if there is a public disclosure, if the relator qualifies as an original source. North Carolina's original-source exception to the public disclosure bar is narrower than its federal counterpart.

Under the N.C. FCA, an individual is an "original source" of publicly disclosed allegations if that individual has "direct and independent knowledge" of the information on which the allegations are based and has "voluntarily provided the information to the state" before filing an action based on that information. Prior to 2010, the federal FCA had a nearly identical original-source exception as the N.C. FCA, but in 2010 the federal FCA was amended. The federal FCA now provides that an individual need only have "knowledge that is independent of and materially adds to the publicly disclosed allegations or transactions" to qualify as an "original source." This provision moderates a potentially unforgiving and previously contentious public disclosure bar. The N.C. FCA lacks the relaxed standard of the federal FCA and may not, therefore, be as effective in incentivizing qui tam suits. •

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The Tar Heel State Steps Up Its Fight Against Fraud — Part II

North Carolina's False Claims Act has a more stringent "first-to-file" provision than its federal counterpart. The federal False Claims Act's first-to-file provision is intended to prevent potential relators from filing parasitic suits based on the same allegations that underlie an already pending qui tam suit.

Marc S. Raspanti, Pamela C. Brecht and James F. Wyatt

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Editor's note: This is the second article in a two-part series discussing North Carolina's False Claims Act. The first article discussed the Federal False Claims Act and its state counterpart as passed by the legislature in North Carolina.

North Carolina's False Claims Act has a more stringent "first-to-file" provision than its federal counterpart. The federal False Claims Act's first-to-file provision is intended to prevent potential relators from filing parasitic suits based on the same allegations that underlie an already pending qui tam suit. Thus, under the federal FCA, when a relator brings a qui tam action, only the government may intervene or bring a related action on facts underlying that qui tam action.

The N.C. FCA is stricter than the federal FCA, however, and prohibits persons other than the state from intervening or bringing a related action based on the facts underlying a pending N.C. FCA action, federal FCA action or an action based on any similar provision of law in any state. Thus, the first-to-file bar could be more of a hindrance to potential relators under the N.C. FCA than under the federal FCA.

Public Employee Limitation

The N.C. FCA also includes a major departure from the federal FCA because it limits the scope of qui tam matters that can be brought by public employees. Specifically, the N.C. FCA bars public employees or officials from filing FCA suits if the allegations of the suit are based substantially upon allegations of wrongdoing or misconduct that (1) such person had a duty or obligation to report or investigate within the scope of his or her public employment; or (2) information or records to which the person had access to as a result of his or her public employment or office.

In contrast, the federal FCA does not prevent public employees from being relators, even if those employees had a duty or obligation to report misconduct to their employer. By barring an entire class of potential relators from filing suits, the N.C. FCA is less effective than the federal FCA in encouraging and incentivizing qui tam suits.

Anti-Retaliation Provision

Both the N.C. FCA and the federal FCA protect relators with anti-retaliation provisions. However, the Department of Health and Human Services also found the N.C. FCA to be less protective than the federal FCA because it lacks an explicit statute of limitations period for anti-retaliation claims.

Although the N.C. FCA contains an anti-retaliation provision that is nearly identical to the federal FCA, it lacks the federal FCA's three-year statute of limitations. The North Carolina Legislature omitted a specific statute of limitations for N.C. FCA anti-retaliation claims. Accordingly, whistleblowers must rely on the most analogous North Carolina statute of limitations provision.

Applying this standard would not pose a disincentive to N.C. FCA whistleblowers, however, because a three-year statute of limitations under §1-52(5) applies to wrongful discharge actions. This is identical to the post-amendment version of §3730(h), which specifies that claims for retaliation have a three-year statute of limitations. Thus, as applied, the N.C. FCA is "as protective" as the federal FCA. Respectfully, HHS was mistaken on this point.

Despite its lack of an explicit statute of limitations for anti-retaliation actions, the N.C. FCA is actually more protective of potential whistleblowers than the federal FCA. Under §1-613 of the N.C. FCA, "any employee, contractor or agent who is discharged, demoted, suspended, threatened, harassed or in any other manner discriminated against in the terms and conditions of employment because of lawful acts done ... in furtherance of an action under the article or in furtherance of other efforts to stop one or more violations of G.S. §1-607 ... shall be entitled to all relief necessary to make the employee whole." Additionally, North Carolina's Medicaid Anti-Fraud statute's anti-retaliation provision, which pre-dates the passage of the N.C. FCA, is also incorporated by reference into the N.C. FCA.

Employees who are discriminated or retaliated against in violation of the N.C. Medicaid statute may bring an action under the N.C. FCA for violations of the N.C. Medicaid statute, which predates the passage of the N.C. FCA. By adopting a strong anti-retaliation provision, the state of North Carolina removed a major intimidating influence on potential relators — the fear of being fired, demoted, harassed or discriminated against by their employer for blowing the whistle.

There is no meaningful difference between the anti-retaliation provision of the N.C. FCA and §3730(h)(1) of the federal FCA. Section 1-613 of the N.C. FCA protects employees or others acting in furtherance of both "an action under this article" and "other efforts to stop one or more violations." The federal FCA protects potential whistleblowers engaged in "lawful acts ... done in furtherance of efforts to stop one or more violations." Presumably, the N.C. FCA's "furtherance of an action" and "other efforts" would encompass "lawful acts" referred to in the federal FCA.

In addition, the relief available to an employee under the N.C. FCA is identical to that available under §3730(h)(2) of the federal FCA: two times the amount of backpay and interest on the backpay; reinstatement with the same seniority status; and compensation for any special damages, including litigation costs. Furthermore, North Carolina's Medicaid Anti-Fraud statute's anti-retaliation provision, which predates the passage of the N.C. FCA, is also incorporated by reference into the N.C. FCA. The N.C. FCA allows actions to be filed based on acts committed prior to Jan. 1, 2010, if that action would have been covered under the North Carolina Medical Assistance Provider False Claims Act and if the applicable statute of limitations period has not lapsed.

Thus, employees who are discriminated or retaliated against in violation of the N.C. Medicaid statute may bring an action under the N.C. FCA. Because §1-616 of the N.C. FCA mandates that the act be construed to be consistent with the federal FCA and its amendments, the scope of the N.C. FCA's anti-retaliation provision is at least as protective as that of the federal FCA. The only difference is that, while the N.C. FCA encompasses the same statute of limitations as the federal act, it does not contain an explicit three-year statute of limitations.

The Civil Investigative Demand

Like the federal FCA and several other qui tam states, North Carolina has added an FCA-specific civil investigative demand process. This process allows the North Carolina attorney general (NCAG) to issue subpoenas to obtain information and documents from a defendant related to false claims.

While this process will do much to further an N.C. FCA investigation, it does not specifically authorize the NCAG to take depositions or seek oral testimony from a defendant. By contrast, the federal FCA allows the government to request an oral examination of any person who the government reasonably believes to be in possession or control of evidence indicating a violation of the federal FCA. Because this provision strengthens the government's ability to investigate FCA violations, the omission of such a provision in the N.C. FCA may curtail an NCAG FCA investigation that does not potentially involve Medicaid fraud.

Seal Period

Under §1-608(b)(2) of the N.C. FCA, a qui tam complaint filed under the act will remain under seal for at least 120 days while the NCAG investigates the relator's allegations. The federal FCA, however, provides for a more limited 60-day seal period to investigate the relator's claim and to make a decision on whether to intervene before the complaint is unsealed.

Because the state of North Carolina has far fewer personnel and resources than the federal government, this longer seal period could afford the state the opportunity to make a more thorough determination on the merits of a relator's complaint before making an intervention decision. On the other hand, the longer seal period could slow the litigation process and lead to a backlog of cases. However, as a practical matter, very few (if any) qui tam matters are unsealed within the first 120 days.

Litigation-Cost Provision

Notably, under §1-608(c), the NCAG can recoup the state's cost to litigate FCA cases, including reasonable attorney fees. The NCAG may also retain a portion of the state's recovery from successful qui tam suits. This provision, which is not found in the federal FCA, will provide necessary funding for the NCAG's Office to investigate and litigate N.C. FCA cases. Eventually, this provision may allow the NCAG's Office to become self-sustaining, as litigation costs collected from wrongdoers will facilitate stronger investigation and prosecution of even more cases. When this occurs, reductions in the state's overall budget will not have as great an impact on the NCAG's offensive against fraud committed against the state fisc.

An Important Tool for Recovery

The N.C. FCA provides a very important tool for recovering wrongfully taken state taxpayer money. The qui tam provisions will incentivize whistleblowers to file suit on behalf of the state to recover funds lost to fraud, while also providing for the NCAG's effort to become self funding. While North Carolina taxpayers will immediately benefit from this new fraud-fighting mechanism, a few changes are needed for the N.C. FCA to reach its potential. The North Carolina General Assembly should modify its public disclosure bar, original source exception and first-to-file provision to bring them in line with their counterparts under the most recent amendments to the federal FCA.

In addition, removing the public employee limitation would incentivize an entire sector of potential whistleblowers. The North Carolina General Assembly should also add to the NCAG's arsenal of investigative tools so that it encompasses the ability to conduct depositions — a powerful tool in collecting crucial information for a qui tam investigation. Additionally, the state might shorten the 120-day seal period so that it mirrors the federal FCA. These changes would further strengthen the N.C. FCA and bring this important legislation in line with the federal FCA qui tam provisions. These efforts would create the maximum return for the taxpayers of North Carolina. •

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