Professional Perspective

The Original Source Exception

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The False Claims Act (FCA) has long been a formidable tool in the hands of the Department of Justice, Inspectors General, and private qui tam plaintiffs (whistleblowers) to pursue government fraud cases against companies and individuals claiming federal funds. While companies regularly contracting with the government are likely to be familiar with the FCA, businesses using the array of federal aid programs may be less experienced in this field.

Even for veteran government contractors, however, post-2020 litigation will necessitate a considerable shift in strategy, as 2010 reforms to the FCA's public disclosure bar and original source requirement will fully replace more defendant-friendly components of the FCA. This article reviews changing FCA standards, specifically the elements of the original source exception to the public disclosure bar, and how it will affect future FCA defendants.

The FCA imposes liability on individuals and entities that make materially false claims or defraud government programs. Damages stemming from successful lawsuits can be significant, including treble damages and civil penalties. 31 U.S.C. § 3729(a)(1)(G). Importantly, § 3730(b) of the FCA empowers private citizens (relators) to sue on the government's behalf (in qui tam actions), and obtain substantial whistleblower awards, including attorney's fees, if they succeed.

No Knowledge, No Case

While the FCA can provide staggering awards to relators in successful cases, not all would-be whistleblowers are eligible. Under the FCA's public disclosure bar, relators are prohibited from bringing an FCA lawsuit based on a fraud that has already been disclosed through certain public channels, unless the relator is an "original source" of the information. § 3730(e)(4).

Prior to 2010, the FCA defined an original source as "an individual who has direct and independent knowledge of the information on which the allegations are based and has voluntarily provided the information to the Government before filing an action ..." (the 1986 version). § 3730(e)(4)(B) (2006).

In July 2010, the Patient Protection and Affordable Care Act (PPACA) amended the FCA to state that original source status depends on whether the relator has "knowledge that is independent of and materially adds to the publicly disclosed allegations or transactions." § 3730(e)(4)(B). These changes both add new requirements and remove existing requirements for relators bringing claims, which in concert will likely make it easier for many relators to bring such claims and pursue cases where the government declines to intervene.

Although the original source exception was amended 10 years ago, to date the updated statutory requirements have had limited judicial exposure, in part due to the typically long period of time between an alleged improper act and a successful FCA suit. Because most FCA cases addressed by the courts have involved allegations dating to before July 2010, they largely apply the original 1986 definition of an original source. In addition, almost all federal circuit courts, with the 7th Circuit being the only outlier, have concluded that the July 2010 amendments do not apply retroactively. However, these decisions have become largely irrelevant, as the FCA's 10-year absolute bar has now run for cases whose violations were committed prior to the July 2010 amendments, to which the 1986 version applied. This is even after the Supreme Court's liberal interpretation of that provision in *Conchise Consultancy, Inc. v. United States ex rel. Hunt*, 139 S. Ct. 1507 (2019).

Before and After the 2010 Amendment

The likely effect of the 2010 amendment is to increase the number of relators filing FCA suits by lowering the bar for relators filing a claim. The 1986 FCA defined an original source as "an individual who has direct and independent knowledge of the information on which the allegations are based ..." 31 U.S.C. § 3730(e)(4)(B) (2006). Congress conceived the original definition in 1986 in an effort to make the public disclosure bar and the original source exception work in unison to reward relators who provided valuable information.

In practice, however, courts varied widely in their interpretation of the original source exception. The divisions were particularly evident in different circuits' definitions of "direct" and "independent" knowledge, leading to an unresolved split. In its *United States ex rel. Moore & Co., P.A. v. Majestic Blue Fisheries* opinion, the Third Circuit commented that "although the original public disclosure bar was less restrictive ... it was by no means a low bar for relators to clear. Indeed,

given its broad language, as well as different courts' varying interpretations of that language, relators faced a formidable hurdle." 812 F.3d 294 (3d Cir. 2016).

To lower this hurdle and further incentivize future relators, Congress amended the original source exception, along with the public disclosure bar, to read:

> Original source means an individual who either (1) prior to a public disclosure … has voluntarily disclosed to the Government the information on which allegations or transactions in a claim are based, or (2) who has knowledge that is independent of and materially adds to the publicly disclosed allegations or transactions, and who has voluntarily provided the information to the Government before filing an action under this section. 31 U.S.C. § 3730(e)(4)(B).

As the court in *Moore* noted, "although no direct legislative history seems to exist, the textual changes alone evince Congress's intent to lower the bar for relators, at least as to some of its components." 812 F.3d 294 at 299.

In practice, multiple whistleblowers often come forward with related allegations against the same company even before any public disclosure. Their qui tam actions are usually similar at a high level, but often reference different specific allegations, and almost always reference different transactions. The amended clause (1), above, is thus likely to spur litigation regarding the breadth of the phrase "allegations or transactions in a claim are based," when specific allegations or transactions fall within a broader scheme on which the claim is based.

If the clause is ultimately construed narrowly, companies could face additional exposure from relators disclosing new allegations or transactions that fall within a broader, previously disclosed scheme. Conversely, a narrow construction would likely bar many such relators under the public disclosure bar.

Through these amendments, Congress also created an entirely new method for determining an original source, in addition to revising the existing method.

First, every relator that reported the fraud to the government prior to a qualifying public disclosure is automatically an original source. 31 U.S.C. § 3730(e)(4)(B). Qualifying as an original source is not, of course, the only criterion for prospective relators, as they must also be the first to have filed a complaint containing the allegations at issue under the "first-to-file" bar. § 3730(b)(5). In practice, relators are sometimes open to discussing arrangements that will avoid litigation over who disclosed which of the salient facts first and instead agree upon a split among relators of any work contributing to the ongoing case and any potential award. Arguments regarding whether a "first to file" relator was an original source under this new method will undoubtedly ensue.

Second, Congress revised the method for determining original source status in cases where a relator waited until after a qualifying public disclosure to contact the government to report fraud. The 2010 amendment removed the direct knowledge requirement, included a "materially adds" requirement, and clarified the independent knowledge requirement. All three changes affect available defenses in FCA cases.

Removal of Direct Knowledge Requirement

Removal of the direct knowledge requirement will likely be one of the most significant challenges for defendants in FCA civil actions. Although there was no consensus among circuits about how to define direct knowledge, most adopted an approach that required relators to possess firsthand knowledge of the alleged fraud, a high bar for many relators. See, e.g., *United States ex rel. Schumann v. Astrazeneca Pharms. L.P.*, 769 F.3d 837, 847 (3d Cir. 2014).

In a substantial number of cases, relators acquired the information underlying their allegations from third parties or from their own deductions based on second-hand accounts. See, e.g., *United States ex rel. Saldivar v. Fresenius Med. Care Holdings, Inc.*, 841 F.3d 927, 931 (11th Cir. 2016). Relators, and their counsel, sometimes spend months asking other employees about potential red flags in the hopes of bolstering their qui tam case.

In the past, many courts were unwilling to classify knowledge of third-party allegations as direct knowledge. Unless a relator was a corporate insider with immediate knowledge of the precise fraudulent activity underway, a defendant could generally prevail in court on the directness element. See, e.g., *United States v. Medco Health Sols. Inc.*, 777 F. App'x 30 (3d Cir. 2019).

Signaling its intention to lighten the relators' burden, Congress removed the direct knowledge requirement entirely, and replaced it with the "materially adds" requirement. Although this replacement limits the original source requirement as

discussed below, it softens the FCA's knowledge requirement by permitting relators to rely on second-hand information, and incentivizes them to conduct their own investigation prior to filing suit. For example, under the 1986 FCA, a relator with second-hand information would most likely fail to qualify as an original source, even if this information materially added to and was independent of publicly disclosed allegations. The 2010 Amendment, however, makes the difference between first- or second-hand nature of the information irrelevant, thereby eliminating a potent defense for FCA civil action defendants.

Defining 'Materially Adds'

Part of Congress's impetus to amend the FCA was born out of unresolved circuit splits stemming from definitional disagreements, including the "direct knowledge" requirement. However, its replacement in the amended FCA, the "materially adds" requirement, has itself produced a flurry of definitions and analyses among the circuits.

At the root of the various interpretations of the "materially adds" requirement is the public disclosure bar itself. It reads: "The court shall dismiss an action or claim under this section, unless opposed by the Government, if substantially the same allegations or transactions as alleged in the action or claim were publicly disclosed …" 31 U.S.C. § 3730(e)(4)(A). The use of both "substantially the same" in the public disclosure bar and "materially adds" in the original source exception has prompted some courts to hold that the two inquiries must be distinct, while other courts have chosen not to make the distinction at all. The different approaches, though sometimes yielding similar results, will significantly impact defense strategy.

The First Circuit in *United States ex rel. Winkelman v. CVS Caremark Corporation*, 827 F.3d 201, 211-12 (1st Cir. 2016) and the Tenth Circuit in *United States ex rel. Reed v. KeyPoint Government Solutions* have adopted similar approaches focused on distinguishing between allegations that are "substantially similar" to publicly disclosed information and those that "materially add" to it. To accomplish this, the two courts have used a definition of materiality found both in Black's Law Dictionary and in the liability section of the FCA itself: "a relator 'materially adds' to public disclosures if her information 'is sufficiently important to influence the behavior of the recipient.'"

To accurately determine whether a relator's allegations would have influenced the government or merely added less significant details to publicly disclosed information, "the materially-adds analysis must be firmly grounded in the facts and circumstances of a particular case." Crucially, because it held that the materiality inquiry is distinct, the Tenth Circuit noted that "[t]he plain terms of the original-source exception contemplate that some qui tam claims involving allegations that are substantially the same as publicly disclosed allegations nevertheless will survive the public disclosure bar because they materially add to the publicly disclosed information."

On the other end, the same court held that a relator who merely adds background information or details about a known fraudulent scheme does not materially add to the publicly disclosed information. 923 F.3d 729, 729-56 (10th Cir. 2019).

The Seventh Circuit in *Cause of Action v. Chicago Transit Authority*, 803 F. App'x 522, 525-26 (2d Cir. 2020) and the Second Circuit in *Vierczhalek v. MedImmune Inc.* adopted a markedly different standard. Unlike the First and Tenth Circuits, the Seventh chose not to distinguish between the "substantially similar" and "materially adds" inquiries. Instead, it held that if a relator's allegations are substantially similar to those contained in the public disclosures, the allegations cannot materially add to the public disclosures. 815 F.3d 267 (7th Cir. 2016).

The lack of distinction between the two inquiries is beneficial to defendants in non-intervened FCA actions, since it closes one avenue to a relator seeking a way around the public disclosure bar. A relator with allegations that are substantially similar to previously disclosed information would not prevail, regardless of whether such allegations would have influenced the government's actions.

Another notable approach to the "materially adds" inquiry comes from the Third Circuit. In *Moore*, it held that "a relator materially adds to the publicly disclosed allegation or transaction of fraud when it contributes information ... that adds in a significant way to the essential factual background: 'the who, what, when, where and how of the events at issue." 812 F.3d 294, 307. Of the three approaches, the Third Circuit's gives relators the greatest opportunity to avoid the public disclosure bar. Like the Tenth Circuit, the Third Circuit draws a distinction between the "substantially similar" and "materially adds" inquiries. Unlike the Tenth Circuit, however, the Third Circuit does not necessarily reject allegations that contribute only background information or details. This relieves relators of another limitation to the original source exception.

Independent Knowledge vs. Independent of Public Disclosure

Original source status also requires knowledge that is independent of the publicly disclosed allegations or transactions. 31 U.S.C. § 3730(e)(4)(B). Congress previously used the word "independent" in the 1986 definition, as in "direct and independent knowledge," there referring to the much-litigated prohibition on claims derived from second-hand knowledge. By contrast, "independent" as used in the 2010 amendment is tied to whether the claim is independent of publicly disclosed allegations or transactions. Thus far, only three circuits, the Third, Fifth, and Seventh, have put forth their interpretations of the new "independent" element.

In *Moore*, the Third Circuit revisited the 1986 definition of "independent" and chose to create an entirely new standard for post-amendment cases. The court concluded that the relator's knowledge need only be independent of the qualifying public disclosure and not independent from any and all information existing in the public domain. Moreover, the court held that amended FCA language requires courts, on a case-by-case basis, to compare the relator's knowledge with the information that was disclosed through the public disclosure sources enumerated.

The court admitted that under the pre-amendment public disclosure bar, the relator in *Moore* would not have qualified as an original source. However, using the new method, it found that the relator's knowledge was independent of public disclosure when he used discovery from a separate wrongful death suit to gain information about the defendants in an FCA action. 812 F.3d 294, 304-06. Thus, the Third Circuit's approach further limits the defenses available to an FCA civil action defendant.

The three other circuits to consider the term "independent" since 2010 have each declined to follow the Third Circuit's approach and instead deferred to the pre-2010 definition of "independent knowledge." The Second Circuit in *Vierczhalek*, the Fifth Circuit in *Stennett v. Premier Rehabilitation, LLC*, 479 F. App'x 631 (5th Cir. 2012), and the Seventh Circuit in *Cause of Action* all briefly discussed the "independent of public disclosure" standard. All three courts cited to cases that applied the 1986 definition of "independent knowledge," and did not fundamentally revise how they analyze this element in the post-amendment definition. Instead, they have used the pre- and post- 2010 versions of "independent" interchangeably. This suggests a greater level of continuity for defendants seeking to make use of the public disclosure bar.

Defense Strategies for FCA Litigation

While courts have only recently begun to apply the amended definition of an original source and have produced divergent interpretations, it is clear that the new standards are designed to lower the bar for future relators. As such, the most effective strategy for companies concerned about FCA liability is timely self-disclosure. The amended original source definition incentivizes voluntary disclosure in several ways.

First, the relator's potentially automatic qualification as an original source if she reports fraud prior to any public disclosure gives whistleblowers a significant advantage over their companies. Defendants thus benefit from getting ahead of whistleblowers by proactively rooting out potential FCA-related misconduct and disclosing such information to the appropriate authorities through defense counsel, even where such disclosure may not be required (as in cases where federal government contractors are required to make voluntary disclosures where they find "credible evidence" of an FCA violation). See, e.g., FAR 52.203-13(b)(3)(i). This is particularly true while Department of Justice guidance incentivizing voluntary disclosures of potential FCA violations remains in place.

Second, the quality of information disclosed has even greater importance than in pre-2020 cases. Most public disclosures giving rise to the bar under 31 U.S.C. § 3730(e)(4)(B) come from newspaper and other journalistic accounts, reports from federal agencies and state governments, and other sources unrelated to the company. However, some in fact do come from companies' own disclosures, whether through press releases or securities filings.

Of course, there are many non-FCA-related reasons for companies not to disclose conduct that potentially gives rise to FCA liability. However, when companies do choose to withhold potentially relevant details from their public disclosures, they risk facing whistleblower suits that take advantage of the "materially adds" element of the original source exception should those disclosures be less than complete.

On the other hand, excessive disclosure can also subject companies to increased liability and scrutiny. For this reason, companies, through counsel, should consider carefully how to disclose the facts surrounding potential FCA violations. Although public disclosure must be balanced against the other countervailing reasons for refraining to disclose, the earlier

and more comprehensive the public disclosures are, the harder it is for a relator to demonstrate that she acquired her knowledge of fraud independently.

Once in court, defendants will likely have a more difficult time dismissing relators based on the public disclosure bar, and relators relying on second-hand knowledge will likely have an easier time demonstrating that they are original sources, as long as their allegation adds material value to publicly disclosed information. Because the definition of "material addition" has been discussed briefly by only a few courts, however, recipients of FCA suits, together with defense counsel, still have an opportunity to shape what "material addition" means, and in turn, the hurdles relators will face in the years and cases to come.

Conclusion

With the amended FCA fully replacing its predecessor in 2020, companies are likely to face significant external and internal pressure surrounding potential fraud, together with a lowered bar for FCA relators in qui tam actions. The first step to mitigation will always be a robust compliance program. Upon discovery of a potential violation or whistleblower, however, the next step is a timely and carefully considered disclosure broad enough to foreclose future potential relators from materially adding information. And finally, if an FCA claim has already been made, a vigorous defense that takes advantage of the nuances—and as yet unresolved definitional ambiguity—present in the 2010 amendments.

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