

Court of Appeal No. 05-2016

IN THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

UNITED STATES EX REL. JEFFREY E. MAIN
Plaintiff/Appellant

v.

OAKLAND CITY UNIVERSITY founded by GENERAL BAPTISTS, INC.
d/b/a OAKLAND CITY UNIVERSITY
Defendant/Appellee

On Appeal from the United States District Court
for the Southern District of Indiana Evansville Division
The Honorable Richard L. Young, Judge, Presiding
Case No. 3:03-CV-71-RLY-WGH

**BRIEF OF AMICI CURIAE AMERICAN COUNCIL ON EDUCATION
AND CAREER COLLEGE ASSOCIATION IN SUPPORT OF
DEFENDANT/APPELLEE'S PETITION FOR REHEARING AND
REHEARING EN BANC**

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I. STATEMENT IN SUPPORT OF REHEARING EN BANC

Amici Curiae American Council on Education ("ACE") and Career College Association ("CCA") submit this brief in support of Defendant Oakland City University's ("University's") Petition for Rehearing and Rehearing En Banc. Rehearing is appropriate because the panel's decision conflicts with well-established law regarding promissory fraud claims under the False Claims Act ("FCA"), 31 U.S.C. § 3729 and reduces the standard for such claims to a level that would permit every garden-variety claim for breach of contract or regulatory violation to be actionable as fraud under the FCA. Under the panel's decision, a party can salvage an otherwise deficient complaint by simply making conclusory statements that a defendant never intended to comply with its regulatory or contractual obligations. By applying such a low threshold, this ruling could make it virtually impossible to dismiss a promissory fraud claim in the FCA or any other setting.

This decision is also inconsistent with this Court's recent ruling that, to state a FCA action on a false certification theory, a relator must establish that the certification was a condition of or prerequisite to government payment. *United States ex rel. Gross v. AIDS Research Alliance-Chicago*, 415 F.3d 601, 604 (7th Cir. 2005). In contrast, this decision would allow a FCA claim to go forward no matter how minor the violation or far removed the requirement is to any government decision to provide financial aid to a student. Contrary to established FCA law, the end result would be to permit relators to use the FCA to enforce regulatory requirements and encroach upon the Department of Education's ("ED's") enforcement process. *See United States ex rel. Lamers v. Green Bay*, 168 F.3d 1013, 1020 (7th Cir. 1999) (FCA not vehicle for enforcing "compliance with administrative regulations"). Courts, however, have long held that FCA liability attaches to the claim for payment, not the alleged wrongful activity. For these reasons, a rehearing by the panel or en banc is justified in this matter.

II. INTEREST OF AMICI CURIAE

ACE is a major coordinating body for the nation's higher education institutions, consisting of approximately 1,800 non-profit, accredited colleges, universities and higher education-related associations and organizations. CCA is a voluntary membership organization of over 1,200 private, accredited, postsecondary schools, institutes, colleges, and universities that comprise the for-profit sector of higher education. Together, ACE and CCA represent the vast majority of all providers of post-secondary education in the country. Most of ACE and CCA's members participate in federal financial aid programs. ACE, CCA, and their members have an interest in this matter because the panel decision significantly expands the conditions under which a relator may maintain a FCA action against an educational institution for alleged violation of regulatory requirements applicable to these programs.

III. ARGUMENT

A. Summary of Panel Decision

Under Title IV, Higher Education Act ("HEA"), all institutions that wish to participate in federal financial aid programs must execute a Program Participation Agreement ("PPA") in which they must agree, among many other things, that they "will not provide any commission, bonus, or other incentive payment based directly or indirectly on success in securing enrollments or financial aid" to those involved in recruiting activities. 20 U.S.C. § 1094(a)(20). Relator contends that the University violated this provision by paying its admissions representatives commissions, bonuses, and other incentive payments based upon their success in securing enrollments.

The panel assumed for purposes of Defendant's Motion to Dismiss that the University "knew of the prohibition against paying contingent fees to recruiters" and lied to ED to obtain a certificate of eligibility that it would not have obtained had it told the truth. The panel explained

that one who "accepts federal funds that are contingent on following a regulation which it then violates, has broken a contract." The panel ruled that the violation of a contract or regulation does not itself amount to fraud, but would if the relator could prove a defendant never intended to honor its obligations. The panel reversed the district court's dismissal of the action, although there were no allegations in relator's complaint, other than conclusory statements, that would establish that the University's promise to comply with the terms of its PPA was false when made.

B. In Conflict with F.R.C.P. 9(b), the Panel Decision Allows a Relator to Turn Every Alleged Regulatory Violation or Contract Breach into a FCA Action by Simply Alleging the Defendant Never Intended to Comply

The issue presented by the panel decision, but not addressed by it, is: what does a relator need to plead to state a promissory fraud claim under the FCA? The panel assumed that the University executed its PPA without any intention of performing, without examining whether relator alleged sufficient facts to support this allegation. Under the panel's analysis, all a relator needs to do to state a promissory fraud case is simply allege the defendant did not intend to honor its promise. This reasoning would render every alleged regulatory or contractual violation a false claim and make it virtually impossible to dismiss a FCA claim at the pleading stage.

In the FCA context, courts have explained that an action based on a promissory fraud or a fraud-in-the-inducement theory is "actionable in *rare circumstances*." *United States ex rel. Hopper v. Anton*, 91 F.3d 1261, 1267 (9th Cir. 1996) (emphasis added). This is because, as this Circuit and others have stressed, the "FCA is not an appropriate vehicle for policing technical compliance with administrative regulations." *Lamers*, 168 F.3d at 1020; *see Hopper*, 91 F.3d at 1267 ("Mere regulatory violations do not give rise to a viable FCA action."); *United States ex rel. Thompson v. Columbia/HCA Healthcare, Corp.*, 125 F.3d 899, 902 (5th Cir. 1997) ("services rendered in violation of a statute do not necessarily constitute" false claims). This Circuit, in fact, has cautioned that allowing suits "based on nothing more than an allegation of a fraudulent

promise" creates "a risk of turning every breach of contract suit into a fraud suit." *J.H. Dresnick v. American Broadcasting Co.*, 44 F.3d 1345, 1354 (7th Cir. 1995). This risk is realized if a court must "accept as true" conclusory allegations that a defendant never intended to honor its promise, without facts independent of the alleged violation to establish it was false when made.

Courts that have addressed this issue have rejected promissory fraud claims premised solely on allegations that a defendant did not live up to its promise. *See United States ex rel. Willard v. Humana Health Plan of Texas Inc.*, 336 F.3d 375, 386 (5th Cir. 2003) ("no inference of fraudulent intent . . . from the mere fact that a promise made is subsequently not performed") (quoting *United States v. Shah*, 44 F.3d 285, 293 n.14 (5th Cir. 1995); *United States ex rel. Graves v. ITT Educ. Servs., Inc.*, 284 F. Supp. 2d 487, 503 (S.D. Tex. 2003) ("mere fact of nonperformance [under a PPA] does not state a claim for fraudulent inducement"), *aff'd*, 2004 U.S. App. LEXIS 21799 (5th Cir. 2004), *cert. denied*, ___ U.S. ___; 125 S. Ct. 1869 (2005); *United States ex rel. Swan v. Covenant Care, Inc.*, 2001 U.S. Dist. LEXIS 25480 at *5 ("failure to comply with program conditions after promising to do so . . . does not prove or suggest that its initial promise of compliance was false when it was made"). These courts have required relators to allege facts independent of the alleged breach to establish that a defendant never intended to comply. Without such facts, all that is left is the breach itself, which does not provide a sufficient basis to infer that defendant never intended to honor its obligations.

In this case, relator's complaint contains no allegations independent of the alleged breach to support such an inference. At most, all relator alleges is that "[a]t all times material hereto," the University was aware it was violating Title IV HEA limits on incentive compensation. App. Appendix, p. B3, ¶ 16. These allegations fall far short of establishing that the University never intended to comply with its PPA. Should the decision stand, the legal and practical effect would

be to encourage relators (and plaintiffs in breach of contract cases) to make similar conclusory allegations of promissory fraud as a means of avoiding dismissal. The function of F.R.C.P. 9(b), however, is to require "the plaintiff to conduct a precomplaint investigation in sufficient depth to assure that the charge of fraud is responsible and supported, rather than defamatory and extortionate." *Ackerman v. Northwestern Mut. Life Ins. Co.*, 172 F.3d 467, 469 (7th Cir. 1999). The panel decision turns this notion on its head, by allowing a relator to salvage claims that are otherwise deficient through conclusory allegations in hopes of filling in the missing elements through discovery. This cannot be the law of the Circuit.

C. To Insure that FCA Actions Based on Promissory Fraud Are "Actionable in Rare Circumstances," the Statute or Regulation the Defendant Is Alleged to Have Violated Must Be a Condition of Payment by the Government

Relator's promissory fraud FCA claim is also deficient because many of the hundreds, if not thousands, of program requirements included in the PPA are not conditions of government payment of financial aid to students. Recently, the Seventh Circuit joined the Second, Fourth, Fifth, Ninth, and D.C. Circuits in ruling that a FCA claim premised on a false certification of compliance with a statute or regulation is actionable only if compliance is "a condition of or prerequisite to government payment." *Gross*, 415 F.3d at 604. This holding is a recognition that liability under 31 U.S.C. § 3729(a)(2) (for making a false statement to get a false claim paid) and § 3729(a)(3) (conspiring to get "a false or fraudulent claim allowed or paid"), "plainly links the wrongful activity to the government's decision to pay." *United States ex rel. Mikes v. Straus*, 274 F.3d 687, 696 (2d Cir. 2001). In other words, the FCA "attaches liability, not to the underlying fraudulent activity . . . but to the 'claim for payment.'" *Harrison v. Westinghouse Savannah River Co.*, 176 F.3d 776, 785 (4th Cir. 1999) (quoting *United States v. Rivera*, 55 F.3d 703, 709

(1st Cir. 1995)). These cases recognize the well-established principle that the FCA is not a means of enforcing regulatory compliance.¹

The panel's decision conflicts with this principle by ignoring and not requiring any linkage between the wrongful activity and the government's decision to pay. A false statement is actionable, however, only if made or used to get a false or fraudulent claim approved or paid. 31 U.S.C. § 3729(a)(3). In the PPA, for example, an institution must agree to comply with a whole host of regulations and statutes, including "all statutory provisions of or applicable to Title IV of the HEA, all applicable regulatory provisions prescribed under that statutory authority, and all applicable special arrangements, agreements, and limitations entered into under the authority of " Title IV HEA, many of which are far removed from the government's payment decision. 34 C.F.R. § 668.14(b)(1). Under the panel's analysis, a breach of any one of these statutes, regulations, or arrangements can result in FCA liability, no matter how minor or far removed they are from the government's decision to provide financial aid to a student.²

In this case, nothing in the statute or regulation conditions government payment of financial aid to students on an institution's compliance with the incentive compensation limits.

¹ The implications of the panel's decision extend far beyond the education sector and impact virtually all recipients of government funding. For example, health care providers must apply to participate in Medicare and other medical programs. Under the panel's decision, it will be impossible to get a FCA action against a provider dismissed if relator alleges the provider did not intend to comply with any one of the thousands of requirements to which it must agree to comply to maintain its eligibility, without consideration of the nexus between the program requirement and the government funding decision. This is not (and should not be) the standard the courts have applied in deciding motions to dismiss FCA actions.

² For example, a PPA requires that schools supply information to students regarding job placement, as well as requiring the timely submission of surveys required by ED. 34 C.F.R. § 668.14(b). Under the panel's decision, a conclusory allegation that an institution did not intend to timely provide the requested information when it executed its PPA would preclude dismissal of the action and expose the institution to discovery and potential FCA liability.

At least four courts have dismissed very similar FCA allegations asserted against other institutions precisely because compliance with the incentive compensation limitation is not a condition of or prerequisite to government payment.³ As is the case with other violations of Title IV, HEA requirements, ED has a variety of enforcement options, including limiting, suspending, or terminating an institution's participation in any Title IV, HEA program; imposing a civil penalty; or deciding to take no action at all. 20 U.S.C. § 1094(c)(1)(F). The mere fact an agency has the power to enforce its own regulations does not convert a condition of participation in a federal program into a condition of or prerequisite to government payment.

In addition, allowing a claim to proceed on a promissory fraud theory in a situation in which payment is not conditioned on compliance improperly interferes with ED's discretion and ability to administer its own programs. As one court explained, allowing a FCA action in such a situation would allow a relator to supplant an agency's authority and turn what might be a discretionary denial of payment into a mandatory penalty:

To allow FCA suits to proceed where government payment of . . . claims is not conditioned on perfect regulatory compliance – and where [an agency] may choose to waive administrative remedies, or impose a less drastic sanction than full denial of payment – would improperly permit qui tam plaintiffs to supplant the regulatory discretion granted to [an agency], essentially turning a discretionary denial of payment remedy into a mandatory penalty for failure to meet [statutory or regulatory] requirements.

United States ex rel. Swan v. Covenant Care, Inc., 279 F. Supp. 2d 1212, 1222 (E.D. Cal. 2002).

There is no reason why a relator should be permitted to interfere with an agency's enforcement

³ These cases are: (1) *Graves*, 284 F. Supp. 2d at 501; (2) *United States ex rel. Gay v. Lincoln Tech. Inst.*, No. 3:01-CV-505-K, 2003 U.S. Dist. LEXIS 25968 (N.D. Tex. Sept. 3, 2003), *aff'd*, 2004 U.S. App. LEXIS 21489 (5th Cir. 2004) (*per curiam*); (3) *United States ex rel. Bowman v. Education America, Inc.*, No. H-00-3028 (S.D. Tex. Jan. 8, 2004), *aff'd*, 2004 U.S. App. LEXIS 24673 (5th Cir. 2004); and (4) *United States ex rel. Hendow v. University of Phoenix*, No. CV S-03-457 GEB DAD (E.D. Cal. May 20, 2004) (appeal pending).

mechanism. The result is particularly troubling here, as the allegations are wholly insufficient to support a FCA claim even had the University actually certified that it was in compliance with the limits on incentive compensation – which it did not. There is simply no reason why FCA liability should be applied to issues of compliance with federal regulations – under a promissory fraud or any other theory – that are not conditions of or prerequisites to government payment.

IV. CONCLUSION

For these reasons, Amici Curiae ACE and CCA respectfully request that the Court vacate its opinion and set this case for rehearing en banc or rehearing by the panel.

DATED: November 10, 2005

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