



# California False Claims Ruling: Contractor Invoices Include Implied Certification of Contract Compliance

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Under a recent California appellate decision, public agencies have a cause of action under the California False Claims Act against contractors submitting invoices that, although facially correct, fail to identify areas of non-compliance with the contract.

## SUMMARY

Under the California False Claims Act (CFCA)[1] a contractor that fraudulently bills a public agency for goods or services can be held liable for treble damages and other remedies. The central issue in *San Francisco Unified School District ex rel. Contreras v. Laidlaw Transit, Inc.* (Laidlaw), February 26, 2010, Cal. App. 2010 LEXIS 249, focused on the standard by which an invoice could be considered fraudulent. On February 26, 2010, a California Court of Appeal ruled that a contractor has violated the CFCA if it submits invoices while aware of its noncompliance with material express contract requirements or in reckless disregard of whether it is in compliance, regardless of whether or not the invoice itself contains false claims. In the *Laidlaw* case,[2] the California Court of Appeal for the Second Circuit held that invoices include an implied certification that the contractor is not in violation of any material requirement of the contract. The court further held that a CFCA claim can be filed against a contractor even if there is no false statement in an invoice itself, and no explicit contractual obligation to certify that a contractor is not in violation of any contract requirement. The decision conforms California law to the federal False Claims Act, which permits plaintiffs to base a false claims suit upon the alleged breach of an invoice's implied certification that the contractor is in compliance with material contract terms. This means that claims against contractors by or on behalf of public agencies are not required to allege actual misstatements in the request for payment, and that successful plaintiffs may recover treble damages and civil penalties.

## BACKGROUND

The CFCA mirrors the federal False Claims Act<sup>[3]</sup> and allows private plaintiffs, sometimes referred to as *qui tam* plaintiffs, to sue contractors for filing false claims with a public agency (subject to prior notice and the opportunity to take the case to the state Attorney General and, if applicable, local law enforcement). If the Attorney General and local authorities decline to take the case, the private plaintiff can prosecute the case and, if successful, recover on behalf of the public agency not only damages caused by the false claim, but even treble damages and civil penalties. Prior to the *Laidlaw* decision, California case law had concluded that a false claims action could only be maintained if the contract either contained a requirement that the contractor certify its compliance with all material provisions of the contract as a condition to payment (and the certification was false), or that the request for payment contained an actual and intentional misstatement of fact, or a reckless disregard for the accuracy of the information.

In *Laidlaw*, the California court adopted the federal rule that a request for payment contains an implied certification of compliance with all material requirements of the contract.<sup>[4]</sup> Consequently, allegations that Laidlaw materially breached the contract by failing to provide safe and non-polluting busses were held sufficient to state a claim under the CFCA, even if the request for payment itself did not contain a misstatement.

## FACTS AND DISCUSSION

The case arose when two Laidlaw Transit employees, suing as *qui tam* plaintiffs on behalf of the San Francisco Unified School District, asserted that Laidlaw Transit was in violation of numerous material contract requirements to provide bus transportation services to the District. Under the contract, the District agreed to pay monthly for "services satisfactorily performed...after receipt of properly documented invoices." Laidlaw Transit demurred to the complaint and the trial court sustained the demurrer. The plaintiffs appealed.

Laidlaw Transit responded by asserting immunity from liability under the CFCA since the invoices it submitted did not expressly assert compliance with all requirements of the contract nor did the contract require certification of compliance with all contract terms as a condition to payment. The defendant also argued that its claims were not false because there was no literally false information on the face of the invoices, which merely identified routes driven and the resultant charges. Referring to the language of the CFCA, the court noted that the law contained alternate grounds for liability: (i) presentation of a false record or statement to get a false claim paid; or (ii) presentation of a "false or fraudulent claim for payment or approval."<sup>[5]</sup> The court concluded that, in light of the specific requirement for a "false record or statement" in the first option, the second option required the conclusion that an invoice did not need to contain a false statement to be actionable.

In reaching this conclusion, the court cited decisions under the federal False Claims Act holding that liability can arise even absent a false statement in the claim itself.<sup>[6]</sup> The court also cited an earlier California decision that held that when a contractor delivered parts that did not comply with the requirements of the contract, its submittal of requests for payment constituted false claims because the contract had been "induced by falsity" and because the requests sought payment for goods that had not been provided.

The court also addressed two other elements necessary to establish a false claim:

- **Materiality** Citing federal cases, Laidlaw Transit asserted that in order to state a claim, the plaintiff needed to allege that the falsity was "critical" to the public agency's decision to pay out money.[7] The court adopted a much softer materiality standard: whether the falsity had a "natural tendency to" or was "capable of" influencing agency action.
- **Causation** Laidlaw claimed that plaintiffs had failed to allege in their complaint that the asserted false claims caused any damages. Citing federal authorities, the court concluded the issue was premature and no proof of damages was required in order to state a claim sufficient to overcome the demurrer. Damages, according to the court, could be inferred by reason of Laidlaw's implied false certifications. In addition, the court noted that causation was not required to recover statutory false claims penalties.

## CONCLUSION AND COMMENT

*Laidlaw* expands possible CFCA liability and raises the issue of potential CFCA claims in a much broader context. The definition of a material falsity in respect to the implied certification will be a critical future issue. Under the federal rule, the falsity must be significant (i.e. "critical" to the agency's determination to pay); under the rule adopted in *Laidlaw* (i.e. "capable of" influencing the agency's decision), however, much of what might be considered minor noncompliance issues could be elevated to the status of materiality. Under this standard, plaintiffs may not even need to allege that the falsity caused the agency to pay an invoice, only that it might have.

Since plaintiffs under the CFCA are entitled to treble damages and to civil penalties, significantly more CFCA claims may be triggered because every material contract breach may result in a false claim, even if invoices themselves are accurate.

The parties may seek a California Supreme Court review of the case. If review is granted, the decision could be modified or reversed. We will monitor and report any further developments.

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[1] California Government Code § 12650 *et seq.* ("CFCA").

[2] *San Francisco Unified School District ex rel. Contreras v. Laidlaw Transit, Inc. (Laidlaw)*, March 1, 2010, Cal. App. LEXIS 249.

[3] 31 U.S.C. § 3729, *et seq.*

[4] See, e.g., *Shaw v. AAA Engineering & Drafting, Inc.* (10<sup>th</sup> Cir. 2000) 213 F.3d 519, 531 (*Shaw*).

[5] Former California Government § 12651(a). Section 12651(a) was amended in 2009 effective January 1, 2010 to impose liability for a "false *or fraudulent* claim" (italics added) for payment. The court concluded that the amendment, which occurred after the events giving rise to the claim, was not material to the claims in *Laidlaw*.

[6] E.g., *Shaw, supra*, at p. 531.

[7] *Ab-Tech Constr., Inc. v. U.S.* (1994) 31 Fed. Cl. 429, 434.