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False Claims Act - The Tenth Circuit Fails to Fully Consider the Harm to Public Policy Caused by Enforcement of a Prefiling Release Agreement in a Qui Tam Action: *United States Ex Rel. Ritchie v. Lockheed Martin Corp.*

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FALSE CLAIMS ACT—THE TENTH CIRCUIT FAILS TO FULLY CONSIDER THE HARM TO PUBLIC POLICY CAUSED BY ENFORCEMENT OF A PREFILING RELEASE AGREEMENT IN A QUI TAM ACTION: *UNITED STATES EX REL. RITCHIE V. LOCKHEED MARTIN CORP.*

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UNITED STATES ex rel. Ritchie v. Lockheed Martin Corp. analyzes the enforceability of a release agreement between private parties where the releasing party subsequently files a qui tam False Claims Act (FCA) suit as a relator for the United States.[1] The qui tam section of the FCA allows private persons to bring actions as relators for the government against those who have committed fraud upon it and guarantees most relators a portion of the proceeds from the action or postfiling settlement, regardless of whether the government intervenes.[2] The few courts that have addressed the enforceability of prefiling settlements have turned to the *Rumery* test set forth by the Supreme Court, which balances the interests in enforcing the release against the harm to public policy caused by enforcement.[3] The *Ritchie* court held that the interest in encouraging settlements outweighed the public policy of qui tam FCA suits since the al-

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[1] 558 F.3d 1161, 1167-71 (10th Cir. 2009).

[2] False Claims Act, 31 U.S.C. §§ 3729(a), 3730(b)(1), (d)(2) (2006). When the government intervenes, taking primary control of the qui tam litigation, the relator is typically entitled to 15% to 25% of the proceeds, as compared to the 25% to 30% guaranteed where the government leaves the relator to bring the action alone. *Id.* §§ 3730(d)(1), (2).

[3] Town of Newton v. Rumery, 480 U.S. 386, 392 (1987); *see, e.g.*, United States *ex rel.* Gebert v. Transp. Admin. Servs., 260 F.3d 909, 917 (8th Cir. 2001) (holding that the prefiling release was enforceable under the *Rumery* test since a settlement entered into during bankruptcy does not harm FCA public policy); United States *ex rel.* Green v. Northrop Corp., 59 F.3d 953, 969 (9th Cir. 1995) (holding that the prefiling release was unenforceable under the *Rumery* test since barring a qui tam action which uncovered fraud would significantly harm FCA public policy).

leged fraud had been disclosed to the government prior to the release.[4]

Ruth Ritchie worked for Lockheed and its predecessors for twenty-five years before being voluntarily terminated in accordance with a settlement agreement in 2005.[5] Beginning in 2002, she became responsible for overseeing and authenticating two databases which held information about Lockheed's employee pay incentives for U.S. Air Force contracts.[6] That same year, Ritchie internally reported her concern that "Lockheed managers were falsifying records to increase incentive payments to Lockheed employees."[7] She reported the problem again to Lockheed in May 2003, convinced that corrective actions taken by the contractor had not fixed the inaccuracies.[8] After further internal investigation, Lockheed dismissed some of Ritchie's claims as unsubstantiated and concluded that the remaining inaccuracies did not result in overstated incentives, and thus, the Air Force had not been overcharged.[9]

Lockheed notified the Air Force about the fraud allegations and the favorable findings of its internal investigation after Ritchie's May 2003 complaint.[10] The Defense Contract Audit Agency (DCAA) then undertook its own audit where Ritchie acted as the Lockheed point of contact and communicated with DCAA's auditor several times before the agency decided to refer the allegations to the Defense Criminal Investigative Service.[11] During the government's investigation, Ritchie sought damages from Lockheed for alleged retaliation related to her whistleblowing activities.[12] The two parties reached a settlement agreement in 2004, about a year before DCAA issued its final audit.[13] The settlement provided for Ritchie's termination and

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[4] *Ritchie*, 558 F.3d at 1169–70.

[5] *Id.* at 1164–65.

[6] *Id.* at 1164.

[7] *Id.*

[8] *Id.* The complaint also included allegations of retaliatory behavior by her supervisors. *Id.*

[9] *Id.*

[10] *Id.*

[11] *Id.* at 1164–65. DCAA initially limited the scope of their investigation to a single database and fiscal year, but later expanded this scope based on Ritchie's input. *Id.* at 1164–65.

[12] *Id.* at 1165.

[13] *Id.* at 1164–65. Neither the trial court nor the appellate court indicated any consideration of the DCAA's findings. *See generally Ritchie*, 558 F.3d 1161; United States *ex rel.* Ritchie v. Lockheed Martin Corp., No. 04-cv-01937-EWN-MJW, 2008 WL 608586 (D. Colo. Mar. 4, 2008).

the general release (the Lockheed Release) of claims by her against Lockheed.[14] Shortly after the settlement, Ritchie filed this qui tam action under the FCA.[15] Enforcing the release agreement, the District Court of Colorado granted Lockheed summary judgment.[16] Ritchie appealed, arguing that enforcement "would frustrate the policies of the FCA."[17]

The Tenth Circuit Court of Appeals upheld the enforceability of the release agreement and affirmed summary judgment for Lockheed.[18] After determining that the Lockheed Release covered the qui tam claim, the *Ritchie* court applied the *Rumery* balancing test to determine whether the release was enforceable.[19] Since Lockheed had notified the federal government of the fraud allegations before the settlement with Ritchie, allowing the government to investigate the claims, the court found that the federal interest in encouraging such disclosures and settlements outweighed the potential harm to the public's interest in uncovering fraud under the FCA.[20]

Though contract enforceability is normally considered under state law, the *Ritchie* court turned to the *Rumery* test under federal common law so as not to frustrate the FCA goal of deterring and remedying fraud.[21] The court explained that varying treatments of prefiling qui tam settlements amongst states would likely lead to forum shopping by plaintiffs seeking to optimize their recovery.[22] Since the FCA limits postfiling recovery by relators to a percentage of the amount recovered and remains silent on prefiling settlements, the *Ritchie* court noted that a government contractor could settle with a would-be relator for less than the contractor would pay in a qui tam action but more than the would-be relator would receive under the FCA.[23] Therefore, the court felt that a uniform federal approach was necessary to "protect[ ] the federal government's right to recover under the FCA" and followed the approach of the Ninth

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[14] *Ritchie*, 558 F.3d at 1165. The release language stated that Ritchie released "any and all claims [she] might have arising under federal, state or local law." *Id.* at 1167.

[15] *Id.* at 1165.

[16] *Id.* at 1167.

[17] *Id.* at 1167–68.

[18] *Id.* at 1163–64.

[19] *Id.* at 1167, 1169–71.

[20] *Id.* at 1171.

[21] *Id.* at 1168–69.

[22] *Id.* at 1169.

[23] *Id.* at 1168–69.

Circuit Court of Appeals in applying the *Rumery* balancing test to determine release enforceability.[24]

The *Ritchie* court compared two Ninth Circuit cases when weighing the interests in enforcing the Lockheed Release against the harms posed to the FCA's public policy by its enforcement.[25] In *United States ex rel. Green v. Northrop Corp.*, the Ninth Circuit held a release unenforceable where the government only learned of the fraud allegations upon qui tam filing;[26] whereas in *United States ex rel. Hall v. Teledyne Wah Chang Albany*, the Ninth Circuit held a release enforceable where, prior to the settlement, the government had full knowledge of the allegations and found them to be unsubstantiated upon investigation.[27] The *Ritchie* court likened the circumstances of the Lockheed release to *Hall* since Lockheed had notified the Air Force and DCAA of the allegations before settling with Ritchie.[28] The court indicated that by uncovering fraud, Lockheed's disclosure helped serve the FCA's policy interests.[29] The court acknowledged, however, that unlike *Hall*, there was still a federal interest in having Ritchie supplement FCA enforcement at the time of the release due to DCAA's ongoing investigation.[30] The court determined that the interest in encouraging settlements and disclosures outweighed this concern though and held that the Lockheed release was enforceable.[31]

Judge Briscoe dissented from the majority, arguing that *Hall* fails to fully account for the public policies underlying the FCA.[32] Referencing the Senate Report on the False Claims Amendments Act of 1986 (the 1986 Report), he pointed out that in updating the FCA, Congress intended to "supplement[ ] Government efforts to recoup monies lost due to fraud" as well as to encourage insiders to report fraud against the government.[33] Concerned with the implications of *Hall* regarding the government's compensatory interests, he noted that a lack of resources may prevent the government from independently fil-

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[24] *Id.* at 1169–70.
[25] *Id.* at 1170–71.
[26] 59 F.3d 953, 966, 969 (9th Cir. 1995) (discussed at *Ritchie*, 558 F.3d at 1169).
[27] 104 F.3d 230, 231–33 (9th Cir. 1997) (discussed at *Ritchie*, 558 F.3d at 1169).
[28] *Ritchie*, 558 F.3d at 1170 n.7.
[29] *Id.* at 1170.
[30] *Id.* at 1170–71.
[31] *Id.* at 1171.
[32] *See id.* at 1174.
[33] *Id.*; *see* S. REP. No. 99-345, at 1–2 (1986), *reprinted in* 1986 U.S.C.C.A.N. 5266, 5266–67.

ing suit on meritorious allegations and that *Hall* nonetheless allows private parties to "bargain away the Government's claim."[34] Judge Briscoe proposed that prefiling releases should only be enforceable with the Attorney General's express written consent.[35]

The Tenth Circuit appropriately recognized the federal interest in dealing uniformly with qui tam FCA releases amongst the states but failed to fully account for the public policy behind these claims in adopting the *Hall* analysis.[36] Even though there is a legitimate public interest in encouraging settlement over litigation, FCA policy interests would be significantly harmed if private parties were allowed to reach financial agreements releasing qui tam claims at the expense of the government's compensatory interests.[37] The 1986 Report indicates that the overall purpose of the reform was "to enhance the Government's ability to recover losses sustained as a result of fraud against the Government" and that a lack of resources was "perhaps the most serious problem" in the government's enforcement efforts against fraud.[38] It also explained that 1986 qui tam statutory changes guaranteeing relators a portion of the action or settlement's proceeds were specifically intended "to encourage more private enforcement suits."[39] In applying *Hall*, the *Ritchie* court fails to recognize the important role of the qui

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[34] *Id.* at 1174–75.

[35] *Id.* at 1175. Judge Briscoe explained that the government could then preserve its compensatory interest in a potential suit simply by refusing consent or requiring satisfactory disclosure before granting consent. *See id.* However, this requirement may be an impractical demand on government resources as contractors would likely seek consent on all general releases to ensure full protection.

[36] *See id.* at 1169. In *United States ex rel. Radcliffe v. Purdue Pharma, L.P.*, the Western District Court of Virginia similarly critiques *Hall*, observing that a government investigation does not negate the public interest in a qui tam FCA suit, "which includes not only disclosing information to the government, but also potentially investigating and prosecuting the case on behalf of the government," allowing it to recover funds lost due to fraud. 582 F. Supp. 2d 766, 780 n.10 (W.D. Va. 2008).

[37] For instance, counting on the government's inability to prosecute a complicated or questionable fraud claim due to a lack of resources, a government contractor could effectively cut the government out of a settlement. *See Ritchie*, 558 F.3d at 1168–69 (explaining how both the contractor and relator may benefit more from a private settlement than a qui tam action). This poses a serious threat to FCA policy since the settled claim revolves around a statute established for the purpose of returning funds to the government.

[38] S. REP. NO. 99-345, at 1, 7.

[39] *Id.* at 23–24, 27–28.

tam action in achieving the FCA's primary goal—recovering money lost by the government.[40]

Moreover, release enforceability as a disclosure incentive does not further the FCA's policy of uncovering fraud since the government would likely learn of any actual fraud through a relator's qui tam suit or a contractor's disclosure anyway. Disclosure incentives under the FCA are not aimed at government contractors, but rather, target individuals, as FCA qui tam actions rely on the "strong stimulus of personal ill will or the hope of gain" to accomplish its goals.[41] Contractors will likely only disclose possible fraud when it is in their best interest to do so, such as where the claims are meritless or where discovery is highly probable anyway. An increased likelihood of discovery exists where an employee has filed repeated internal complaints as in *Ritchie* or where an eventual outside audit would reveal fraud.

Where the claims are meritless, contractors falsely accused of fraud need not rely on release agreements to protect them since the FCA discourages such allegations by awarding attorney fees and expenses to defendants for frivolous claims.[42] Encouraging disclosure of these unfounded claims through release enforcement does not further the FCA goal of uncovering fraud. Where the government is already likely to discover unresolved claims of fraud or actual fraud, the monetary incentives for a qui tam relator under the FCA and the business interests of a contractor who wants to continue working on government contracts should sufficiently motivate disclosure. It is hard to imagine a situation where a contractor would voluntarily disclose fraud where no threat of litigation or business repercussions previously existed.

In light of the government's interest in recovering funds through private enforcement suits to supplement its own limited resources[43] and the questionable value of fraud disclosed prior to execution of a release, the significant harm to FCA public policy caused by enforcement of prefiling releases outweighs the enforcement interest in encouraging settlements, even where the government has a chance to investigate the allegations

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[40] *See Ritchie*, 558 F.3d at 1170 n.8 (implying that the FCA compensatory interests have been protected since the government can still bring the action without the relator).

[41] S. REP. NO. 99-345, at 11 (quoting Black, J. in United States *ex rel.* Marcus v. Hess, 317 U.S. 537, 542 n.5 (1943) (citation omitted)).

[42] *See* False Claims Act, 31 U.S.C. § 3730(d)(2) (2006).

[43] *See* S. REP. NO. 99-345, at 1, 7, 23–24.

before the settlement. The government's compensatory interests are inextricably tied with private enforcement suits, and disclosures motivated by promises of release enforceability do little to enhance the government's likelihood of uncovering fraud.

Though the government still has the option to independently bring a qui tam action where a release has been enforced, guilty companies may be willing to bet that the government will not thoroughly investigate or prosecute allegations due to lack of resources.[44] This potential loophole undermines the value of the disclosure that the *Hall* analysis bases release enforceability on since it frustrates the FCA's overall purpose of recovering money. As evidenced by the government's minimum 70% proceeds interest in qui tam actions where it declines to intervene, FCA policies extend considerably beyond the government's awareness and investigation of fraud.[45]

The holding in *Ritchie* fails to fully consider the harm to FCA policies caused by release enforcement and instead emphasizes a contractor's disclosure of fraud allegations without examining the context prompting the disclosure. The *Ritchie* court explained the need for a uniform federal approach to qui tam FCA prefiling releases to preserve the government's right to recover under the FCA but presumed this right had been preserved because the government could still bring a qui tam action against the contractor where the would-be relator could not.[46] This ignores FCA policy interests in recovering losses from fraud through private enforcement actions rather than relying on limited government resources.[47] The *Ritchie* court emphasized the

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[44] A recent report issued by the Government Accountability Office (GAO) discussed how the large volume of audits undertaken by the limited resources of DCAA has contributed to decreased audit quality and higher risk of undetected and unchallenged fraud. U.S. GOV'T ACCOUNTABILITY OFFICE, DCAA AUDITS: WIDESPREAD PROBLEMS WITH AUDIT QUALITY REQUIRE SIGNIFICANT REFORM 36 (2009). Another GAO report highlighted instances where significant deficiencies were removed from DCAA audits under pressure from the Department of Defense and "contracting community" to issue "adequate" audit opinions. U.S. GOV'T ACCOUNTABILITY OFFICE, DCAA: ALLEGATIONS THAT CERTAIN AUDITS AT THREE LOCATIONS DID NOT MEET PROFESSIONAL STANDARDS WERE SUBSTANTIATED 22–25, 29–33 (2008).

[45] *See* False Claims Act, 31 U.S.C. § 3730(d)(2) (2006) (entitling qui tam relators to 25% to 30% of action or settlement proceeds where the government chooses not to intervene).

[46] United States *ex rel.* Ritchie v. Lockheed Martin Corp., 558 F.3d 1161, 1170 n.8 (10th Cir. 2009).

[47] *See* S. REP. NO. 99-345, at 1, 7, 23–24.

interest in encouraging disclosure of fraud allegations,[48] but such disclosure does not add value to the government's efforts under the FCA. By adopting *Hall*, the Tenth Circuit opened the door for government contractors and would-be relators to settle claims more favorably than they might have in qui tam litigation, leaving the federal recovery of funds under the FCA to the scarce resources of the government and thus frustrating the compensatory purpose of the statute.

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[48] *Ritchie*, 558 F.3d at 1171.