

A Brave New World: Defending Against Unclaimed Property False Claims Act Attacks

**Tax Whistleblower is
Awarded \$38 million
by IRS**

**\$21M settlement reached in Texas
EMS agencies, hospital
whistleblower suit**

CFTC ANNOUNCES MULTIPLE
WHISTLEBLOWER AWARDS
TOTALING MORE THAN \$45M

SEC Issues Two
Whistleblower Awards,
Handing Out \$54 Million

Whistle-Blower Awarded \$104 Million by IRS

**Wells Fargo Whistle-
Blower Wins \$5.4 Million
and His Job Back**

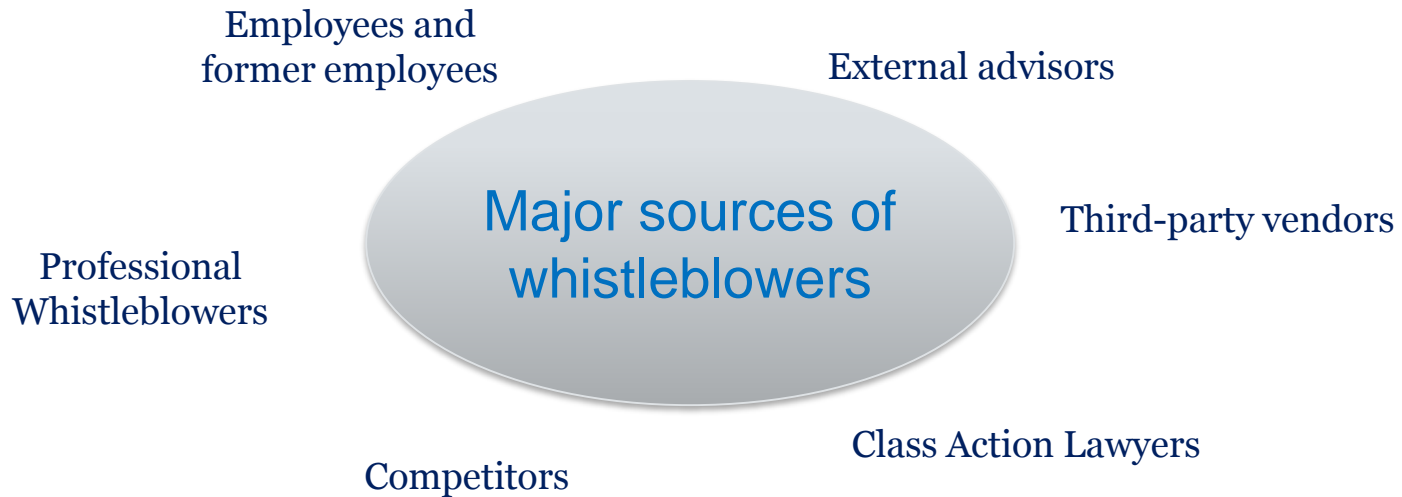
**WALL STREET TIPSTER
GETS RICH OFF IRS
WHISTLEBLOWER
PROGRAM**

- Why You Should Care
- False Claims Act Standards and Defenses
 - Types of Whistleblowers
 - Elements of Claim
 - Damages
 - Procedure
 - Defenses
- Delaware
- New York
- Lessons Learned
- Best Practices

- Retailers with gift card company affiliates or using 3rd-party gift card issuers/managers
- Health care companies with unmatched insurance payments
- Companies with gaps in matching voided checks to re-issued checks
- Companies with historic compliance but with limited historical records
- Any company with a compliance gap

- A state False Claims Act action goes by several additional names
 - *Qui tam*
 - Whistleblower
 - Private attorney general
- Such action allows suit to be brought in the name of a purported defrauded government entity by a person [“relator”] with independent knowledge of the facts.
- Federal whistleblower statute generally used for government contractors or Medicare fraud
- Similar state whistleblower statutes enacted

Types of Whistleblowers



- Protect their position
- Advance the “cause” – do the right thing
- Misunderstanding of the rules
- Financial gain
- Vindictiveness

It Could Happen to You

McDermott
Will & Emery



- Knowing use of a false record or statement material to an obligation to pay money to the State, or
- Knowingly conceals or knowingly and improperly avoids or decreases an obligation to pay money to the State

A “Knowing” Violation Requires:

- Actual knowledge,
- Acting in deliberate ignorance of the law, or
- Acting in reckless disregard of the law

A “knowing” violation may not require proof of specific intent to defraud.

- Not required to be “insiders;” may proceed on behalf of government in declined cases.
- If there has been a prior public disclosure, allegations must be “based upon” independent knowledge and *qui tam* plaintiff must be “original source.”

- Forum
- Burden of Proof
- Discovery
- Privilege
- Confidentiality
- Damages
- Penalties
- Attorney's Fees

- Treble damages (three times unclaimed property liability)
- Attorneys' fees (state and *qui tam* plaintiff)
 - But see *People ex rel. Schad, Diamond & Shedden, P.C. v. My Pillow, Inc.*, 2017 IL App (1st) 152668 (June 15, 2017) (a law firm serving both as client and attorney may not recover statutory attorneys' fees under the Illinois False Claims Act)
- Per occurrence penalties
- Long term public relations issues can also result...
 - Tried in public domain and often labeled as fraud
 - Attorney General may issue press release and hold press conference

- Relator files complaint **under seal**
- State has period to investigate allegations
- State decides whether to intervene in the lawsuit
- If State intervenes, it assumes primary responsibility for the litigation
 - Relator remains a party
 - State may dismiss or settle case even if relator objects and if court deems this action fair
 - Relator may receive 15% - 25% of proceeds

- The State may decline to intervene at the outset.
 - Relator has right to continue the case
 - Relator may recover 25% - 30% of proceeds
 - State may subsequently decide to intervene at any time

- Failure to Meet Heightened Pleading Standard
- Inappropriate Use of False Claims Act
 - Tennessee - *State of Tenn. Ex rel. Beeler, Schad & Diamond P.C. v. Target Corp.*, No. 02-3763-III (Tenn. Chancery Ct. Dec. 1, 2003)
 - Nevada - *Int'l Game Tech., Inc. v. Second Judicial Dist. Court of the State of Nev.*, 127 P.3d 1088 (Nev. 2006)

- State-Related Defenses
 - State-filed motion to dismiss
 - Prior audit history
 - Government knowledge defense
 - Conflicts between FCA and other areas of law (e.g., state constitution)
- Prior Public Disclosure/Not an Original Source

What if general topic is disclosed, but not facts regarding specific defendant?

- Fact-Specific Defenses
 - Audit facts
 - Returns disclosed practice
 - No false statement
 - Reliance on advice of experienced advisor
 - Researched issue
 - Other

- Defenses Based on Legal Arguments
 - Not owed as a matter of law
 - No “knowing” violation because state of the law regarding the obligation is unclear
 - Statute of limitations
 - Reduction of penalty

- Qui Tam Actions are not new in the unclaimed property area
- Examples:
 - *Grayson v. AT&T Corp.* (DC 2009)
 - *State, ex Re. McCann v. Bank of America* (CA 2011)
 - Life Insurance cases (2012)
 - *State of Delaware ex rel. Higgins v. SourceGas LLC* (Delaware 2012)

- *State of Delaware ex rel. French v. Card Compliant*, No. N13C-06-289 FSS (Del. Sup. Ct. 2015)
 - Numerous DE-incorporated retailers alleged to have violated unclaimed property law by failing to remit unclaimed gift card funds after 5 years of inactivity
 - Original over 80 defendants: retailers and restaurants and Card Compliant issuing entities
 - Cards issued by related entities incorporated in a jurisdiction with an exemption. Case removed to federal court; remanded by order finding claims involved questions of state law (12/10/14)
 - 116 page complaint; Delaware joined in 2014
 - Alleged: sham; CardFact entity not actual issuer; lack of economic substance; retailers maintained control of proceeds

- *State of Delaware ex rel. French v. Card Compliant*, No. N13C-06-289 FSS (Del. Sup. Ct. 2015)
 - Some defendants previously subject to Delaware audit or voluntary disclosure agreement
 - Delaware previously accepted arrangement during audits
 - Determination of who was “debtor” and “holder” was central to case

- All defendants except Overstock settled.
 - Reported settlement total between \$25 and \$30 million
- Jury verdict finding against Overstock
 - \$3 million gift card liability
 - Delaware cost-of-goods sold value
 - Treble damages
 - 3 years of liability – there may be subsequent years with allegedly similar conduct
 - One hour of jury deliberation after a five-day trial

- Recent history in tax cases
 - Starbucks example
- New York Attorney General's office may have a FCA investigation with or without a relator
- Current unclaimed property developments

- Court's viewpoint may be influenced by belief in importance of false claims act litigation.
- Court may be challenged by complex intersection of state unclaimed property/false claims act laws.
- "Fact dispute" temptation.
- Emphasize heightened pleading requirement.
- Disclose positions to state/auditors. Record the fact of disclosure
 - Request affirmative guidance?

- Hire the right people. Vet new hires. Monitor stressors. Use a team approach with levels of review.
- Publicize opportunities for internal disclosure and assure confidentiality.

- Know and monitor the law. Set policies and follow them.
- Review basis of and support for positions.
- Prepare legal memoranda supporting positions.
- Contemporaneously map out how positions could be defended – witnesses, documents, etc.

- Have a **robust internal reporting function** and regularly discuss that things are investigated
 - Establish process for receiving internal claims
 - Publicize internal claim process
 - Use process—investigate all reported claims and report generic requests or investigations
 - Publicize results where possible – build a positive internal perception that process works

- **Document and investigate** claims and the results of the investigation
- **Communicate outcomes** and decisions to claimant, where possible
- Conducting an internal investigation
 - Who should conduct the investigation?
 - Should the company hire external counsel? Criteria?
 - Privilege issues: Communications with advisors and consultants that are not lawyers are not privileged, must be turned over to state/relator if asked and can be damning

- Focus on who you hire
 - Background checks
 - Monitor workload and other stressors
 - Use team approach with levels of review
- Involve HR in investigating claims
- Termination procedures

- “Narrow the circle”: limit disclosures of compliance planning/exposure to as small a group as possible
- When privileged information is at issue, preserve the company’s assertion of privilege by warning the relator and any government agency already involved