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False Claims Act cases: A cautionary tale in transactional diligence

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An increase in healthcare deal activity and intense diligence have resulted in False Claims Act (FCA) settlements in which the government has focused not only on the seller but the buyer as well. Third-party buyers may be exposed to liability post-sale related to their diligence findings, the seller's pre-sale operations, and the post-sale response of both parties.

This article will explore the genesis of this relatively new development and the government's approach to the liability of third-party buyers. We will suggest some preventive measures to mitigate the risk exposure of sellers and buyers. The structure of transactions will vary widely, and the structural options to mitigate or isolate liability between and among the parties, the parent entities, and affiliated organizations are beyond the scope of this article.

Our premise is simple. Buyers and sellers participating in a transaction will gain knowledge of sensitive information that may result in a whistleblower, i.e., a qui tam relator, filing an FCA suit. Similarly, a qui tam relator may already have sensitive information, and an FCA suit could be in process or could already have been filed under seal. And the conduct of the respective parties pre-sale and post-sale with respect, particularly, to the issues that surfaced in diligence may heavily influence the outcome of the case.

Case in point

The cases of the Alliance Family of Companies LLC (Alliance) illustrate an example of the focus by the Department of Justice (DOJ) on the conduct of the seller pre-sale and the conduct of both the seller and the buyer post-sale as presented in several qui tam cases.[1] Between March 6, 2017, and May 2, 2019, qui tam relators filed six different FCA cases against Alliance (or a subsidiary or affiliate thereof).[2] At their core, according to the settlement agreement,[3] these cases all involved allegations that Alliance paid independent-contractor neurologists to interpret EEG tests. Alliance allegedly would, in turn, provide these reports free of charge to nonneurologist referring physicians to enable them to bill federal payer programs for the professional interpretations that they did not perform, which the government believed to be an inducement to refer patients to Alliance. Because Alliance received referrals from these physicians, the opportunity to bill and receive payment for the professional interpretations was deemed an inducement to refer. In these cases, the relators also alleged that Alliance filed false claims for services not actually performed as required to bill for the services, and filed claims that relators contended were upcoded.

From an FCA standpoint, the *Alliance* cases are not particularly remarkable. From a transactional standpoint, they serve as a valuable "time out" moment for would-be investors and/or purchasers in businesses that derive income from federal payer programs. Ancor Holdings LP (Ancor), a Texas private investment fund, purchased a minority interest in Alliance following due diligence during which Ancor learned of the alleged conduct.

Following the sale transaction, Ancor entered into a management services agreement to manage Alliance, was paid monthly fees by Alliance, and held two seats on Alliance's Board of Directors. DOJ contended that Ancor "caused false claims when it allowed the alleged conduct . . . to continue during the period July 1, 2017 through January 1, 2020."[4] Ancor closed the sale transaction and became a minority shareholder in Alliance on July 1, 2017. Notably, the settlement agreement contains a provision that states that the parties dispute the government's rendition of the facts. Even if the parties continue to dispute the relevant facts of the underlying six FCA cases, this matter remains a cautionary tale for deal work involving targets that do business with the federal government.

The settlement agreement required Alliance to pay $13,500,000 to resolve allegations that it submitted or caused to be submitted false claims that resulted from kickbacks to referring physicians, or that it sought payment for work not performed, or it sought payment at a higher rate than was justified. In addition, Ancor agreed to pay in excess of $1,800,000 for allegedly causing false billing resulting from the continuation of the alleged misconduct of Alliance through its management services agreement with Alliance.

This case is presented to illustrate that transactional diligence may serve as a basis for liability for buyers. DOJ's allegations in settlement were essentially the following: (1) Alliance was engaged in violations of the federal Anti-Kickback Statute and FCA, (2) Ancor learned of the conduct in diligence and proceeded to purchase an interest in Alliance, (3) Ancor served on the Board of Directors of Alliance post-closing, and (4) Ancor caused the conduct to continue post-closing pursuant to a management services agreement with Alliance.