What Standard Governs the Dismissal of a Relator's Claim for Violation of the False Claims Act's Seal Requirement in an Action Over Hurricane Katrina-Related Insurance Payments?

CASE AT A GLANCE

In the aftermath of the destruction caused by Hurricane Katrina in 2005, Cori and Kerri Rigsby accused State Farm Fire and Casualty Company of falsely misclassifying wind damage as flood damage, among other misdeeds, leaving a federal government-backed flood insurance policy to unnecessarily pay wind damage as flood damage out of United States Government funds. In 2006, the Rigsbys brought suit against State Farm under the federal False Claims Act (FCA). The FCA imposes civil liability on any person who submits false or fraudulent claims to the federal government for payment or approval. "Relators," like the Rigsbys, may bring actions under the FCA for themselves and for the government. If a lawsuit initiated by a relator under the FCA results in civil penalties or the recovery of damages, the award is typically divided between the government and the relator. In 2011, a federal district court in Mississippi awarded the Rigsbys the maximum possible share under the FCA for proving a false claim upon the federal government of $250,000. The court also awarded the Rigsbys over $2.9 million in attorney's fees and expenses. State Farm's appeal from the award seeks to undermine the result based on disclosure violations that the company attributes to the Rigsbys, including violations by the attorneys who initially represented the Rigsbys, of an FCA requirement that claims first be filed "under seal," and not disclosed until allowed under the FCA. This case calls upon the Supreme Court to address how a relator's seal violation affects a relator's right to prosecute and recover for FCA claims and what discretion judges have to police such violations. Relators play a significant role in the instigation of FCA cases. Relator cases are reported to have led to $2.9 billion in FCA recoveries in 2015.

State Farm Fire and Casualty Company v. United States, ex rel. Rigsby
Docket No. 15-513

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ISSUE

What standard governs the dismissal of a relator's claim for violation of the False Claims Act's seal requirement, 31 U.S.C. § 3730(b)(2)?

FACTS

Hurricane Katrina hit the Gulf Coast on August 29, 2005. More than 1,800 people died as severe winds and floods wracked Gulf communities. Many of the homeowners who lost homes or experienced damage had insurance coverage under at least two policies, often issued by the same insurance company. One policy covered flood-caused damage and excluded wind damage. The other covered wind-caused damage and excluded flood damage. A private insurance company frequently administered both policies, with wind damages paid from the insurance company's assets and flood policies paid with government funds through a Federal Emergency Management Agency (FEMA) program. The insurers took a fee for administering the FEMA program policy.

Cori and Kerri Rigsby, both certified and experienced adjusters, and sisters, worked as claims adjusters on Katrina-related claims for a contractor of the State Farm Fire and Casualty Company. The Rigsbys came to believe that State Farm, and others, deliberately overpaid flood insurance claims in order to reduce their own exposure for wind damage. According to Kerri Rigsby, after Katrina, State Farm trainers told its adjusters that they would see "water damage." "The wind wasn't that strong. You are not going to see a lot of wind damage. If you see substantial damage, it will be from water." The Rigsbys also alleged State Farm trainers told adjusters that Katrina was a "water storm" and that "all major damage to homes was caused by flooding." State Farm additionally allegedly told the adjusters to "hit the limits" of flood policies and "to manipulate the totals" to ensure that policy limits were reached.

A few weeks after Katrina, Kerri Rigsby and another adjuster for State Farm inspected a home in Biloxi, Mississippi, covered by two State Farm insurance policies—a FEMA-backed policy that excluded

wind damage and a State Farm policy excluding flood damage. The two adjusters assumed that flooding caused the primary damage to the house and did not do a line-by-line estimate of the damage. The State Farm supervisor approved a maximum flood damage payout. State Farm subsequently retained an engineering company to analyze the damage. The engineering company's report concluded the damage to have been primarily caused by wind.

State Farm refused to pay for the report and withheld the report from the FEMA insurance program file. A State Farm supervisor put a note on the report indicating the bill should not be paid and the report should not be discussed. State Farm arranged for a second report. The second report determined that, although wind damage had occurred, water caused the primary damage to the house. There was evidence that the State Farm supervisor pressured the engineering company to issue reports finding flood damage at the risk of losing contracts with State Farm. The engineer who had concluded wind had caused the damage to the home lost his job.

Kerri Rigsby maintained that she never before saw instructions similar to those she found on the engineer's report. In her experience it was unprecedented to have two engineering reports on a single property, and it was also unusual to see an engineering report prepared just two days after the engineer inspected the property, as was the case with the second report.

These events, among others, led the Rigsbys to believe that State Farm unlawfully had sought to maximize its policyholders flood claims to minimize wind claims at the federal government's expense. The United States reimbursed State Farm for Katrina claim payments made to settle flood policy claims. The payments State Farm had to make to cover wind payments under its homeowner policies fell to State Farm to pay from its own accounts.

The Rigsbys supplied copies of documents to state and federal law enforcement about the claim settlement practices that concerned them. When they disclosed to their employer what they had done, the employer terminated them. The employer also sued them for taking the documents.

The Rigsbys undertook a lawsuit under the federal False Claims Act, often referred to as the FCA. The FCA provides a mechanism for the federal government to recover for false or fraudulent claims presented to the government for payment or approval. The FCA allows the United States Attorney General to bring lawsuits to enforce the FCA. Individuals may also bring suits "for the United States Government" with some limitations, and receive a percentage of the recovery. The suits are commonly called qui tam suits—actions brought by "an informer," under a statute that establishes a penalty for the commission or omission of a certain act.

The Rigsbys' lawyers abided by the FCA's requirement at 31 U.S.C. § 3730(b) that requires the filing of the complaint with the court, in camera, and under seal (unavailable to the public or any defendant), for at least 60 days, and not served on any defendant until the court so orders. They filed the complaint on April 26, 2006, with the case name becoming *United States ex rel. Cori Rigsby and Kerri Rigsby v. State Farm Fire and Casualty Company, et al.* The United States moved to extend the sealing period to allow the government additional time to decide whether to intervene in the action. The federal district court granted the request and issued subsequent orders further extending the sealing period. The court partially lifted the seal in January 2007 to allow the Rigsbys to make certain disclosures in another case in Alabama and fully lifted the seal on August 1, 2007. The government did not intervene, leaving the Rigsbys to pursue the case on their own through their lawyers.

Between April 2006 and January 2007, the Rigsbys and the attorneys who also represented them in other litigation against State Farm, made many public statements against State Farm in which they alleged company misconduct in its claims adjustment practices. The attorneys (Richard Scruggs, and other lawyers associated with the Scruggs Law Firm and the participants in the Scruggs Katrina Group, a joint venture of a number of Mississippi attorneys) also served as the attorneys for a large number of individual property owners making claims against State Farm and other insurers named in the Rigsbys' original FCA complaint, so they did not speak just on the Rigsbys' behalf.

The ABC news magazine 20/20 subsequently included a segment containing excerpts of interviews with the Rigsbys. In the interviews, the Rigsbys discussed their accusation that State Farm had mischaracterized wind damage as water damage to avoid paying legitimate policyholder claims. But the program did not specifically disclose the existence of the FCA suit.

State Farm brought three instances to the federal trial court's attention that had occurred prior to the date of the partial unsealing when the attorneys for the Rigsbys, who no longer represent them, revealed the facts alleged in and the existence of the pending FCA case. The instances all involved disclosure of the document entitled "Relators Evidentiary Disclosures Pursuant to 31 U.S.C. § 3130." Senior District Judge L.T. Senter Jr. of the United States District Court for the Southern District of Mississippi, Southern Division, found the other disclosures identified by State Farm, that he considered relevant, to "reflect, to one degree or another, disclosures and discussions of the underlying facts, but they contain no disclosure of the existence of the FCA action." The judge focused on the 3 disclosures, out of 49 claimed by State Farm, since he concluded that the court mooted the original seal of the qui tam case by partially lifting the seal on January 1, 2007, to allow disclosures in the Alabama case, without specifying that the Alabama disclosures be made under seal.

Judge Senter noted that Attorney Richard Scruggs's assistant had sent a pleading from the FCA case to an ABC News representative on July 28, 2006 (three months after the filing of the FCA case). In August 2006, Attorney Scruggs sent what appeared to be another copy of the FCA evidentiary disclosures to an AP employee. (Judge Senter's opinion does not specify whether "AP" refers to the Associated Press). Scruggs's assistant also sent a copy of the evidentiary disclosures to the *New York Times* in September 2006.

The judge commented: "It is abundantly clear that Richard Scruggs and the SKG [the joint venture of Mississippi attorneys who represented the Rigsbys as well] used formidable public relations resources … in an effort to control the public perception of the case at the heart of this qui tam action. …" He also concluded that the attorneys were not free to disclose the existence of the qui tam case. But he distinguished between the attorneys' efforts to publicize the

claim that State Farm deliberately mischaracterized wind damage as flood damage in assessing claims under the insurance policies it was adjusting and the "improper disclosures" of the Rigsbys qui tam action. According to Judge Senter, "[a]s far as the wind damage claims are concerned, these attorneys were acting well within their rights as advocates for their clients who had home owner policy claims."

But Judge Senter ruled that the record of the case before him did not show that the government's ability to investigate the Rigsbys' allegations had been compromised. He also noted that, although the government declined to intervene in the case, it did not disclose the reasons for its decision and the government had not filed any pleadings that he could use to determine the extent of the damage, if any, that the government believes it sustained. Judge Senter additionally found no evidence that the prepartial unsealing disclosures made by the attorneys to the media had led to a public disclosure by the media that the action had been filed.

The judge determined, too, that the Rigsbys personal role in making the disclosures "was not an active one." Judge Senter ruled that while a client is "responsible for the actions taken by his attorney," there was no showing that the Rigsbys initiated the three improper disclosures and no basis to conclude that the Rigsbys had acted willfully or in bad faith.

The judge did not find any cases decided by the Fifth Circuit Court of Appeals, the circuit that handles appeals from the federal court in which the case was litigated, dealing directly with the issue State Farm had raised. He cited a Ninth Circuit case that says a violation of the sealing requirements does not require dismissal of a qui tam complaint in all circumstances. He acknowledged the Sixth Circuit employs a per se rule that failure to abide by the FCA sealing requirements requires dismissal of the complaint, "but no other circuit court has adopted this per se rule." Judge Senter noted other cases, as well, including a Second Circuit case, for the proposition that failure to file an FCA complaint under seal and to observe other procedural requirements of the FCA may support a district court's exercise of discretion "to impose the sanction of dismissal."

On appeal, the Fifth Circuit affirmed Judge Senter's decision to employ his discretion to reject State Farm's arguments that the court should dismiss the Rigsbys' FCA case. The Fifth Circuit's decision contains other rulings favorable to the Rigsbys including rulings on State Farm's motions for a new trial and judgment notwithstanding the verdict. The lower court had granted the Rigsbys a 30 percent share of the $758,250 award against State Farm and $2,913,228.69 in attorneys' fees and expenses. The Fifth Circuit's decision reversed a ruling that would have deprived the Rigsbys of obtaining other information through further proceedings to support additional FCA claims against State Farm.

The Fifth Circuit in reviewing the case noted the jury's conclusion that the government had suffered damages under the FCA as a result of State Farm's submission of false flood claims and of a "false record." It reasoned that whether a violation of the FCA's seal requirement of 31 U.S.C. § 3730(b)(2) "compels dismissal," presents a statutory interpretation question.

The circuit court ruled: "While cognizant of the justification for and the merits of a per se rule, we conclude that a seal violation does not automatically mandate dismissal." As the Ninth Circuit recognized in *Lujan v. Hughes Aircraft Co.,* 67 F.3d 242 (9th Cir. 1995) "and the government stated as amicus in this case, nothing in the text of § 3730(b)(2) explicitly authorizes dismissal as a sanction for disclosures in violation of the seal requirement" (Internal quotations omitted). Also, "the 1986 amendments [that added the seal provision] to the FCA were intended to encourage more, not fewer private FCA actions."

In applying, the *Lujan* analysis of the appropriate sanction for violations, the Fifth Circuit reviewed the factors of (1) the harm to the government from the violations; (2) the nature of the violations; and (3) whether the violations were made willfully or in bad faith. The court agreed with the district court's assessment that none of the disclosures looked to have resulted in the publication of the existence of the lawsuit before the court partially lifted the seal. "If State Farm was not tipped off about the existence of the suit from the Rigsbys' disclosures, a fundamental purpose of the seal requirement—allowing the government to determine whether to join the suit without tipping off a defendant—was not imperiled."

The court commented that there was, "no indication that the Rigsbys themselves communicated the existence of the suit in the relevant interviews. Were we to impute their former attorneys' disclosures to them, however, we would conclude that they acted in bad faith." But "[e]ven presuming bad faith, the *Lujan* factors favor the Rigsbys. Although they violated the seal requirement, the Rigsbys' breaches do not merit dismissal."

State Farm now seeks to convince the Supreme Court that the Rigsbys repeatedly and willfully violated the seal requirement and that the matter presents "an unprecedented, flagrant disregard for the seal provision—all aimed at generating hostile media coverage as a litigation tactic against petitioner State Farm."

CASE ANALYSIS

State Farm asserts that "the text, structure, history and purpose of the FCA's seal provision support a bright-line rule that a seal violation merits dismissal of a private relator from an FCA case." It maintains that a relator's involvement in a case is conditioned upon "a series of mandatory statutory perquisites, including compliance with the seal requirement." Also, even if the Court rejects a rule of mandatory dismissal, the Court should reverse or vacate the decision below in light of the "egregious conduct" involved in the case. State Farm argues that the considerations supporting this result include "the avalanche of unfavorable publicity that was undeniably damaging to State Farm's reputation."

As factual background, State Farm notes that Richard Scruggs withdrew as the Rigsbys' attorney "after he was indicted in November 2007 for conspiring to bribe a Mississippi state judge." Also, Scruggs paid the Rigsbys annual salaries of $150,000 a year as consultants. State Farm quotes a District Court of Alabama finding that: "Scruggs was the alter ego of the Rigsbys, and the Rigsbys were the alter egos of Scruggs. They could not have been any more closely 'identified' without obtaining a marriage license." State Farm also draws the Court's attention to "video, photographs

and other evidence … that Hurricane Katrina had inundated" the McIntosh house [the home that was the subject of the Rigsbys' misclassified claims case] with approximately five feet of flood water."

The Rigsbys' response to State Farm's position is that the FCA does not specify a consequence if a relator or her attorney violates a seal order. They indicate "the ordinary rule—embraced by the vast majority of courts that have considered the question—is that district courts have discretion to fashion an appropriate sanction." They submit that dismissal ought to be the last resort because it impairs the government's interest in recovering damages for fraud upon the government.

They emphasize that the fraud they discovered was proven before a jury. The attorneys who violated the seal order did so without the Rigsbys knowledge or consent and that those attorneys have been disqualified from the case. The Rigsbys assert the government now stands to "recover billions." (The district court trial addressed the fraud claims for one property leaving open the opportunity for further proceedings on other claims). The Rigsbys argue, "dismissal would award a proven fraudster while punishing the government and the innocent relators—even though the violations prejudiced nobody, and even though the actual violators will suffer no consequence." "Because dismissal would be unjust, unwise and inconsistent with Congress's design in enacting the FCA, this Court should affirm."

The United States has filed a brief as amicus curiae supporting the Rigsbys. It notes: nothing in the FCA suggests that Congress intended to punish every seal violation through the extreme sanction of dismissal of the relator's suit. The text reflects the opposite expectation. "Congress expressly mandated dismissal in particular circumstances, but it declined to do so in the seal provision." The United States supports the application of the standards applied by the court of appeals. It urges the Court to affirm the court of appeals for reasons including that the district court did not abuse its discretion in deciding the case. There is reason to anticipate that the government's reasoning and its support of the Rigsbys' positions and the positions of the district court and circuit court who have considered the Rigsbys' case may be enough to tip the scales in favor of the affirmance.

SIGNIFICANCE

The FCA's reach extends to "any person." The Rigsbys report that the vast majority of FCA cases are filed by relators who have facilitated enforcement of the statute since its enactment in 1863. Changes to the act have encouraged more private enforcement suits. The Rigsbys cite to United States Justice Department Fraud Statistics that indicate the government recovered over $3.5 billion under the statute in 2015, with $2.9 billion coming from whistleblower/relator lawsuits.

As with the Rigsbys case, which is now in its eleventh year, charges of government fraud can engender long and burdensomely expensive litigation for all parties involved, sometimes under the spotlight of national media attention. The landscape of obligations concerning speaking or otherwise communicating about cases under seal is complicated by case law that protects disclosures of underlying allegations but not the existence of an FCA lawsuit while it is under seal. See *American Civil Liberties Union v. Holder,* 673 F. 3d 245 (4th Cir. 2011). The prospects of a partial unsealing mooting a sealing order, as the trial and court of appeals found to have occurred in this case, means the government and parties faced with partial unsealing orders should consider the parameters of such orders carefully when proposed and once adopted.

The Supreme Court's decision, at the least, should resolve the split in the circuits about whether dismissals for seal violations are mandatory. (State Farm refers to the split as a three-way split with the Second and Fourth, the Sixth, and the Ninth Circuits being the circuit courts that have addressed the issue.) Of course, Congress is free to address the question itself, if dissatisfied with the Court's ruling. Battling fraud against the government tends to be a priority regardless of which party controls.

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PREVIEW of United States Supreme Court Cases, pages 44–47.
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