ARNOLD & PORTER LLP

CLIENT ADVISORY

HHS OIG Issues Criteria for Evaluating State False Claims Acts to Fight Medicaid Fraud

August 2026

I. SUMMARY

On August 21, 2006, the Department of Health and Human Services, Office of Inspector General (OIG), issued guidelines for determining whether state false claims acts will qualify states for an additional 10% share of successful Medicaid fraud suits.[1] Currently, in states where they have a state false claims act, the states receive a share equal to the percentage they contribute to their Medicaid programs, which are jointly funded by the federal government. Beginning January 1, 2007, states will be eligible for an additional 10% if the OIG determines that the state law contains provisions similar to the federal False Claims Act (FCA).[2]

This is an important development for drug and medical device manufacturers—and others that have been sued under federal or state false claims acts. Although most states have some sort of false claims act, only a handful currently allow whistleblowers to bring *qui tam* suits on behalf of the government. The OIG's guidelines will likely result in:

- More states enacting false claims acts.
- States including more robust *qui tam* provisions in their existing laws.
- States encouraging whistleblowers and intervening in more cases.
- States using more creative state law theories, including violations of state drug marketing and disclosure laws, as the basis of a state false claims act case.
- More whistleblowers filing cases for Medicaid fraud because they will be entitled to a greater percentage of the proceeds.

1 *See* HHS OIG, Notice, "Publication of OIG's Guidelines for Evaluating State False Claims Acts," 71 Fed. Reg. 48,552 (Aug. 21, 2006).

2 31 U.S.C. §§ 3729-3733.

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II. BACKGROUND

Under the federal FCA, anyone who knowingly submits a false or fraudulent claim to a state Medicaid program must pay three times the federal government's damages, plus penalties of $5,000 or $10,000 for each false or fraudulent claim. The FCA includes *qui tam* provisions that encourage private whistleblowers (known as "relators") to file lawsuits for Medicaid fraud on behalf of the government. The FCA's *qui tam* provisions allow the Department of Justice to investigate the claims and determine whether it wants to intervene and assume responsibility for the suit. If the government intervenes, the whistleblower is entitled to between 15 and 25% of the damages and penalties recovered, depending on the extent to which the relator contributed to the case. If the government chooses not to intervene, the whistleblower can pursue the case alone, and will be entitled to between 25 and 30% of the damages and penalties.

Eleven states and the District of Columbia have enacted their own false claims acts with *qui tam* provisions.[3]

III. CRITERIA

The Deficit Reduction Act requires the OIG to determine whether states have effective false claims acts before the state can qualify for the additional 10% share in recoveries. The OIG must determine whether state laws:

(i) impose liability for knowingly submitting, or causing to be submitted, false or fraudulent claims similar to the FCA;

(ii) reward and facilitate *qui tam* actions at least as much as the FCA does;

(iii) permit suits to be filed under seal for 60 days while being reviewed by the state attorney general; and

(iv) contain a civil penalty that is not less than the penalty authorized in the FCA.[4]

One of the most important criterion is that state laws must adequately reward and facilitate *qui tam* actions at least as much as the federal FCA. For a state law to meet this requirement, it must (a) allow private whistleblowers to sue on behalf of the state government, (b) create an effective system for such suits, including ways to file under seal while the state attorney general reviews the case, and (c) reward the whistleblower with a portion of the recoveries that is at least equal to the FCA. The OIG explains these criteria in detail in its guidelines.

IV. IMPACT

Currently, out nearly 40 states with false claims acts, only 11 states and the District of Columbia permit whistleblowers to file *qui tam* suits.[5] However, several states are in the process of amending or enacting new false claims acts that include more robust *qui tam* provisions. Senator Chuck Grassley (R-IA), Chairman of the Senate Finance Committee, sent a letter to the OIG and Department of Justice urging them to ensure that state false claims acts meet the *qui tam* provisions required by Congress.[6] Grassley explained that although many state legislatures are in the process of crafting state false claims acts, some have deviated from the federal FCA in ways that "may ultimately undermine the ability of whistleblowers to file *qui tam* complaints on behalf of the government." OIG's guidelines include very specific criteria for

3 *See* Robert Fabrikant, *et al., State False Claims Acts*, in Health Care Fraud, Enforcement, and Compliance § 4.01A (American Lawyer Media, Inc., 2006). The states with false claims acts that currently permit *qui tam* suits include California, the District of Columbia, Delaware, Florida, Hawaii, Illinois, Louisiana, Massachusetts, Nevada, Tennessee, Texas, and Virginia.

4 Deficit Reduction Act of 2005, § 1909(b), 42 U.S.C. § 1396h(b).

5 *See* Fabrikant, *et al.* at § 4.01A.

6 *See* Letter from Charles E. Grassley to Daniel R. Levinson of the HHS OIG and Alberto Gonzales of the Department of Justice, (March 21, 2006), at http://www.senate.gov/~finance/press/Gpress/2005/prg032106.pdf.

meeting the *qui tam* requirements, so states have every opportunity to create or tailor laws that qualify for the additional share of Medicaid suits.

With the new OIG guidelines, companies should expect these laws to conform to the OIG's criteria and thus make states eligible for the 10% bonus on successful Medicaid fraud recoveries. Drug and medical device manufacturers should be aware of the increased legal risks associated with the newly written or revised state false claims acts.

First, states have greater financial incentives not only to enact more stringent false claims acts, but to encourage and participate in *qui tam* suits by whistleblowers. State false claims acts have already led to sizeable recoveries.[7] For example, 20 states recovered a total of $29.3 million from a settlement with Medco Health Systems, Inc., one of the largest pharmaceutical benefit managers (PBMs) in the country.[8] States may also develop better relationships with whistleblowers and the private plaintiff's bar. Some observers believe that states have generally been less willing than the Department of Justice to share recoveries with whistleblowers.[9] The new incentives may change that. Moreover, some state attorneys general have begun hiring private plaintiff's firms to bring cases under state false claims acts, which will also help develop the relationship between the state and whistleblowers.

Second, whistleblowers may be encouraged to bring more *qui tam* actions under state law. Whistleblowers may be less intimidated filing suit under state laws and working with state attorneys general than dealing with federal laws and the Department of Justice. Moreover, because some state false claims acts can be appended to federal suits under the theory of "pendant jurisdiction,"[10] whistleblowers may bring more suits if they can recover under both state and federal laws for Medicare and Medicaid fraud.

Finally, state false claims actions may be based on more creative state law theories. A significant number of states have recently enacted aggressive laws that target the marketing and promotional activities of drug and device manufacturers. California, the District of Columbia, Maine, Minnesota, Vermont, and others have enacted such laws. The risk is that whistleblowers or state attorneys general could use these laws to argue that companies are violating the state false claims act.

One mitigating factor is that states are not required to pass laws that meet the criteria set forth by the OIG or the Deficit Reduction Act. States may choose not to enact false claims acts, or may choose to enact laws that do not meet the OIG's requirements.[11] Nevertheless, the additional 10% bonus should provide enough financial incentive for states to implement false claims acts, and most states will likely follow the OIG's guidelines in order to have their laws approved. The Deficit Reduction Act and the OIG guidelines are part of a larger trend of states more actively combating fraud and abuse.

7 *See* Alice G. Gosfield, *Medicaid Fraud Control Units (MFCUs)*, in Medicare and Medicaid Fraud and Abuse § 6:10 (2006).

8 *See, e.g.*, Washington State Attorney General, "Washington Among 20 States to Settle with Medco Health Solutions," (Apr. 26, 2004), at http://www.atg.wa.gov/releases/rel_medco_042604.html; *see also id.* at n.20.

9 Fabrikant, *et al.*, at § 4.01A (*citing* "State Attorneys General Goals Include Consumer Protection, Containing Costs," 8 Health Care Fraud Rep. (BNA) 20: 1079-1092 (Oct. 13, 2004)).

10 Gosfield at § 6:10.

11 Theoretically, the OIG could approve a state law that does not meet all of the OIG's criteria if it finds that the law meets the criteria in the Deficit Reduction Act.

If you have questions about this advisory, or other related issues, please feel free to contact your Arnold & Porter attorney or:

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