

Grant-Fraud Guilty Plea Underscores Potential Civil and Administrative Liability for Recipients of Federal Funds

by John Marti, RJ Zayed, Alex Hontos, and Kirk Schuler

For most individuals and organizations, it does not get much worse than the threat of a criminal conviction. But for recipients of Federal funds—whether providers, grantees, or contractors—a federal criminal conviction is not necessarily the last straw. In addition to consequences like debarment or program exclusion, a unique “statutory estoppel” provision can make it exceptionally difficult to defend against follow-on **civil** False Claims Act liability arising from the same alleged misconduct. An ongoing saga between an executive, his affiliated corporations, and the federal government is a case-in-point.

Recently, a corporate executive and his affiliated corporations pleaded guilty to criminal wire fraud offenses in federal court for filing over \$1 million in false claims with the government. Notably, the defendants had already paid more than \$1 million in restitution for their offenses, and they now await sentencing that could result in additional monetary obligations (fines for the corporations and the executive) and probation or imprisonment for the executive. However, because of the False Claims Act’s “collateral estoppel” provision in 31 U.S.C. § 3731(e), the defendants could also be facing a subsequent civil FCA lawsuit *without any defense to liability*. This case is an important reminder of the interplay between criminal convictions and FCA liability, and the importance of “thinking globally” to resolve government allegations of misconduct.

The executive and his companies applied for grants through two federal programs—the Small Business Innovation Research (“SBIR”) and the Small Business Transfer Technology Research (“STTR”) programs—and ultimately received over \$1 million from three agencies participating in the programs: the National Science Foundation (“NSF”), the National Aeronautics and Space Administration (“NASA”), and the Department of Energy (“DOE”). The fraud occurred because the executive’s companies were basically the same entity. That is, each company shared the same resources and executives (the executive and a few other individuals), and were co-located at a common facility in California. They also performed “essentially equivalent” work, which means, contrary to the SBIR and STTR program requirements, they performed substantially the same research proposed for funding in more than one grant application submitted to one or

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more federal agencies, or they performed work where the specific research objective and the research design for accomplishing the objective were the same or closely related to another grant award regardless of the funding source. In sum, the executive's businesses were impermissibly double-dipping from the federal government's coffers.

The gravity of the situation—the theft of over \$1 million—convinced the United States Attorney's Office for the District of South Dakota to pursue criminal penalties against the defendants. And the executive, attempting to escape the harshest of criminal penalties—prison—agreed to a “package plea” deal with federal prosecutors wherein all defendants would plead guilty and pay full restitution. In return, the prosecutors will recommend probation for the executive.

Interestingly, but not surprisingly, the defendants' plea agreements are silent regarding FCA civil liability. Each defendant pleaded guilty to wire fraud as a result of filing false claims with the government and, in their factual basis statements supporting their guilty pleas, each defendant admitted filing false claims. Their plea agreements, however, merely state (with emphasis added): “No Further Prosecution: The United States agrees that there will be no further federal **criminal** prosecution of [defendants].” Because their plea agreements do not preclude the federal government from pursuing civil claims, the defendants might be exposed—and largely defenseless—to FCA liability. This is because of Section 3731(e), which provides:

(e) Notwithstanding any other provision of law, the Federal Rules of Criminal Procedure, or the Federal Rules of Evidence, a final judgment rendered in favor of the United States in any criminal proceeding charging fraud or false statements, whether upon a verdict after trial or upon a plea of guilty or nolo contendere, **shall estop the defendant from denying the essential elements of the offense in any action which involves the same transaction as in the criminal proceeding** and which is brought under subsection (a) or (b) of section 3730.

31 U.S.C. § 3731(e) (emphasis added). This is the FCA's “statutory estoppel” provision. It derives from the common-law concept of collateral estoppel, which generally precludes litigation of a claim or issue previously decided in another proceeding. Under the FCA's provision, as one court has explained, “[t]he statute makes clear that a criminal conviction . . . estops a defendant in a FCA case from denying the essential elements of [FCA] offenses when the claims involve the same transaction at issue in the defendant's prior criminal proceeding.” *United States v. FastTrain II Corp.*, 2017 U.S. Dist. LEXIS 21268, *11 (S.D. Fla. Feb. 15, 2017). Although this provision is often overlooked, it can come back to haunt criminal defendants, see *id.* at *11 n.7 (citing cases), even resulting in summary judgment against defendants in the subsequent civil cases, see *United States v. Aleff*, 772 F.3d 508, 510 (8th Cir. 2014) (affirming the district court's award of summary judgment).

There are several strategies to mitigate or eliminate the risk of the statutory estoppel provision, however.

First, in the case of a negotiated disposition to the criminal charges, defense counsel

can *try* to obtain a “global” plea agreement to preclude the government from pursuing, based on the alleged conduct, additional criminal *or* civil claims against the defendant. The United States is traditionally reluctant to agree to such global plea agreements. This is for many reasons, but principal among them is the traditional separation between criminal and civil functions. But defense counsel’s request for one is completely justified in light of the exposure created by “statutory estoppel” under the FCA and should be fought for whenever possible. In addition, although it may be difficult to achieve a global resolution through a written plea agreement, verbal or written assurances from the prosecutor as to the United States’ intentions may be possible. In fact, such assurances may be all that can be hoped for and achieved (and perhaps were achieved in the executive’s case—time will only tell).

Second, because the statutory estoppel provision applies to a civil “action which involves the same transaction as in the criminal proceeding,” 31 U.S.C. § 3731(e), defense counsel can try to limit the facts of the criminal proceeding. For example, pleading guilty to only one fraudulent transaction instead of many, and carefully drafting the factual basis in support of a guilty plea to reflect only limited transactions, may limit the exposure under the statutory-estoppel provision. See, e.g., *United States v. Lamanna*, 114 F. Supp. 2d 193, (W.D.N.Y. 2000) (rejecting the government’s argument that the statutory estoppel provision reached fifteen additional alleged fraudulent transactions that were not included in the defendant’s factual basis for his guilty plea); *United States v. Mickman*, Case No. 89-7826, 1993 U.S. Dist. LEXIS 18200, *10 (E.D. Pa. Dec. 22, 1993) (recognizing the preclusive effect of guilty pleas under the FCA’s statutory estoppel provision “extends only so far as the conduct described in the count or counts to which the guilty plea applies”).

Finally, because “the government still bears the burden of proving its damages” in the civil case, *United States v. Nardone*, 782 F. Supp. 996, 998 (M.D. Pa. 1990), defense counsel can also try to minimize proof of loss in the criminal proceeding to avoid being estopped from disputing damages in the FCA case. Whereas “[a]n order of restitution is not a judicial determination of damages,” *United States v. Barnette*, 10 F.3d 1553, 1156 (11th Cir. 1994), a defendant’s admission or a judicial determination of the amount of loss in a criminal case would operate to estop the defendant from arguing against damages in a subsequent civil FCA case, see *United States v. Boutte*, 907 F. Supp. 239, 242 (E.D. Tenn. 1995) (using the district court’s finding of loss in the criminal case as the base number to assess treble damages in the subsequent civil FCA case).

When resolving matters with the Government an individual or organization must think comprehensively about the various remedies—criminal, civil, and administrative—that the government might bring to bear to avoid jumping out of the frying pan right into the fire of something like the FCA’s “statutory estoppel” provision. Only a **global** resolution of all claims (or assurances from the government) will ensure that the resolution is truly and finally resolved.