

Some Serious Strings Attached: Sponsored Research Funding, Adequate Accounting Systems, and False Claims Act Exposure

by Nicole Engisch and Alex Hontos

The federal government awards billions of dollars each year in sponsored research funding to institutions of higher education, academic research institutions, non-profit organizations, and companies—making federal grants an enticing source of funding for research and development. But a recent decision from a Pennsylvania federal court illustrates that non-compliance with federal grant requirements, including the fine print related to compliance systems, creates a material risk to the grantee of not just cost disallowances, but exposure under the False Claims Act (“FCA”), with its treble damages and whistleblower provisions. Recipients of federal research funding looking to allocate finite compliance resources should not overlook the potentially high cost of FCA exposure arising from non-compliance with federal grant terms and conditions, including having inadequate or poorly documented accounting and internal control systems.

Case Background

A recent decision by the U.S. District Court for the Western District of Pennsylvania takes an expansive view of FCA liability for “inadequate” accounting systems under broadly applicable federal grant rules, and provides an interesting case study of how one court assessed grant term non-compliance through an FCA lens. See *United States ex rel. Ruggeri v. Magee-Womens Research Institute and Foundation*, 2:19-CV-862-NR, 2024 WL 1767514 (W.D. Pa. Apr. 24, 2024).

Ruggeri involves a Foundation focusing on women’s health research and education that received 73% of its funding from grants awarded by the National Institutes of Health (“NIH”). As an NIH grant recipient, the Foundation is subject to certain Uniform Guidance (2 C.F.R. § 200 *et seq.*) requirements, such as having adequate financial management and internal controls systems. See 2 C.F.R. § 200.302. Over the lifecycle of the grant, the Foundation was required to provide NIH with financial performance reports and budgets.

A whistleblower brought an FCA *qui tam* action against the Foundation, alleging, in part,

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that the Foundation's accounting and financial systems were "outdated and obsolete," "cumbersome," and limited in their ability to produce reports, budgets, and trace expenditures. The whistleblower alleged that the Foundation's budgets and reports submitted to the NIH "could not be accurate," and therefore the Foundation violated the FCA (1) by falsely certifying that the Foundation's system was compliant, and (2) by making false certifications each time an inaccurate budget or report was submitted to the NIH.

The Foundation moved to dismiss the FCA allegations regarding the Foundation's inadequate accounting system, arguing that the claim failed to establish falsity under Fed. R. Civ. P. 9(b) pleading standards and the FCA's materiality requirement. The district court denied the Foundation's motion, explaining that the whistleblower adequately pleaded an FCA claim on fraudulent inducement and false certification theories. Taking the allegations as true, the court explained that the Foundation's accounting system "couldn't trace budget expenses, couldn't produce accurate monthly reports, and couldn't be used to verify that account funds were being properly spent," as required by the Uniform Grant Guidance and the NIH Grants Policy Statement. Because the Foundation certified in its grant applications and reports that its accounting system were adequate, even though the system was "anything but," the court concluded that the complaint adequately pleaded falsity under the FCA.

The court also held that the whistleblower adequately pleaded materiality under the FCA, emphasizing that the NIH Grants Policy Statement stated that failure to have adequate financial controls was a material violation of the award. The court noted the whistleblower's allegation that the government had pursued investigations against and settlements with other NIH grant recipients for deficient financial controls systems. Finally, the court noted that NIH had reduced the Foundation's grant awards after becoming aware of the allegations, "underscoring that these infractions were material."

Key Takeaways

The *Ruggeri* decision highlights several important realities for recipients of federal grant funding—and the legal teams that advise those grant recipients.

First, the fine print in grant documentation (and the regulations incorporated by reference) can create material risk under fraud, waste, and abuse laws like the FCA. Administrative remedies for breach of grant obligations, although meaningful, typically entail cost disallowances or grant termination. But the FCA adds a material risk vector that ups the ante significantly: treble damages, civil penalties, and investigation costs.

Second, even broad and vague obligations, such as the requirement to have an "adequate" compliance and financial system, are being used to create organizational exposure under the FCA. Internal legal counsel and compliance professionals should ensure that organizational leadership and grant administrators/principal investigators understands the potential exposure—as well as the upside—that comes with accepting federal funding. Legal counsel and compliance professionals should ensure that an organization's investments in compliance systems keep pace with the scale and

sophistication of the organization's federal funding.

Third, certain areas of federal grant compliance continue to generate outsized government-enforcement and whistleblower risk. These include inadequate or misrepresented financial and compliance systems, poor effort reporting/time tracking by grantees, misstatements to funding agencies (in the application process or during the course of performance), inadequate cyber-security and data-security requirements, and lax or false disclosures related to so-called foreign "malign" influence in academic research.

Fourth, a violation of federal grant requirements, without more, is not something that should be policed by the FCA. It is well-established that "[n]ot every regulatory violation is tantamount to making a knowingly false statement to the government." See *United States ex rel. Cantekin v. Univ. of Pittsburgh*, 192 F.3d 402, 416 (3d Cir. 1999). For grantees that attempt to comply in good faith, continue to make smart investments in mitigating the risk that comes with federal funding, and take prompt remedial action (including internal investigations), the risk associated with the FCA should be manageable and not an impediment to the research—and breakthroughs—that federal grants are designed to catalyze.