

“MATERIALITY” AFTER ESCOBAR: THE FIFTH CIRCUIT’S HARMAN DECISION

Robert L. Vogel
Vogel, Slade & Goldstein
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In *United States ex rel. Harman v. Trinity Industries, Inc.*, Case No. 15-41172, 2017 WL 432527966 (5th Cir. Sept. 29, 2017) (“*Harman*”)¹, the United States Court of Appeals for the Fifth Circuit addressed the legal standard for materiality, an issue that has arisen in numerous False Claims Act cases following the Supreme Court’s seminal decision in *Universal Health Servs., Inc. v. United States ex rel. Escobar*, 136 S. Ct. 1989 (2016).

Harman was a *qui tam* case in which the relator, acting on behalf of the United States and various States, alleged that the defendant manufactured a defective structure used in conjunction with highway guardrails, fraudulently obtained approval of the structure by the Federal Highway Administration (“FHWA”), and then sold them to various states, who were purchasing the structures with funds provided by the federal Government. After the United States and the State plaintiffs declined to intervene in the case, the relator proceeded to take the case to trial, where the jury returned a verdict against the defendant. *Harman* at *4. The United States District Court for the Eastern District of Texas entered judgment for the plaintiffs in the amount of \$663,360,750, plus an award of attorneys’ fees and costs to the relator. *Id.* at *5.

While the case was pending, FHWA conducted additional tests and analyses of the guardrail system and re-affirmed its approval. Also, during the pendency of the case and continuing to the present, state governments, with knowledge of the relator’s allegations of wrongdoing, have continued to pay claims for the allegedly defective guardrail device. *Id.* at *4.

On appeal, the Fifth Circuit found the fact that the states continued to pay these claims to be “very strong evidence” that the defendant’s alleged violations of safety standards were not

¹ Throughout this paper, all citations to *Harman* are to the Westlaw cite.

material, and that plaintiffs had failed to rebut this evidence. *Id.* at *16. Accordingly, the Fifth Circuit reversed the district court’s decision, holding “that the finding of fraud cannot stand for want of the element of materiality.” *Id.* at *1.

In addition to its holding based on materiality, the court offered its views on various False Claims Act topics unnecessary for its holding, including damages, falsity, and scienter. *See id.* at *6-*11. This paper will address only the court’s actual holding on materiality, and not on the dicta concerning those other issues.

I. The Facts in *Harman*.

The *Harman* case involved allegations surrounding the “ET-Plus,” a highway guardrail structure known as an “end terminal” system. The ET-Plus was developed by the Texas A&M Transportation Institute (“TTI”); manufactured by Trinity Highway Products, LLC, a Trinity Industries, Inc. (“Trinity”) subsidiary; and subsidized by FHWA. *Id.* at *1. In the continual effort to enhance highway safety and decrease the risk of vehicle impalement by guardrail ends in head-on crashes, TTI engineers created the ET-Plus with a terminal head that would flatten, thrust the guardrail away from the impacted vehicle, and gate the incoming vehicle. Combined, these efforts were intended to slow the vehicle’s speed and significantly decrease the danger of the rail ends to the vehicle and its passengers. *Id.* Continuing to this day, TTI designs the ET-Plus, Trinity manufactures it per TTI’s design, highway contractors purchase and install it on numerous U.S. highways, and the federal government reimburses states for such installations. *Id.*

FHWA must approve the ET-Plus before anyone can purchase the product with federal funds. *Id.* As part of its approval process, FHWA can require the manufacturer to test its products, except for those that are deemed “nearly certain to be safe” or that are “so similar to

currently accepted features that there is little doubt that they would perform acceptably.” *Id.* In 2000, TTI tested and FHWA approved the ET-Plus for utilization on the National Highway system in conjunction with guardrails that were 27^{3/4} inches high. *Id.* at *2.

In response to the growing numbers of vehicles with taller centers of gravity, TTI modified the ET-Plus in 2005 for use on guardrails 31 inches high; in the process, TTI altered the ET-Plus’ terminal head width from five to four inches and made other essential fabrication modifications. *Id.* Trinity maintained that this altered four inch terminal head was included in the guardrail system during TTI’s crash testing of the product at the 31-inch height, and that Trinity sent a detailed drawing of this modified head, along with the other fabrication changes, to TTI for inclusion in its crash report. *Id.* TTI prepared the crash report and sent it to Trinity, who then sent it to FHWA and ultimately secured FHWA approval for the ET-Plus at the 31-inch height on September 2, 2005. *Id.* However, TTI had inadvertently omitted Trinity’s detailed drawing of the modified head and any discussion of the altered head and the related essential fabrication changes from its report, despite having included in its discussion the other modifications made to conform to the 31-inch height. Trinity later sent the drawing to FHWA. *Id.*

The Relator in this case, Joshua Harman, was a Trinity customer who had bought and installed its products in the United States. *Id.* In addition, as the Fifth Circuit observed, Harman was also a Trinity competitor who had co-owned two businesses that manufactured terminal heads. *Id.* Harman conducted a cross-country exploration of guardrail accidents, obtained six to eight ET-Plus heads, and found several changes he deemed responsible for the accidents—the biggest being the modified terminal head width. *Id.* at *3. According to Harman, this modified

head width, combined with the various other width and height alterations, turned the ET-Plus into an entirely different product. *Id.*

Following these discoveries, Harman met with FHWA in January 2012 to make a PowerPoint presentation of his findings of the 2005 ET-Plus changes—including the terminal head width change, a shortened guide channel, a decreased extruder chamber height, a narrowed exit gap, and other changes—and to share photographs from various guardrail accidents. *Id.* An FHWA representative, Nicholas Artimovich, took measurements and photographs of the ET-Plus heads Harman brought to the meeting. *Id.*

In February 2012, FHWA met and discussed Harman's claims with Trinity, who explained that the crash test had included the altered terminal head and that TTI had inadvertently omitted information regarding this width change in the report it sent to FHWA. *Id.* While FHWA met two more times with Harman and Harman's counsel, the agency simultaneously confirmed the ET-Plus' eligibility for reimbursement to numerous state departments of transportation. *Id.*

Harman filed a *qui tam* complaint against Trinity on March 6, 2012. *Id.* Ten months later, the Government declined to intervene in the case. *Id.* Following Harman's *Touhy* request to FHWA to make available for deposition its employees, the FHWA circulated an official memorandum, dated June 14, 2014, asserting that the modified ET-Plus with the narrower terminal head had been tested and approved for reimbursement, while also stating that this ongoing approval had never been interrupted since its initial approval in 2005. *Id.* In response to Harman's *Touhy* request, the DOJ emailed Harman FHWA's memorandum and noted DOT's belief that the memorandum precluded the need for any government employee testimony. *Id.*

Trinity moved for summary judgement on the basis of the memorandum, but the district court denied the motion and the case went to trial. *Id.* at *4. The first trial ended in a mistrial due to the court's finding that both parties had engaged in inappropriate conduct. *Id.* Trinity subsequently asked the Fifth Circuit for a writ of mandamus. Although the court of appeals denied the writ, it stated, based on the "FHWA's authoritative June 17, 2014 letter," that "a strong argument can be made that the defendant's actions were neither material nor were any false claims based on false certifications presented to the government." *Id.* The district court held a second trial, which lasted six days. *Id.* At the conclusion of the trial, the jury found in favor of the United States and against Trinity. *Id.* Trinity then renewed to the district court a Rule 50(b) motion for judgement as a matter of law. *Id.*

After the jury returned its verdict and amidst the ensuing publicity and queries from state Attorneys General concerning the ET-Plus, the government maintained its approval of the ET-Plus but ordered that a joint task force independently examine and crash-test the installed devices across the United States. *Id.* The task force scrutinized more than one thousand ET-Plus installation systems, existing between November 2014 and January 2015, and found that the installed ET-Plus systems were all of one version across the country and that this version was indeed what TTI had successfully crash-tested in pursuit of its 2005 FWHA approval. *Id.* Notwithstanding this new finding, the district court denied Trinity's motion for judgment as a matter of law and entered its final judgement in favor of Harman for \$663,360,750. *Id.* at *5. Trinity then filed a motion for a new trial, based in part on the results of the post-trial crash tests and the findings of the joint task force. *Id.* The district court denied Trinity's motion for a new trial, and Trinity then filed an appeal to the Fifth Circuit.

II. The Harman Court's Holding.

In *Harman*, the Fifth Circuit held that Trinity was entitled to prevail at trial because there was insufficient evidence of the materiality of any false statements or omissions. Focusing primarily on the evidence that the Government continued to pay for the Trinity guardrails notwithstanding the Government’s knowledge of their purported deficiencies, the court of appeals quoted from, and focused on, the following passage from *Escobar*:

[I]f the Government pays a particular claim in full despite its actual knowledge that certain requirements were violated, that is very strong evidence that those requirements are not material. Or, if the Government regularly pays a particular type of claim in full despite actual knowledge that certain requirements were violated, and has signaled no change in position, that is strong evidence that the requirements are not material.

Id. at *11, citing *Escobar*, 136 S. Ct. at 2003-04.

The court of appeals noted that in *Escobar*, the Supreme Court held that in determining materiality, one should look “to the effect on the likely *or actual* behavior of the recipient of the alleged misrepresentation.” *Harman* at *11, citing *Escobar*, 136 S. Ct. at 2002 (emphasis in the original).

The *Harman* court then examined several other post-*Escobar* circuit court decisions regarding materiality in situations comparable to the one in *Harman*, *i.e.*, where the government had continued to pay claims after learning that such claims were for goods or services that were allegedly noncompliant with relevant rules or guidelines. *Id.* at *11-*13.² Summarizing these holdings, and comparing them to the *Harman* case, the *Harman* court wrote:

The lesson we draw from these well-considered opinions is that, though not dispositive, continued payment by the federal government after it learns of the alleged fraud substantially increases the burden on the relator in establishing materiality. Notably these cases do not fully address the gravity and clarity of the

² The post-*Escobar* circuit court cases discussed in this portion of the *Harman* opinion were: *D’Agnostino v. EV3, Inc.*, 845 F.3d 1 (1st Cir. 2016); *United States v. Sanford-Brown, Ltd.*, 840 F.3d 445 (7th Cir. 2016); *United States ex rel. Kelly v. Serco, Inc.*, 846 F.3d 325 (9th Cir. 2017); *United States ex rel. McBride v. Halliburton Co.*, 848 F.3d 1027 (D.C. Cir. 2017); *United States ex rel. Petratos v. Genentech, Inc.*, 855 F.3d 481 (3d Cir. 2017).

government's decision here. This system was installed throughout the United States, and the government's rejection of Harman's assertions, if in error, risked the lives on our nation's highways, not just undue expense. Where violations of the 'certain requirements' described by *Escobar* involve potential for horrific loss of life and limb, the government has strong incentives to reject nonconforming products, and *Escobar*'s cautions have particular bite when deployed to decisions as here. Further, this case is not about inferring government approval from continued payment. Here, the government has never retracted its explicit approval, instead stating that an 'unbroken chain of eligibility' has existed since 2005.

Id. at *13.

Importantly, the *Harman* court stopped short of establishing an ironclad rule, cautioning: "[T]here are and must be boundaries to government tolerance of a supplier's failure to abide by its rules." *Id.* The court of appeals pointed out that the Ninth Circuit had offered some guidance in the case of *United States ex rel. Campie v. Giliad Sciences, Inc.*, 862 F.3d 890 (9th Cir. 2017). The *Harman* court noted that in *Campie*, the Ninth Circuit had rejected—at the pleading stage of the case—the argument that the government's continued payment for drugs after it learned of allegations of FDA violations mandated dismissal of the case for lack of materiality. *Harman* at *13. The *Harman* court noted that the Ninth Circuit found in *Campie* that "(1) questions remained as to whether the approval by the FDA was itself procured by fraud; (2) there existed other potential reasons for continued approval that prevent judgment for the defendant on 12(b)(6); and (3) the continued payment came after the alleged noncompliance had terminated and 'the government's decision to keep paying for compliant drugs does not have the same significance as if the government continued to pay despite noncompliance.'" The *Harman* court further pointed out that that the parties in *Campie* disputed "exactly what and when the

government knew, calling into question its actual knowledge.” *Id.*, citing *Campie*, 862 F.3d at 906-07.³

The *Harman* court concluded that while it agreed with other courts that “no single factor is outcome determinative, the ‘very strong evidence’ here of FHWA’s continued payment remains unrebutted.” *Id.* at 14. The court proceeded to discuss in detail the evidence that the relator introduced at trial, and found that the relator’s evidence did not really address or rebut the fact that the FHWA, with full knowledge of the relator’s claims about the purported deficiencies in the ET-Plus system, continued to approve that system. *Id.* at *14-*16.

³ The *Harman* court also pointed out that, after the Supreme Court remanded the *Escobar* case to the court of appeals, the First Circuit found that the relator had met his burden on materiality, finding “no evidence that the relevant government agency had actual knowledge of any violations when it decided to pay the claims.” *Harman* at *11, citing *United States ex rel. Escobar v. Universal Health Serv., Inc.*, 842 F.3d 103, 110 (1st Cir. 2016).