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CIVIL FALSE CLAIMS ACT: Court Applies *Contra Proferentem* Doctrine against the Government in an FCA Case Based on an Ambiguous Contract Provision

In order to resolve the "falsity" element in many False Claims Act ("FCA") cases, courts often must grapple with the meaning of the contractual or regulatory term alleged to have been violated. The issue often is presented for court resolution when the FCA defendant argues that the relevant terms are ambiguous or, at worst, subject to a reasonable interpretation that obviates the claimed violation. Many courts faced with such ambiguity arguments in FCA cases have deferred the issue with respect to FCA "falsity" and have instead addressed it as part of the FCA "knowledge" or "intent" element. *See United States ex rel. K & R Ltd. P'ship v. Massachusetts Hous. Fin. Agency*, 530 F.3d 980 (D.C. Cir. 2008); *United States ex rel. Farmer v. City of Houston*, 523 F.3d 333 (5th Cir. 2008); *United States ex rel. Oliver v. Parsons Co.*, 195 F.3d 457 (9th Cir. 1999). *See also* FraudMail Alert No. 08-07-09, *DC Circuit, Applying Supreme Court's Decision in Safeco to False Claims Act, Finds Lack of "Reckless Disregard" in FCA Allegations Based on Ambiguous Government Requirements* (July 9, 2008). In addressing contractual ambiguity arguments under the FCA, however, it has been rare for courts to apply the interpretive rule known as the doctrine of *contra proferentem*. The rule is based on a principle of fundamental fairness: a party that drafts and imposes an ambiguous term should not benefit from that ambiguity. While courts have long recognized and applied this general rule of contract interpretation that requires a latent ambiguity in a contract provision to be construed against the party that drafted the provision in other contexts, such as traditional contract and insurance cases, the rule had not been applied in a reported FCA case. That circumstance changed last month.

In *Chapman Law Firm v. United States*, No. 09-891C, 2012 WL 256090 (Fed. Cl. Jan. 18, 2012), the U.S. Court of Federal Claims applied the doctrine to the interpretation of an ambiguous term in a Department of Housing and Urban Development ("HUD") contract underlying an FCA counterclaim asserted by the government. In doing so, the court found that the contractor's interpretation was reasonable, and denied the government's motion for partial summary judgment. The application of this contract interpretation doctrine in an FCA case should not be surprising, but it is significant because it makes clear that, in certain FCA cases, fraud claims cannot rest on facially ambiguous contract provisions. Moreover, the rationale of the doctrine applies in areas outside of contracts, and FCA defendants should therefore be able to assert the *contra proferentem* doctrine as a defense in cases in which the underlying theory of FCA liability rests on ambiguous contract and grant terms and conditions or on ambiguous government-drafted regulations.

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The Contract Dispute in *Chapman*

HUD awarded the Chapman law firm ("Chapman") a contract for the management and marketing of single family homes in Ohio and Michigan. The contract specified that (a) Chapman was required to "routinely inspect and take all actions necessary to preserve, protect and maintain each [HUD] property," and (b) inspections for wood-destroying organisms ("WDO") were to be performed on each home. Pursuant to applicable state law, WDO inspections were to be carried out by licensed inspectors when requested by a party involved in "a contemplated real estate transaction." Following an anonymous tip to the Ohio Department of Agriculture, a state official interviewed Chapman personnel about how inspections were done. According to the official's report, Chapman had performed general HUD inspections and certain WDO inspections, putting completed pest inspection forms relating to its inspections on a website for marketing purposes. The state official advised Chapman that the pest inspection forms were for licensed WDO inspections only and were not to be used for any other inspection or purpose. After receiving this advice, Chapman removed the forms from the website, and the state official concluded that Chapman committed no error in conducting WDO inspections using unlicensed inspectors. Shortly after Chapman received the state official's report, however, HUD declined to exercise an option under the contract.

In response to HUD's decision not to extend the contract, Chapman requested an equitable adjustment under the contract to recover costs Chapman incurred as a result of the government's pre-performance, stop work orders, and other changes in the contract. When HUD rejected the equitable adjustment request, Chapman filed a complaint in the Court of Federal Claims seeking reimbursement from HUD for these incurred costs.

The government's answer to Chapman's complaint asserted various affirmative defenses, but the government also asserted a counterclaim under the False Claims Act alleging that Chapman had knowingly violated a key contract term and thus submitted false claims to HUD. The government's FCA claim rested on its theory that the contract and Ohio law required Chapman to employ licensed inspectors to perform WDO inspections for the HUD properties and that Chapman knowingly failed to comply with that requirement.

Chapman contended that "a contemplated real estate transaction" referred to an impending sale of the property, and that inspections before houses were listed for sale did not involve such a transaction because no purchaser for the property was yet identified. The government argued that because it was considering the eventual sale of the property, the "contemplated real estate transaction" requirement was met by the potential seller—HUD—alone. Both parties stipulated that Chapman performed certain inspections using unlicensed inspectors. The government moved for summary judgment, arguing that its interpretation of the contract entitled it to judgment as a matter of law.

The Court's Application of *Contra Proferentem*

With Chapman and the government disagreeing over how to interpret the phrase—"a contemplated real estate transaction"—the court had to confront this key contract interpretation dispute. It did so and concluded that the phrase was ambiguous because both parties' interpretations fell "within a 'zone of reasonableness.'" *Chapman*, 2012 WL 256090, at *14.

The court first noted that the Federal Circuit has applied the doctrine of *contra proferentem* in contract disputes where an ambiguity was not so glaring or substantial that a duty to inquire was required. The

doctrine applied "[w]hen a dispute arises as to the interpretation of a contract and the contractor's interpretation is reasonable," and required "that ambiguous or unclear terms that are subject to more than one reasonable interpretation be construed against the party who drafted the document." *Id.* at *12. The court concluded that Chapman's interpretation of the disputed language was reasonable, and construed the disputed provision less favorably to the government because HUD had drafted the contractual language:

> HUD drafted and selected the contractual language, which incorporated Ohio Administrative Code § 901:5-11-01 as written. The doctrine of *contra proferentem* favors accepting plaintiff's interpretation of the disputed, ambiguous phrase, "party involved in a contemplated real estate transaction," and the court construes the disputed provision "less favorably" to defendant. *United States v. Seckinger*, 397 U.S. at 216. The court, therefore, finds that when conducting the WDO inspections prior to listing the properties to prepare the properties for sale, and prior to identification of a buyer, Chapman was in compliance with its duties of performance under the terms of the Ohio state law as incorporated into the Contract between the parties. Moreover, the Ohio Department of Agriculture inspector, interpreting and implementing the state statute found that plaintiff had not violated the Ohio Revised Code when it did not use Ohio licensed inspectors. The only violation the state inspector found was incorrect posting of the NPMA–33 forms online, which plaintiff corrected.

Id. at *15. Thus, the court accepted Chapman's interpretation of the contract, and of Ohio law as incorporated into the contract, and found that the inspections complied with Chapman's interpretation. The court noted that, if HUD had intended to mandate that all inspections under the contract must be conducted by Ohio licensed inspectors, it could have drafted the contract to make that requirement clear.

The Significance of the *Contra Proferentem* Doctrine in FCA Cases

The *contra proferentem* doctrine can be significant in a broad spectrum of FCA cases. Most FCA disputes involve an allegation that requirements incorporated into government grants, contracts, and regulations have been violated. Of particular concern to defendants are FCA allegations that employ the false certification theory of liability, under which expansive liability may be premised on a multitude of such requirements. *See* FraudMail Alert No. 10-11-03, *Fifth Circuit Holds "Prerequisite to Payment" is a Fundamental Requirement in Establishing "Falsity" in a False Certification Case* (Nov. 3, 2010). These requirements are drafted by the government, and where they are ambiguous or capable of more than one reasonable interpretation, the rule that ambiguous requirements are construed against the drafter places the burden on the government to draft clear requirements, which is where that burden belongs. Indeed, as the court in *Chapman* observed

> [i]n government contract cases, when the government drafts or selects the contract language this principle is accorded "considerable emphasis" because of the government's resources and stronger bargaining position in contract negotiations.

Id. at *13. This issue is not limited to FCA cases that are based on government contracts; it is also present in FCA cases in the health care area as well as in any other highly regulated area where the government drafts and imposes requirements. Given the government's direct responsibility for drafting

requirements in grants and regulations in these areas, this principle is equally applicable to FCA claims based on those requirements. This rule necessarily applies to *qui tam* relators, whose standing to sue is premised on the government's claim.

In addition, the doctrine provides an argument that a statement or claim is not "false," rather than simply an argument that the false claim was not submitted "knowingly." Allowing ambiguity to be considered on the issue of falsity adds the opportunity for early dismissal in FCA cases involving alleged violations of ambiguous requirements in contracts, grants, or regulations, after a limited inquiry into the reasonableness of the contractor's interpretation of the requirement. If the defendant's interpretation is reasonable, this limited inquiry into the "falsity" of the FCA claim could obviate the need to assess other elements of liability, particularly the often subjective and fact-laden element of intent. *Cf. United States ex rel. K & R Ltd. P'ship v. Massachusetts Hous. Fin. Agency*, 530 F.3d 980 (D.C. Cir. 2008) (affirming summary judgment for FCA defendant based on lack of intent where defendant's interpretation of ambiguous provision was reasonable); *United States ex rel. Oliver v. Parsons Co.*, 195 F.3d 457, 464 (9th Cir. 1999) (ruling that "[a] contractor relying on a good faith interpretation of a regulation is not subject to liability, not because his or her interpretation was correct or 'reasonable' but because the good faith nature of his or her action forecloses the possibility that the scienter requirement is met").

Application of this doctrine is critical in FCA cases that rest on ambiguous contract provisions, regulations, or other requirements in government-drafted legal documents. It should be noted that, as the court pointed out in *Chapman*, the doctrine of *contra proferentem* is most useful for resolving "latent" ambiguities that do not raise the duty to inquire that comes into play when an ambiguity is glaring or obvious. In cases of "patent" ambiguities, the doctrine may still apply, although the contractor's efforts to determine the meaning of the ambiguous requirement will also need to be assessed. Nonetheless, this case opens the door to the argument in a number of FCA cases and, importantly, holds the government accountable—if it wishes to base a fraud claim on ambiguous language in key requirements—for not cogently setting forth those key requirements.

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