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The Jurisdictional Conflict At Center Of 9th Circ. FCA Case

By **Douglas Baruch, Jennifer Wollenberg and James Nelson**
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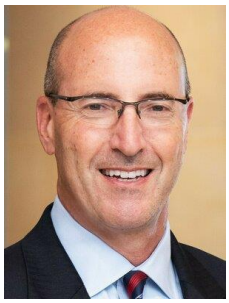

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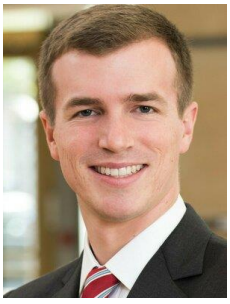

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In a pending case, Island Industries Inc. v. Sigma Corp., the U.S. Court of Appeals for the Ninth Circuit is poised to decide whether district courts have subject matter jurisdiction over False Claims Act qui tam actions that are based on alleged avoidance of customs duties.

Federal district courts generally have jurisdiction over FCA claims brought by either the U.S. or a qui tam relator.[1]

However, in FCA cases based on violations of customs laws and regulations — which are appearing with increasing frequency — that general grant of jurisdiction clashes with Title 28 of the U.S. Code, Section 1582(3). This section provides that the "Court of International Trade shall have exclusive jurisdiction of a civil action which arises out of an import action and which is commenced by the United States ... to recover customs duties."

As the typical allegation in FCA cases based on violations of customs laws is that the defendant committed a reverse false claims violation under FCA Section 3729(a)(1)(G) by avoiding payment of customs duties, this jurisdictional conflict has major import for the litigation — and potentially for the viability — of these cases.

Now, for the first time in nearly 20 years, a federal circuit court of appeals is likely to address it.

Background of Island Industries Inc. v. Sigma Corp.

Island Industries is a nonintervened qui tam action in which the relator, Island Industries, alleged that business competitors — including the defendant, Sigma Corp. — committed FCA violations by failing to pay anti-dumping duties on certain imported pipe fittings.

At trial in the U.S. District Court for the Central District of California, the jury returned a verdict against Sigma and found $8 million in damages based on the avoided duties, after which the district court entered judgment for $26 million — treble damages plus statutory penalties.

Sigma appealed to the Ninth Circuit, which held oral argument in January.[2] At argument, the government — which had filed an amicus curiae brief in support of Island Industries — was allotted time to argue.

Although jurisdiction was not argued in any of the appellate briefings, one of the panel members asked the government to address subject matter jurisdiction in light of the Ninth Circuit's 2004 decision in U.S. v. Universal Fruits & Vegetables Corp., in which the court had held that district courts lack jurisdiction over FCA cases brought by the government seeking unpaid customs duties because the CIT had exclusive jurisdiction over such actions.

Following the argument, the court directed the parties and the government to brief this question, particularly "addressing whether the district court lacked subject-matter jurisdiction over [the] suit" even though it was "prosecuted by a private relator."[3]

Background of U.S. v. Universal Fruits & Vegetables Corp.

In 2004, the Ninth Circuit held that an FCA lawsuit by the U.S. based on unpaid customs duties was a lawsuit to recover customs duties, and thus fell within the exclusive jurisdiction of the CIT.[4]

The court reasoned that "at least part of the government's damages" in the FCA case — if it were to prevail — "will be 'customs duties,' namely the antidumping tariffs it claims Universal fraudulently evaded." So, no matter how the government creatively frames the complaint, an FCA case is still a suit for customs duties.[5]

As a result of this holding, the court reversed the district court's merits holding and remanded with instructions to transfer the case to the CIT.

After provisionally accepting transfer of the case given the plausibility of jurisdiction in the CIT,[6] the CIT eventually held that it did not have jurisdiction over the government's reverse FCA claim against the importer because it only had jurisdiction over the effort to recover customs duties — not FCA treble damages and per-claim penalties.[7]

Despite that holding appearing to conflict with the Ninth Circuit's decision that the CIT had exclusive jurisdiction over the case, and even though there was some activity following the holding — an appeal by the government that later was voluntarily dismissed, and litigation over the defendant's attorney fees — the U.S. Court of Appeals for the Federal Circuit has never addressed the jurisdictional question of whether the CIT may adjudicate FCA cases based on unpaid customs duties.

Arguments Against a Relator's Pursuit of Customs-Based FCA Cases

Not surprisingly, Sigma is arguing that the Ninth Circuit's Universal Fruits rationale naturally and properly should be extended to qui tam cases brought in the name of the U.S. since the government remains the real party in interest, whether or not it intervenes in the action.

It is well established that a qui tam relator stands in the shoes of the government and is acting on the government's behalf with respect to substantive FCA claims.

For instance, the U.S. Court of Appeals for the Eleventh Circuit held in its 2021 Yates v. Pinellas

Hematology & Oncology PA decision that the Eighth Amendment governs nonintervened qui tam actions because, in reality, it is the U.S. that imposes a fine.[8]

The Eleventh Circuit wrote that even where the U.S. "is not a formal party in a non-intervened qui tam action, in such a case the relator prosecutes the suit 'in the name of the'" U.S., and is "a partial assignee of the United States' damages claim."[9]

Put differently, an FCA relator is a government actor because, as the court wrote, the relator performs "'a function which is traditionally the exclusive prerogative of the state.'"[10]

The U.S. Supreme Court has described FCA relators in the same terms — as filing suit on behalf of the U.S. as the government's assignee.[11] The relator is the government's stand-in, and the U.S. remains at all times the real party in interest in FCA cases.[12]

Other federal appellate courts have made clear that the U.S. is the real party in interest in any FCA qui tam action.[13] Indeed, as the Supreme Court held in the 1991 Edmonson v. Leesville Concrete Co. decision, "[t]he fact that the government delegates some portion of [its] power to private litigants does not change the governmental character of the power exercised."[14]

In addition, as the relator's brief in Island Industries notes, under current law "the United States cannot file FCA actions relating to customs duties in either the CIT or in any district court in the Ninth Circuit."

Permitting qui tam lawsuits in district court would, for all intents and purposes, upend that law and invite mischief. The government would be incentivized to defer customs enforcement to relators for fear that taking affirmative steps would defeat jurisdiction over an FCA case.

Through deference to relators, the U.S. would be able to escape the exclusive jurisdiction of the CIT. And the government's enforcement decisions would not be driven by the merits or other valid considerations, but out of necessity for FCA claim preservation.

However, there should be no concern that — in the absence of district court or CIT jurisdiction over customs-based FCA cases — the U.S. will be without a remedy or that potential whistleblowers would be discouraged.

To the contrary, as the Ninth Circuit recognized in Universal Fruits, the customs laws enable the government to pursue customs duties remedies, including penalties and fines, where appropriate, and provides a federal court forum in which such actions can be contested.

Moreover, whistleblowers remain incentivized to report potential customs violations via the whistleblower reward provisions of Title 19 of the U.S. Code, Section 1619, which authorize a recovery not to exceed 25% to a person who provides information leading to a recovery of any duties withheld.

Arguments in Favor of District Court Jurisdiction Over Customs-Based Qui Tam Suits

In their respective supplemental briefing in the Island Industries case, the government and the relator point out that in Universal Fruits, the CIT later dismissed the action, finding that it lacked jurisdiction over FCA cases.

For its part, the government seized on this fact and dedicated a substantial portion of its brief to arguing that the Ninth Circuit's 2004 decision was wrongly decided.

However, the government recognized that only an en banc court can reverse that 2004 holding. As a result, the government also argued that the jurisdictional bar should not extend to cases brought by relators because those are not commenced by the U.S. within the meaning of the exclusive jurisdiction language of Section1582.[15]

The government pointed to district court decisions finding jurisdiction over customs-related FCA cases initiated by relators instead of the U.S.[16]

In its submission to the Ninth Circuit, the relator made similar arguments. It argued that the phrase "commenced by the United States" requires the government, rather than a relator, to initiate the lawsuit.

The relator highlighted the different procedures at the beginning and end of cases depending on whether they are initiated by the government or relators, and invited the Ninth Circuit to distinguish between cases brought on behalf of the U.S. and cases initiated by the U.S.

Finally, the relator argued that the Eleventh Circuit's Yates decision cited by Sigma in its brief — that an FCA penalty is a fine imposed by the U.S., even in a qui tam case — does not support the position that the U.S. commenced the lawsuit in the first place.

Key Takeaways

Through its sua sponte identification of a potential subject matter jurisdiction defect, the Ninth Circuit has resurrected an issue that has received little attention in the last 20 years.

Notably, no other circuit court has addressed this question, and the Universal Fruits case itself has rarely been cited for its jurisdictional holding.

It is somewhat surprising that the Universal Fruits holding has not been frequently raised as a jurisdictional defense in FCA cases, especially in the Ninth Circuit.

Whether any federal court has jurisdiction over FCA claims based on alleged avoidance of customs duties — meaning that the government's only remedy is to pursue recovery under the customs laws in the CIT — is not an insignificant question.

The government aptly summarized the import of this issue in its recent filing in the Island Industries case:

If this court accepts Sigma's invitation to extend Universal Fruits and hold that district courts also lack jurisdiction over both customs-related qui tam suits and suits initiated by the U.S., it will effectively create a customs-related exception to the FCA within this circuit.

While the appellate court in Island Industries could bypass the question by finding that Universal Fruits does not apply to qui tam cases, it is possible that it will issue a decision that could have enormous consequences by determining that district courts in the Ninth Circuit do not have jurisdiction over any customs-based FCA case.

Moreover, regardless of the decision by the Island Industries court, pending further action by an en banc Ninth Circuit, the current law in that circuit provides that no district court has jurisdiction over such FCA cases when they are brought directly by the government.

And because the Ninth Circuit's Universal Fruits holding has not been addressed by any other circuit courts, defendants facing FCA suits — both government- and relator-initiated suits — based on customs violations should consider raising it and the CIT's exclusive jurisdiction as a defense when such suits are brought outside of the Ninth Circuit.

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Disclosure: The authors were counsel to the National Association of Manufacturers and the U.S. Chamber of Commerce in an amici curiae brief filed in support of Sigma's appeal in the Island Industries matter.

[1] 31 U.S.C. § 3732(a).

[2] Apart from the jurisdictional issues that are the subject of this article, the appeal raises significant issues including the application of "objective reasonableness," materiality, and damages.

[3] Case No. 22-55063, Dkt. No. 59 (9th Cir. Jan. 23, 2023). Supplemental briefing on this question was completed as of February 21, 2023.

[4] United States v. Universal Fruits & Vegetables Corp., 370 F.3d 829, 833-37 (9th Cir. 2004).

[5] Notably, the Ninth Circuit "decline[d] to address the question whether a qui tam relator" — as opposed to the United States itself — "could bring a reverse FCA action involving customs duties in the district courts." Id. at 837 n.14.

[6] See United States v. Universal Fruits & Vegetables Corp., 387 F. Supp. 2d 1251, 1253 (CIT 2005).

[7] United States v. Universal Fruits & Vegetables Corp., 433 F. Supp. 2d 1351 (CIT 2006).

[8] Yates v. Pinellas Hematology & Oncology, P.A., 21 F.4th 1288, 1307 (11th Cir. 2021).

[9] Id. at 1309 (quoting U.S.C. § 3730(b)(1)).

[10] Id. at 1310 (citation omitted).

[11] Vt. Agency of Nat. Res. v. United States ex rel. Stevens, 529 U.S. 765, 773 (2000).

[12] See United States ex rel. Eisenstein v. City of New York, 556 U.S. 928, 934-36 (2009).

[13] United States ex rel. Michaels v. Agape Senior Cmty., Inc., 848 F.3d 330, 340 (4th Cir. 2017) (quoting United States ex rel. Milam v. Univ. of Tex. M.D. Anderson Cancer Ctr., 961 F.2d 46, 48 (4th Cir. 1992)); see United States ex rel. Hunt v. Cochise Consultancy, Inc., 887 F.3d 1081, 1091 (11th Cir. 2018), aff'd, 139 S. Ct. 1507 (2019); United States v. Health Possibilities, P.S.C., 207 F.3d 335, 341 (6th Cir. 2000); United States ex rel. Hall v. Tribal Dev. Corp., 49 F.3d 1208, 1212-13 (7th Cir. 1995); United States ex rel. Killingsworth v. Northrop Corp., 25 F.3d 715, 720 (9th Cir. 1994).

[14] Edmonson v. Leesville Concrete Co., 500 U.S. 614, 626 (1991). Further proof that the United States is a real party in interest abounds. "Even where the government allows the qui tam relator to pursue the action, the case may not be settled or voluntarily dismissed without the government's consent. Moreover, the government may change its mind and intervene at any point in the litigation 'upon a showing of good cause.'" Milam, 961 F.2d at 49 (quoting 31 U.S.C. § 3730(c)(3)). In addition, the government receives most of the benefit from any successful action and has extensive power to take over, or control in other ways, all FCA cases. See id.

[15] See United States ex rel. Felton v. Allflex USA, Inc., 989 F. Supp. 259, 262 (CIT 1997). Similar to Universal Fruits, the Federal Circuit had no occasion to review this decision — this time because the Felton court transferred the case to a district court and transfer orders are not final. United States ex rel. Felton v. Allflex USA Inc., 155 F.3d 570 (Fed. Cir. 1998).

[16] See United States ex rel. Huangyan Import & Export Corp. v. Nature's Farm Prods. Inc., 370 F. Supp. 2d 993, 996-98 (N.D. Cal. 2005) (holding that the district court had jurisdiction over qui tam action commenced by the private plaintiff even though the government intervened in the case); see also United States ex rel. Vallejo v. Investronica Inc., 2 F. Supp. 2d 330, 333 (W.D.N.Y. 1998) ("[T]his Court, and not the [CIT], has jurisdiction over plaintiff's [qui tam action] regarding import duties.").