February 2025

Follow us on LinkedIn

Compliance Update

Federal Contractors With DEI Policies at Increased Risk of False Claims Act Liability

By Avi Weitzman, Kenneth Gage, Ben Snyder, Jane Yoon, Blair Robinson, Ryan Derry, Henry Finkelstein and Mason Busbee

President Donald Trump has signed more than 60 executive orders since taking office, including Executive Order 14173, titled "Ending Illegal Discrimination and Restoring Merit-Based Opportunity" (EO 14173 or the Executive Order). That Executive Order, signed on January 21, 2025, targets what it refers to as government contractors' "illegal" diversity, equity and inclusion (DEI) policies.[1] The Executive Order has already been challenged and, on February 21, 2025, a federal court issued a preliminary injunction blocking enforcement of its key provisions.[2] Nevertheless, until the Executive Order's legal status has been finally resolved, companies that contract with — or receive grants from — the federal government should take account of the new requirements that it establishes, which could expose them to investigations and liability under the False Claims Act (FCA).

Executive Order 14173

EO 14173 directs all federal agencies "to combat illegal private-sector DEI preferences, mandates, policies, programs, and activities," particularly (though not exclusively) at federal contractors and grant recipients. That directive, by itself, was unsurprising in light of statements President Trump had made during the presidential campaign. But the Executive Order also signaled a new mechanism for enforcement of antidiscrimination laws against federal contractors that had not been widely expected. Specifically, the Executive Order requires the head of each agency to include "in every contract or grant award" two provisions with respect to DEI programs. First, it requires a term stating that the contractual counterparty or grant recipient agrees "that its compliance in all respects with all applicable Federal anti-discrimination laws is material to the government's payment decisions for purposes of section 3729(b)(4) of title 31, United States Code" — the section of the U.S. Code that defines materiality for purposes of the FCA. Second, it mandates a term requiring the counterparty or grant recipient "to certify that it does not operate any programs promoting DEI that violate any applicable Federal anti-discrimination laws." Taken together, those two provisions indicate that the Trump administration plans to use the FCA and its treble-damages regime to police federal contractors' operation of DEI programs that arguably violate federal antidiscrimination law.

On February 21, 2025, the U.S. District Court for the District of Maryland entered a preliminary injunction barring enforcement of the certification requirement nationwide.[3] The court determined, among other things, that requiring federal contractors and grant recipients to certify that they do not operate unlawful DEI programs, without any further definition of that term, would unconstitutionally chill First Amendment-protected activity.[4]

The government is likely to appeal that injunction, however, and the long-term status of the Executive Order is presently unclear. If it is ultimately upheld, the Executive Order could significantly change the enforcement of antidiscrimination laws by opening up a new front of litigation under the FCA, which has not historically been used to address allegations of discrimination. In order to assist in-house lawyers responsible for overseeing companies' diversity-related efforts as they account for this potential new development, we provide a high-level explanation of the FCA below and outline certain key considerations that companies should address as they evaluate their existing diversity-related policies.

What is the False Claims Act and how does it work?

The FCA exists to combat fraudulent schemes to obtain payment from the government. Originally enacted in response to contractors who billed the United States for "nonexistent or worthless goods" and "charged exorbitant prices" during the Civil War, the FCA is primarily known for its imposition of civil liability on any individual or company who "knowingly presents" "a false or fraudulent claim for payment or approval" to the government.[5] To be liable under the FCA, an individual or company must have (1) made a false claim for payment, (2) "knowingly" , (3) that was "material" to the government's decision to pay money.[6]

The statute imposes draconian remedies on those found liable, including "3 times the amount of damages which the Government sustains" as well as substantial civil penalties for each false claim submitted.[7] In the fiscal year ending on September 30, 2024, settlements and judgments under the FCA totaled nearly three billion dollars.[8]

Who May Bring a FCA action?

The FCA is unique in that it can be enforced both by the U.S. Department of Justice (DOJ) and by private parties (*i.e.*, whistleblowers) "in the name of the Government."[9] Such a private lawsuit brought in the government's name is called a *qui tam* action.[10] The *qui tam* plaintiff — known as the relator — is often a current or former employee with inside knowledge of a company's practices that allegedly violated the FCA. In the case of DEI programs, it is possible that such insiders will be disgruntled employees or former employees who disapprove of such programs or claim to have been harmed by them.

The FCA requires that the relator file its complaint with the court under seal and serve the complaint on the government along with a written disclosure of all the evidence and information the relator possesses.[11] The complaint remains under seal for a minimum of 60 days to permit the government to decide whether to intervene and proceed with the lawsuit itself. If the government needs more time to make its decision (as is typical), it may seek more time from the court upon a showing of "good cause."[12] During the time that the relator's complaint is under seal, the government conducts its own investigation, which often can take many months or even years. After the government completes its investigation, it must elect to either proceed with the FCA claims itself or decline to do so. If it declines, the relator may proceed with the lawsuit. After the government makes its intervention decision, the complaint is unsealed and served on the defendant.

If the government has intervened in the case, it controls the plaintiff's side of the case going forward. Relators sometimes remain involved in intervened cases, however, and they are entitled to between 15-25% of any eventual recovery. If the government declines to intervene and the relator eventually obtains a recovery on the government's behalf, the relator is entitled to a larger share — between 25-30% of any amount recovered, as well as attorneys' fees and other expenses.[13]

Statutory Bars to FCA *Qui Tam* Actions

The FCA imposes several important limits on *qui tam* actions. Of particular relevance here, the so-called "public disclosure bar" generally requires dismissal "if substantially the same allegations or transactions as alleged in the action or claim were publicly disclosed" in the news media or some other source, such as other government proceedings or reports.[14] This bar does not apply, however, where the relator is the "original source of the information" — meaning that the relator voluntarily disclosed the information to the government prior to its public disclosure or had independent knowledge that materially adds to the publicly disclosed allegations and voluntarily provided that information to the government before filing the *qui tam* action.[15] Thus, the public disclosure bar is most commonly relevant to relators who are outsiders to the defendant-company and have only learned of the company's actions through press reports.

Applying the FCA to EO 14173

If a government contractor maintains a DEI or similar program, whether a DEI compliance certification violates the FCA will turn on the plaintiff's ability to prove the key elements of an FCA claim: falsity, materiality and scienter. We address each of these elements, as well as related questions concerning damages, below.

Falsity/False Certifications

In order to violate the FCA, a claim — that is, a request for payment from the government — must be "false or fraudulent."[16] A claim can be false because of either factual falsity or legal falsity. A factually false claim is one that misrepresents real-world facts, such as by giving an incorrect description of goods delivered or requesting reimbursement for goods or services never provided. A legally false claim is one in which a party represents that it has complied with a contractual condition when, in fact, it has not complied.

In FCA cases brought against federal contractors based on EO 14173's anti-DEI provisions, plaintiffs (either the government or relators) are likely to rely on a theory of legal falsity. As discussed above, EO 14173 provides that future federal contracts must include a certification by the contractor "that it does not operate any DEI programs that violate federal anti-discrimination laws."[17] Where a contractor operates a diversity-related program that is inconsistent with the government's current view of federal antidiscrimination laws, FCA plaintiffs will argue that that certification was expressly false and that all of the claims based on it were therefore false as well.

An initial question in any such case will be whether the contractor's certification was actually false. The Executive Order does not define illegal DEI programs, so it may be unclear whether a particular employer program — such as an affinity group or mentorship program — is even covered by the certification. Moreover, the plaintiff would need to prove that the program in fact violated federal antidiscrimination laws. The Trump administration will likely take the position that those laws prohibit (a) any programs that reflect preferences, quotas, or set asides based on race, gender or other protected characteristics, as well as (b) programs that promote the expansion of opportunities to traditionally disadvantaged groups. Whether such programs actually are unlawful under federal law, however, may be debatable. In practice, therefore, questions about falsity are likely to be heavily litigated.

Materiality

A second central element in most FCA cases is materiality. Only *materially* false claims or statements give rise to liability under the statute.[18] The statute indicates that a claim or statement is "material" if it has "a natural tendency to influence, or be capable of influencing, the payment or receipt of money or property."[19] EO 14173 requires a contracting party to "agree that its compliance in all respects with all applicable Federal anti-discrimination laws is material to the government's payment decisions."[20] This, however, may be insufficient on its own to meet the FCA's materiality prong.

The leading case on materiality is *Universal Health Services, Inc. v. U.S. ex rel. Escobar*, in which the U.S. Supreme Court explained that the FCA "is not an all-purpose antifraud statute" or a "vehicle for punishing garden-variety breaches of contract or regulatory violations."[21] Given that backdrop, the Court held that a representation "cannot be deemed material merely because the Government designates compliance with a particular statutory, regulatory, or contractual requirement as a condition of payment."[22] Nor "is it sufficient for a finding of materiality that the Government would have the option to decline to pay if it knew of the defendants' noncompliance."[23] For example, "[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."[24]

While *Escobar* may indicate that the certification required by EO 14173 will not automatically satisfy the FCA's materiality prong, the materiality clause is likely an effort to clear the way for increased enforcement against companies for non-compliance. Particularly where the DEI program is publicly disclosed, there will be significant litigation surrounding the actual materiality of any DEI program certification to the government's payment decision.

Knowingly — *i.e.*, Scienter

Finally, the government or relator must also show that the false claim was made knowingly, meaning that the person submitting the claim or statement knew that it was false when made. The FCA defines "knowingly" broadly to cover not only circumstances in which a person has "actual knowledge of the information," but also circumstances in which a person "acts in deliberate ignorance of the truth or falsity of the information" or "acts in reckless disregard of the truth or falsity of the information."[25]

In *United States ex rel. Schulte v. SuperValu, Inc.*, the Supreme Court held that the "knowingly" prong is met if, at the time a claim is submitted, the submitting party subjectively:

- Knew the submitted claim was false;
- Was aware of a substantial risk that a claim violated the FCA and intentionally avoided learning whether or not it violated the FCA; or
- Was aware of such a substantial and unjustifiable risk but submitted the claim anyway.[26]

The *SuperValu* decision left many unanswered questions regarding scienter, including how to account for circumstances in which a defendant recognized legal uncertainty as to a particular question and proceeded based on an understanding that it understood to be objectively reasonable but not certainly correct.[27] This latter point is relevant here because companies may well determine that there are multiple reasonable interpretations of how federal antidiscrimination laws apply to their own DEI practices. It is unclear whether choosing the "most aggressive" reasonable, good-faith interpretation, if later determined to be wrong, would subject a company to FCA liability.[28]

Nevertheless, *SuperValu's* subjective scienter requirement makes the certifying party's state of mind at the time of certification relevant to a determination of scienter. Because civil FCA actions may be brought by private parties, a relator with inside knowledge of what a company thought when entering a contract with the government will likely be in a better position to bring an FCA action. Further, the Trump administration could also use FCA actions as a means to engage in costly and invasive discovery into a company's evaluation of its own DEI practices.

Damages

FCA claims also often present difficult questions regarding the calculation of damages. There are multiple FCA damages theories, including the net amount of overpayment (accounting for the value actually received by the government and putting the government in the position it would have been in had the claims not been false)[29] or the entire value of the contract (without any offset for value received by the government).[30]

When faced with FCA suits based on certifications about the absence of any unlawful DEI programs, defendants are likely to argue that the government suffered no actual damages from their false certifications. In such cases, defendants will likely be able to establish that the government received exactly the goods or services it was contracting for and was not harmed on account of the false certification. They may, therefore, be able to argue successfully that no damages should be awarded even if a jury finds that all of the elements of the FCA are met (though they would still be potentially subject to civil penalties for each false statement or claim submitted).

That said, the government and relators are likely to take a much more aggressive tack, contending that the appropriate damages are the entire amount of the contract without any offset for the goods or services received by the government. The U.S. Court of Appeals for the Seventh Circuit adopted a similar theory in *United States v. Rogan*, holding that the government's FCA damages resulting from certain kickback violations consisted of the total amount paid under a contract because, having failed to comply with one of the contract's legal conditions, the defendant was not entitled to receive any payment at all even though it had provided all of the services required.[31] While false DEI certifications are different from kickback violations in important respects, the government invokes *Rogan*'s reasoning frequently and would likely argue here that it is entitled to recover the full amount paid under a given contract because, had it known of a company's illegal DEI program, it would not have awarded that company the contract in the first place or made any payments to the company once the contract was awarded.

Public Disclosure Bar

As noted above, the public disclosure bar will often prevent *qui tam* suits from proceeding if the allegedly illegal program has already been disclosed in the news media or certain other sources. In the DEI context, therefore, news reports of a particular company's diversity-related program may in some circumstances serve to prevent *qui tam* suits alleging that those programs are illegal. Additionally, courts have sometimes determined in other contexts that a company's own disclosure (in SEC filings or publicly available reports) of information that would support a *qui tam* action may trigger the public disclosure bar.[32] Accordingly, companies may be able to preempt *qui tam* actions through well-considered transparency about their diversity-related programs — though such disclosures may also create other legal and reputational risks, including the possibility of FCA suits brought by DOJ (which is not constrained by the public disclosure bar).

Conclusion

Should courts ultimately find the Executive Order's certification requirements to be lawful, an understanding of how companies' own DEI programs interact with it and the FCA will be crucial. The Trump administration has sent a strong message to the business community that it intends to aggressively pursue DEI policies that it considers to be unlawful. Given the potentially significant damages and civil penalties available under the FCA, whistleblowers will have incentives to file qui tam lawsuits alleging that DEI programs resulted in discrimination. Even if companies are ultimately able to show that their programs are lawful (or that they were implemented with a good-faith belief in their legality), the investigations triggered by the filing of such suits are likely to be both costly and distracting. Government contractors should therefore carefully consider proactive steps they can take to protect against potential FCA suits, including seeking confirmation from outside experts of the lawfulness of their current diversity-related efforts, modification of DEI programs that they believe may be legally suspect, and potential strategic disclosures about those programs that could make qui tam suits more difficult without inviting investigations by DOJ or other federal authorities.

✧ ✧ ✧

If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

New York

Kenneth W. Gage
+1-212-318-6046 / +1-312-499-6046
kennethgage@paulhastings.com

Blair Robinson
+1-212-318-6075
blairrobinson@paulhastings.com

Avi Weitzman
+1-212-318-6920
aviweitzman@paulhastings.com

Jane H. Yoon
+1-212-318-6006
janeyoon@paulhastings.com

Henry Finkelstein
+1-212-318-6642
henryfinkelstein@paulhastings.com

Washington, D.C.

Ben Snyder
+1-202-551-1873
bensnyder@paulhastings.com

San Francisco

Ryan Derry
+1-415-856-7092
ryanderry@paulhastings.com

Dallas

Mason Busbee
+1-972-936-7457
masonbusbee@paulhastings.com

---

1 Exec. Order No. 14173, 90 Fed. Reg. 8633 (Jan. 21, 2025), https://www.federalregister.gov/d/2025-02097/page-8633.

2 See Nat'l Assoc. of Diversity Officers in Higher Educ. v. Trump, No. 1:25-CV-00333-ABA, 2025 WL 573764 (D. Md. Feb. 21, 2025).

3 *Id.*

4 *See id.* at *20–22.

5 *Universal Health Servs., Inc. v. United States ex rel. Escobar*, 579 U.S. 176, 182 (2016); 31 U.S.C. § 3729(a)(1)(A).

6 31 U.S.C. § 3729(a)(1); *see, e.g.*, *United States ex rel. Taylor v. Boyko*, 39 F.4th 177, 188 (4th Cir. 2022).

7 31 U.S.C. § 3729(a)(1).

8 U.S. Department of Justice Archives, *False Claims Act Settlements and Judgments Exceed $2.9B in Fiscal Year 2024* (January 15, 2025), https://www.justice.gov/archives/opa/pr/false-claims-act-settlements-and-judgments-exceed-29b-fiscal-year-2024.

9 31 U.S.C. §§ 3730(a), 3730(b)(1).

10 *Qui tam* is a Latin phrase that means "who as well for the king as for himself sues in this matter." Black's Law Dictionary (12th ed. 2024).

11 31 U.S.C. § 3730(b)(2).

12 *Id.* § 3730(b)(3).

13 *Id.* § 3730(d).

14 *Id.* § 3730(e)(4)(A)(iii).

15 *Id.* § 3730(e)(4)(A)–(B).

16 31 U.S.C. § 3729(a)(1)(A).

17 EO 14173 § 3(b)(iv)(B).

18 *See* 31 U.S.C. § 3729(a)(1)(B).

19 *Id.* § 3729(b)(4).

[20] EO 14173 § 3(b)(iv)(A).

[21] 579 U.S. at 193 (citation omitted).

[22] *Id*. at 194.

[23] *Id.*

[24] *Id.* at 195.

[25] 31 U.S.C. § 3729(b)(1)(A).

[26] *United States ex rel. Schulte v. SuperValu, Inc.*, 598 U.S. 739, 757 (2023).

[27] *See* Transcript of Oral Argument at 17–19, 23, *United States ex rel. Schulte v. SuperValu, Inc.*, 598 U.S. 739 (2023) (Nos. 21-1326, 22-111).

[28] *See, e.g.*, *id.* at 41.

[29] *See, e.g., United States v. Sci. Applications Intern. Corp.*, 626 F.3d 1257, 1278–79 (D.C. Cir. 2010).

[30] *See, e.g., United States v. Rogan*, 517 F.3d 449, 453–54 (7th Cir. 2008); *see also United States v. Sikorsky Aircraft Corp.*, 2023 WL 6883637, at *14–15 (E.D. Wis. Oct. 17, 2023).

[31] *Rogan*, 517 F.3d at 453–54.

[32] Federal courts have determined that annual reports may be considered federal reports such that they satisfy the public disclosure bar. *See United States ex rel. Langer v. Zimmer Biomet Holdings, Inc.*, 743 F. Supp. 3d 282, 294 (D. Mass. 2024) ("[T]here is no dispute that Zimmer's Form 10-K annual reports are administrative reports that are one of the statutorily prescribed methods for purposes of the public disclosure bar.").