IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

UNITED STATES OF AMERICA, and THE STATES OF CALIFORNIA, FLORIDA, ILLINOIS, INDIANA, MASSACHUSETTS, MINNESOTA, MONTANA, NEW JERSEY, NEW MEXICO, NEW YORK, AND TENNESSEE, and THE DISTRICT OF COLUMBIA, each ex rel. LYNNTOYA WASHINGTON and MICHAEL T. MAHONEY, **Plaintiffs,** **v.** **EDUCATION MANAGEMENT CORPORATION., et al.,** **Defendants.**	***Jury Trial Demanded*** **Civil Action No. 2:07-cv-00461-TFM** **Hon. Terrence F. McVerry** **Electronically Filed**

DEFENDANTS' BRIEF IN SUPPORT OF THEIR MOTION TO DISMISS AND ALTERNATIVE MOTION TO STRIKE

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INTRODUCTION

The United States (the "Government") has failed to state any claim that could support its complaint against Education Management Corporation and over 100 of its colleges (collectively, "EDMC"). At its core, this case is about a simple regulatory issue: whether EDMC complied with the 2002 Department of Education ("DOE") Safe Harbor regulation that allowed institutions to compensate admissions staff based on student enrollments, so long as enrollments were not the "sole" or "exclusive" consideration. As DOE explained, "the primary purpose of the regulatory safe harbors is to provide **guidance** to institutions so they **may** adopt compensation arrangements that **do not run afoul** of the incentive compensation prohibition [of Title IV of the Higher Education Act, 20 U.S.C. § 1070 *et seq*. ("HEA")]." 67 Fed. Reg. 67054 (emphases added).

As the Government's own exhibits demonstrate, EDMC's compensation plan for its admissions personnel ("Plan") falls squarely within the Safe Harbor and does not violate the HEA as a matter of law. The Plan took into consideration not only enrollment figures, but also standard evaluative factors, such as qualitative factors of job performance, including professionalism, customer service, and business practices and ethics, that DOE has, even in its most recent revisions to the Safe Harbor regulation, recognized as appropriate and permissible. As multiple courts have recognized, such a Plan complies with the Safe Harbor.

Undeterred by this fundamental flaw in its theory of liability, the Government then tries to allege that EDMC ignored the Plan in practice and compensated its admissions representatives based solely on enrollments. But the Government does not and cannot present any facts showing a company-wide sham to defraud the Government. Only a handful of paragraphs in the Government's Joint Complaint in Intervention (the "Complaint") actually pertain to the supposedly wrongful compensation practices that form the basis for the Government's claims.

Of those few, the majority are inconsistent with the Government's own exhibits and allegations. Of the remaining paragraphs, most describe legal conduct, dressed up to impugn EDMC, or reflect mere policy preferences of the current Administration, which recently eliminated DOE's Safe Harbor. Of course, disagreement with the policy and laws of a prior government administration does not justify fraud claims against those who followed the law.

Fatal to its Complaint, the Government does not identify any admissions representative whose compensation was based "solely" on enrollments. In addition, nowhere does the Government allege facts to support the bare contention that any EDMC officer or manager knew that EDMC supposedly failed to comply with the Safe Harbor or the Plan itself. Despite years of investigation, the Government's Complaint relies almost exclusively on the representations of two former EDMC employees, neither of whom ever decided or reviewed recruiter compensation at their lone location, much less at the many other EDMC schools throughout the country that are implicated in this lawsuit.

The Third Circuit recently dismissed similar HEA-based claims under the pleading standard of Fed. R. Civ. P. 8. This Court also recently dismissed for insufficient pleading a securities class action against EDMC alleging that it violated the incentive compensation ban. Under either the standard of Rule 8 or the particularity requirement of Fed. R. Civ. P. 9(b) governing false claims act complaints, the Complaint does not adequately plead claims against EDMC or any of its colleges, much less a massive, nationwide case brought against 111 distinct campuses.

Moreover, the Third Circuit has rejected the fundamental legal theory of the Government's case. As that court held, false claims litigation is an inappropriate means of regulatory enforcement. Particularly where, as in this case, federal agencies have the ability and

discretion to enforce the regulations that they promulgate, litigants may not supplant that agency's authority with *qui tam* lawsuits based on alleged regulatory non-compliance.

The Government ignores its own law, its own conduct, its own exhibits, and the rules of this Court, over-reaching for a mammoth recovery for which it has not a scintilla of factual or legal support. This case should be dismissed with prejudice in its entirety.

BACKGROUND

I. The Educational Market And Government Regulations.

EDMC, headquartered in Pittsburgh and employing 22,000 people nationwide, is one of the largest providers of post-secondary education in North America, and its schools educate well over 100,000 students each year. *See* Compl. ¶¶ 16, 30. In the proprietary education sector, in which EDMC participates, many students come from groups that are traditionally underserved by public and non-profit colleges and universities – working adults and single parents, low-income and minority students, and first-generation college attendees. Nearly 60% of students are women, and about half are minorities. *See* Def. Ex. 1, Dept. of Educ., National Center for Education Statistics at Tables 3.1, 3.2, 3.5-A, 3.5-B, 3.7, 3.11, 5.1, and 5.2 (Sept. 2010).[1]

EDMC operates four different groups of schools, all accredited by a national or regional accrediting agency and certified by DOE as eligible to participate in the federal student aid programs:

[1] The Government attached 53 separate exhibits to the Complaint, which are referenced herein using a "Gov. Ex." citation. Additional material, cited as "Def. Ex.," is appended to this memorandum either as a demonstrative exhibit based on the Government's own filings, or as supplemental factual material that is capable of being judicially noticed. *See, e.g.*, Fed. R. Evid. 201(b)(2). For instance, this Court may take judicial notice of statistics from federal government agencies. *See, e.g.*, *Citizens Fin. Group, Inc. v. Citizens Nat'l Bank*, 383 F.3d 110, 127, n.2 (3d Cir. 2004).

- **The Art Institutes** offer degrees in the creative fields, including design, culinary arts, and fashion, and enroll over 80,000 students in their 48 on-ground campuses and on-line program.
- **Argosy University** offers primarily graduate programs in psychology, education, and behavioral sciences. More than 30,000 students, with an average age of over 35, attend an Argosy school, mainly to pursue credentials as a prerequisite to licensing or career advancement.
- **Brown Mackie Colleges** focus largely on education in the health, legal, and business industries, and help students obtain Associate's degrees or diplomas for high-demand specialties, such as nursing and criminal justice.
- **South University** offers Doctoral, Master's, and undergraduate degrees, primarily in health sciences and business disciplines.

See Def. Ex. 2, 2011 Annual Report, Form 10-K at 5-6 (Aug. 30, 2011).[2] All told, there are more than 100 EDMC campuses across thirty-two States. *Id.* at 5. Three of the groups also offer students the chance to pursue their education online or through a combination of web- and campus-based work, depending on the student's needs and preferences, through an integrated service provider known as the Online Higher Education division ("OHE"). *Id.* at 5, 6, 8.

EDMC schools, like all educational institutions, employ people to recruit students. At EDMC, these employees are called Associate Directors of Admission or Assistant Directors of Admission (collectively, "ADAs"). Also, like other non-profit and for-profit schools, EDMC schools are subject to Title IV of the Higher Education Act, 20 U.S.C. § 1070 *et seq*. ("HEA"), which governs eligibility for federal student-aid programs.

In 1992, out of a concern that commissioned salesmen at some schools were signing up unqualified students, Congress amended Title IV of the HEA to provide that schools whose students receive federal student financial aid must not:

> provide any commission, bonus, or other incentive payment based directly or indirectly on success in securing enrollments or

[2] The Court may also judicially notice information in SEC filings. *See, e.g.*, *Oran v. Stafford*, 226 F.3d 275, 289 (3d Cir. 2000).

> financial aid to any persons or entities engaged in any student recruiting or admission activities.

20 U.S.C. § 1094(a)(20). Known as the "incentive compensation ban," this provision notably did not include "salary" as one of the prohibited types of compensation.

In 2002, DOE promulgated, through notice-and-comment rulemaking, the "Safe Harbor" regulation that sets forth specific compensation arrangements that DOE determined **did not violate** the incentive compensation ban. DOE explained that the Safe Harbor describes "compensation arrangements that **do not run afoul** of the incentive compensation prohibition" of the HEA. 67 Fed. Reg. 67054 (emphasis added). Stated another way, compensation that complied with the Safe Harbor was not an impermissible "incentive payment" under the HEA.

As relevant to this lawsuit, DOE's Safe Harbor authorized:

> The payment of fixed compensation, such as a fixed annual salary or a fixed hourly wage, as long as that compensation is not adjusted up or down more than twice during any twelve month period, and any adjustment is not based **solely** on the number of students recruited, admitted, enrolled, or awarded financial aid.

34 C.F.R. § 668.14(b)(22)(ii)(A) (eff. July 1, 2003 to June 30, 2011) (emphasis added). According to the Secretary of Education, "[i]n this safe harbor, the word 'solely' is being used in its dictionary definition." 67 Fed. Reg. 67055 (Nov. 1, 2002); *see also* WEBSTER'S THIRD NEW INT'L DICTIONARY 2168 (1993) (defining "solely" as "singly," "alone," and "to the exclusion of alternate or competing things"). Thus, the Safe Harbor permitted the consideration of enrollments in adjusting recruiters' salary, provided that the number of students recruited was not the "sole" or "exclusive" factor considered.

After DOE's issuance of the Safe Harbor, EDMC drafted and adopted its Plan, effective July 1, 2003. *See* Gov. Ex. 16. The Plan was then revised in December 2004, but maintained the same basic framework. *See* Gov. Ex. 15.

II. Student Funding Mechanisms.

Like all educational institutions educating students who receive federal student aid, each EDMC-affiliated school certified by DOE signed a Program Participation Agreement ("PPA") with DOE. The PPA "is a prerequisite to the Institution's initial or continued participation in any Title IV, HEA Program." *See* Gov. Exs. 1-3. The PPA sets forth the general terms and conditions of eligibility, under which participating schools agree "to abide by a panoply of statutory, regulatory and contractual requirements." *United States ex rel. Pilecki-Simko v. Chubb Inst.*, No. 10-3907, 2011 WL 3890975, at *1 (3d Cir. Sept. 6, 2011) (not precedential) ("*Chubb II*"). Schools who are found to have violated any of those requirements are subject to a variety of potential sanctions, subject to various due process protections. *See generally* 34 C.F.R. Part 668, Subpart G.

So long as a school has a current PPA, that school may receive Title IV aid for which the student is eligible. Enforcement of the PPA is a matter for DOE. Each PPA for an EDMC-affiliated school grants DOE the authority to investigate regulatory violations and misrepresentations, to provide the school an opportunity to cure any noncompliance, and to decide, at its discretion, the appropriate sanction. *See, e.g.*, Gov. Exs. 1-3. DOE has, at all times, certified EDMC as eligible to award Title IV funds to its eligible students. *See, e.g.*, Gov. Ex. 10.

EDMC also has agreements with California, Florida, Illinois, Indiana, and Minnesota, each of which has also intervened in this case (collectively, the "States"). Those agreements, like their federal counterpart, enable participation in the States' student funding programs. In each State agreement, the educational institution agrees to follow state and/or federal educational laws, including, in some instances, the HEA. *See* Compl. ¶¶ 176, 198, 303, 331; *see also infra*, Part V.

III. The Government Claims.

On April 5, 2007, relator Lynntoya Washington filed a *qui tam* lawsuit against EDMC under the federal False Claims Act, 31 U.S.C. §§ 3729 *et seq*. ("FCA") and nine state FCA statutes, alleging violations of the incentive compensation ban. Joined by a second relator, Michael Mahoney, Ms. Washington filed a Second Amended Complaint dated March 31, 2011, in which she asserted claims on behalf of the United States, eleven states, and the District of Columbia. On April 29, 2011, the Government filed a notice of intervention and subsequently five States – California, Indiana, Illinois, Florida, and Minnesota – also provided notice of their intent to intervene. The United States and four intervening states jointly filed the Complaint on August 8, 2011. It is this pleading that now serves as the operative complaint. *See United States ex rel Alsaker v. Centracare Health Sys.*, No. 99-106, 2002 U.S. Dist. LEXIS 10180, at *6 n. 2 (D. Minn. June 5, 2002).[3]

The Government and States contend, essentially, that EDMC schools falsely certified in their PPAs and elsewhere that the Plan and their compensation practices complied with federal law when, allegedly, EDMC knew that they did not. The Government does *not* assert that the Plan as written violated the FCA.[4] Rather, the Government alleges that the Plan "as applied" violated the FCA because, in practice, EDMC did not follow the Plan and based ADA compensation "solely" on enrollments.[5] Compl. ¶¶ 266-76. Notwithstanding the Government's

[3] Minnesota's subsequent Complaint in Intervention primarily pleads by incorporation the factual allegations underlying the Government's Complaint. *See* Complaint in Intervention by the State of Minn. ¶ 20 (Docket No. 141) (the "Minnesota Complaint").

[4] *See* Complaint ¶ 266 (limiting FCA claim to "compensation plan, *as implemented*" and alleging that "*[i]n practice*, the sole factor that determined changes to the compensation of EDMC's admissions personnel was the number of students recruited . . ."") (emphasis added); *id.* at ¶ 271 (same); *id.* at ¶ 276 (same).

[5] The Government paints its allegations with such broad strokes that it omits fundamental details, such as which Defendant actually signed a PPA, and when, if ever, the Plan applied at

implicit recognition that EDMC's Plan as written is not actionable under the federal FCA, the States claim that the Plan as drafted violates their false claims statutes, although those statutes are interpreted identically to the federal FCA. The Government and States also assert tag-along common-law equity claims that challenge the legality of the Plan both as drafted and as applied.

STANDARD OF PLEADING

Under Rule 8 of the Federal Rules of Civil Procedure, a complaint must be dismissed if it does not contain factual allegations sufficient "to raise a right to relief above the speculative level." *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 545 (2007). Each claimant must plead "enough facts to state a claim to relief that is plausible on its face." *Id*. at 547; *see also Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1950 (2009). In assessing the sufficiency of the pleadings, "[c]ourts are not required to credit bald assertions or legal conclusions improperly alleged in the complaint." *In re Burlington Coat Factories Sec. Litig.*, 114 F.3d 1410, 1429 (3d Cir. 1997); *In re Rockefeller Ctr. Props., Inc. Sec. Litig.*, 311 F.3d 198, 216 (3d Cir. 2002) ("[L]egal conclusions draped in the guise of factual allegations may not benefit from the presumption of truthfulness."). The Third Circuit has thus dismissed FCA claims based on alleged violations of the incentive compensation ban where relators fail to plead little more than "labels and conclusions." *Chubb II*, 2011 WL 3890975, at *4. Similarly, this Court has dismissed allegations that EDMC's Plan violated the incentive compensation ban where plaintiffs failed to allege the factual basis for their claims that Rule 8 requires. *See* Aug. 30, 2011 Report &

(continued…)

each of the more than 100 Defendant schools. EDMC's motion to dismiss attacks the Government's claims as they are pleaded, and should not be construed as an admission that every school signed a PPA or that the Plan applied to all EDMC schools at all times. As the Government knows, but neglected to plead, many of the schools did not implement the Plan until years after it was first developed, some as late as 2010, and some never adopted the Plan at all. *See also infra*, Part II.A.2.

Recommendation at 35, 44-45 (Docket No. 93), *Gaer v. Educ. Mgmt.*, (W.D. Pa. No. 10-1061), *adopted at* Sept. 29, 2011 Order (Docket No. 97).

In addition, Federal Rule of Civil Procedure 9(b) requires that "[a] pleading setting forth fraud as the basis of recovery of damages must, with particularity, allege all the essential elements of actionable fraud." *See Tredenick v. Bone*, 647 F. Supp. 2d 495, 500-01 (W.D. Pa. 2007). This standard applies to both the Government's FCA and common law claims. *See United States ex rel. Pilecki-Simko v. Chubb Inst.*, No. 06-3562, 2010 WL 1076228, at *7 (D.N.J. Mar. 22, 2010) ("*Chubb I*") (dismissing substantially similar HEA compensation claims under Rule 9(b)), *aff'd Chubb II*, 2011 WL 3890975; *see also Va. Sur. Co. v. Macedo*, No. 08-5586, 2009 U.S. Dist. LEXIS 90603, at *31 (D.N.J. Sept. 30, 2009) (ordering dismissal because the plaintiff "failed to plead the underlying fraud, which serves as the basis for its unjust enrichment claim, with particularity, as required by Rule 9(b)").

"Rule 9(b) requires, at a minimum, that plaintiffs support their allegations of … fraud with all of the essential factual background that would accompany 'the first paragraph of any newspaper story' – that is, the 'who, what, when, where and how' of the events at issue." *In re Rockefeller Ctr.*, 311 F.3d at 217 (citations omitted). In addition, Rule 9(b) requires particularized allegations against each named defendant. *See Swartz v. KPMG LLP*, 476 F.3d 756, 764-65 (9th Cir. 2007).

SUMMARY OF ARGUMENT

This case should be dismissed with prejudice for multiple reasons:

First, the Government has failed to allege facts sufficient to state a claim that the Plan – as written or as implemented – violated the HEA's incentive compensation ban. The Government's own allegations and exhibits demonstrate that EDMC's Plan as written complied

with the Safe Harbor. Moreover, the Government's "as applied" claims fail to explain the requisite "who, what, when, where and how" behind the alleged fraud:

- The Government has failed to show how EDMC presented a false claim because it has not alleged facts showing that the number of enrollments were in practice the "sole" basis for compensation.
- The Government relies exclusively on two isolated, low-level employees with virtually no relevant knowledge, and the allegations in the Complaint are contradicted by what little knowledge the relators purport to have, the Government's own exhibits, or both.
- The Government has not alleged any facts from which to infer the required knowledge or recklessness, but relies on an impermissible "collective knowledge" theory based on events at entirely different schools. EDMC's reasonable interpretation of the Safe Harbor also demonstrates that it could not have acted with scienter.
- The Government does not and cannot allege that the purported violations of the incentive compensation ban caused any loss to the Government.
- The Government cannot premise claims of fraud on legal conduct.

Second, the Government has failed to state a viable FCA claim because, under Third Circuit law, the incentive compensation ban is a condition of participation in the federal programs, not a condition of payment. Eligibility to participate in HEA programs is a matter for regulatory enforcement, not FCA claims, and DOE has always deemed EDMC eligible to receive federal funds, as have all the intervening States, and has never instructed EDMC to change its compensation plan, assessed it a monetary liability for an alleged violation of the HEA, or instituted an administrative proceeding to limit or terminate its institutions' participation in the federal student aid programs, whether for alleged violation of the incentive compensation ban or any other regulatory provision. Moreover, because the Government knew of EDMC's Plan for years and did nothing, any fraud claim is barred as a matter of law.

Third, the Government's unprecedented federal common-law claims are barred as a matter of law because DOE's complex regulatory regime and its contractual terms govern the

issue. In addition, equity does not allow for double recovery, and the Government has received the benefit of its bargain.

Fourth, for similar reasons, each State's claims should be dismissed with prejudice. Each State's false claims statute is substantively similar to the federal FCA, and EDMC's compliance with the Safe Harbor precludes liability. Moreover, unique aspects of state law further show why each State has failed to identify a knowingly false certification of a condition of payment. The States' pleadings are also factually deficient, and their equitable claims seek an unfair and improper windfall.

Fifth, Mr. Mahoney's claims should be dismissed because he is the second-filed relator.

ARGUMENT

I. THE PLAN, AS WRITTEN, COMPLIES WITH THE SAFE HARBOR.

The Government's contention in Counts IV-V that the Plan bases compensation for ADAs "solely" on enrollment asks this Court to ignore plain English. On its face, the Plan falls squarely within the terms of the Safe Harbor: it provides for a fixed salary that is adjusted only twice per year and that is not based solely on the number of students enrolled. *See* 34 C.F.R. § 668.14(b)(22)(ii)(A).

A. The Plan Provides A "Fixed" Salary That Does Not Change More Than Twice Annually.

According to the Safe Harbor, the term "fixed compensation" includes "a fixed annual salary" that is not adjusted "up or down more than twice during any twelve month period." 34 C.F.R. § 668.14(b)(22)(ii)(A); *see also* WEBSTER'S THIRD NEW INT'L DICTIONARY 861 (1993) (defining "fixed" as "not subject to change or fluctuation: absolute, settled, definite"). The Plan meets this standard: ADAs received a salary that was not adjusted or changed more than twice a

year. *See* Def. Ex. 3, Admissions Performance Plan, page 21 at "A."[6] Even when an ADA was promoted between semi-annual reviews, the ADA's salary could not change until the next review. *Id*., page 23; Compl. ¶ 94.

The Government's apparent argument that the salary was not fixed because the Plan provides an "incentive" to recruit students disregards its own regulation. Compl. ¶ 153. The Safe Harbor defines arrangements that are **not** an impermissible "incentive payment" under the HEA. *See, e.g.*, 67 Fed. Reg. 67054. Therefore, a plan that complies with the Safe Harbor does not violate the HEA as a matter of law. Indeed, DOE defined "fixed compensation to include up to two pay adjustments during a 12-month period," 67 Fed. Reg. 67054, and has admitted that the Safe Harbor "immunized incentive payments built into semi-annual compensation plans." Def.'s Mot. To Dismiss For Lack Of Jurisdiction, Or In The Alternative, For Summary Judgment, *Career College Ass'n. v. Duncan*, No. 11-038, at 5 (D.D.C. Mar. 18, 2011).[7]

B. The Plan Does Not Base Compensation "Solely" On The Number Of Students Enrolled.

DOE, courts, and the Government all have interpreted "solely" according to its dictionary definition to mean that the number of student enrollments may not be the "exclusive" compensation factor under the Safe Harbor. Indeed, courts have dismissed complaints on Rule 12(b)(6) motions where the relevant plans "bas[ed] compensation not only on enrollment starts" but also other factors such as "student retention, success at recruiting activities, administrative records-keeping, and professionalism." *Chubb I*, 2010 WL 1076228, at *10, *aff'd Chubb II*, 2011 WL 3890975; *see also United States ex rel. Lee v. Corinthian Colleges*, ___ F.3d ___, No.

[6] Defendants' Exhibit 3 includes some annotations for ease of reference, but is otherwise the same document as Exhibit 15 to the Complaint.

[7] The Court can take judicial notice of matters in the public record, such as court filings. *Lum v. Bank of America*, 361 F.3d 217, 221 n.3 (3d Cir. 2004).

10-55037, 2011 WL 3524208, at *6 n.6 (9th Cir. Aug. 12, 2011) (noting that the Safe Harbor applies when the non-recruitment factors "are driven by concrete, merit-based metrics such as those in [*Chubb I*]"); *United States ex rel. Bott v. Silicon Valley Colleges*, 262 F. App'x 810, 812 (9th Cir. 2008) (affirming dismissal because relators did not "ple[ad] specific facts supporting the inference that salary reviews were performed solely on the basis of recruiting success").

DOE has recognized, even after rescinding the Safe Harbor in 2011, that "seniority or length of employment is an appropriate basis for making a compensation decision separate and apart from any consideration of the numbers of students enrolled," and does not violate the HEA. 75 Fed. Reg. 66877. Job knowledge, professionalism, communication skills, interpersonal relations, understanding of technology, and initiative are also among the permissible factors. *See* Def. Ex. 4, Mar. 17, 2011 Letter from Assist. Sec'y, Dep't of Educ. at 13. Further, according to DOE, even today, when the Safe Harbor has been eliminated,[8] "[a] recruiter's knowledge of the institution …, her ability to clearly communicate with prospective students, and prospective students' assessments of her ability to assist them as they consider post-secondary education are all measures of a recruiter's job performance. And their use is permitted under the [2011] regulations." Reply Mem. of Law in Support of Def.'s Mot. to Dismiss at 7, *Career College Ass'n v. Duncan*, No. 11-138 (D.D.C. Apr. 15, 2011).[9]

[8] Although the Government may now disfavor the Safe Harbor regulation – as evident by the fact that it repealed the regulation, effective July 1, 2011 – this cannot change the fact that the regulation during the timeframe covered by this lawsuit unambiguously permitted the consideration of enrollments in setting ADA salaries. The Government cannot retroactively change the Safe Harbor's plain language or DOE's prior interpretation without violating due process. *See Sekula v. FDIC*, 39 F.3d 448, 457 (3d Cir. 1994); *see also Gen. Elec. Co. v. United States*, 53 F.3d 1324, 1334 (D.C. Cir. 1995).

[9] Matters of agency record may also be judicially noticed. *See, e.g., Massachusetts v. Westcott*, 431 U.S. 322, 323 n.2 (1977).

As the Government's exhibits demonstrate, EDMC's Plan based compensation on the very types of factors permitted by the Safe Harbor, DOE, and the courts of this circuit.

1. Starting Salary Is Based On Prior Experience And Education.

Under the Plan, a new ADA's starting salary is based exclusively on prior experience and education. Def. Ex. 3, page 25 at "B." Starting salaries obviously could not be based on enrollments at all, because a brand new employee would not have had any enrollments.

2. First Evaluation: An ADA's First Compensation Adjustment Is Based Only On Quality Factors.

An ADA's first performance review comes six months after hire. At that time, an ADA is eligible for a salary adjustment, which is based exclusively on Quality Points ("Quality Points-Only Method"). *See* Def. Ex. 3, page 26 at "C."

Quality Points are calculated from the ADA's scores in five graded categories, known as Quality Factors, which include Job Knowledge, Business Practices and Ethics, Professionalism, Customer Service, and Initiative. *Id.*, page 15 at "D." On each of these five Quality Factors, ADAs receive a grade of 1 (unsatisfactory) through 5 (outstanding) based on a series of considerations specific to each Quality Factor that are defined in the Plan. *Id.*

Detailed and concrete criteria for assessing an ADA's score in each category are expressly set forth in the Plan. For example, for "Job Knowledge," ADAs are assessed on a variety of job-related activities including how well they use technology, adhere to approved recruitment methods and practices, and know the majors available at the school. *See* Def. Ex. 5, Quality Factor Descriptions.[10] "Professionalism" measures how well ADAs respond to criticism and whether they display a positive attitude in the work environment. *Id.* The "Customer

[10] Defendants' Exhibit 5 reproduces pages LW1222 to LW1226 from Exhibit 13 to the Complaint.

Service" factor incorporates timeliness in managing inquiries and whether the ADA identifies students' needs and expectations, and "Initiative" considers whether the ADA is "[s]elf starting rather than passively complying with instructions or assignments." *Id.* Obviously, these Quality Points involve myriad factors other than the "number of students … enrolled." *Compare Chubb I*, 2010 WL 1076228, at *10, *aff'd Chubb II*, 2011 WL 3890975 (finding compliant with Safe Harbor a compensation plan that considered success at recruiting activities, administrative records-keeping, and professionalism); *Lee*, 2011 WL 3524208 at *6 n.6 (approving *Chubb I*); Def. Ex. 4 at 13 (DOE approving consideration of such factors as seniority, job knowledge, professionalism, analytic ability, initiative, communication skills, understanding of technology, initiative, and interpersonal relations).

3. Second Evaluation: After 12 Months, An ADA's Adjusted Compensation Is Based In Whole Or In Part On Quality Factors.

After a year of employment, an ADA receives another performance evaluation and another salary adjustment. At the Second Evaluation, the adjusted salary will be the greater of (a) the compensation calculated by the Quality Points-Only Method, or (b) the "standard Plan calculation," which incorporates both Quality Points and quantitative metrics in determining salary adjustments. Def. Ex. 3, page 27 at "E"; Compl. ¶ 98.

The "standard Plan calculation" ("Matrix Method") begins with a Matrix within the Plan, which plots the intersection of an ADA's Quality Factor Points and "New Student Points" to determine an annualized base salary for each ADA. *Id.*, page 16 at "F." The Quality Factor Points ("Quality Points") are calculated as described above and are not based "solely" on enrollments. "New Student Points" are based on the number of students enrolled, **and** the type

of program, the type of student, and the geographical zone in which the student is located.[11] *Id.*, page 12-13 at "G." Thus, even New Student Points themselves are not based exclusively on the "number" of students enrolled.

Once the Quality Points and New Student Points are calculated, the Matrix determines the "annualized baseline salary." *Id.* at 16. In the EDMC Plan, the left axis is the New Student Points and the axis across the top is the Quality Points. *Id.* The ADA's salary is determined by the intersection of the ADA's Quality Points and New Student Points on the Matrix. **By virtue of the Matrix structure, it is impossible to calculate an ADA's salary without considering *both* Quality Points and New Student Points**. Both metrics **must** be considered to determine the intersection point that determines the "annualized baseline salary."

For example, an ADA who received 176 New Student Points and 9 Quality Points would receive a $40,000 annualized base salary.

[11] The Complaint erroneously contends that "whether an ADA is 'on the Matrix,' is a function of whether or not the ADA meets the required enrollment numbers in her Student Start Plan." Compl. ¶ 121. The Plan never mentions start plan goals and applies equally to all ADAs covered by the Plan, regardless of their individual goals – as the Complaint elsewhere admits. *Id.* at ¶ 104. In addition, the Government is wrong to allege that New Student Points are credited immediately upon confirmation of enrollment. *See id.* at ¶ 109. An ADA is not credited with a start until after the end of the add/drop period. *See, e.g.*, Def. Ex. 3 at 12.

Level	New Student Point Range	Annualized Salary, Based on Quality Points				
		Unsatisfactory	Needs Improvement	Meets Expectations	Highly Effective	Outstanding
		5-8 points	9-12 points	13-17 points	18-22 points	23-25 points
1	0 - 99	$26,000	$27,000	$29,000	$31,000	$33,000
2	100 - 125	$28,500	$29,500	$32,000	$34,000	$36,000
3	126 - 150	$31,250	$32,500	$35,000	$37,000	$39,000
4	151 - 175	$34,750	$36,000	$39,000	$41,000	$43,500
5	176 - 200	$38,500	$40,000	$43,000	$45,500	$48,000
6	201 - 225	$42,500	$44,000	$47,000	$49,750	$52,000
7	226 - 250	$47,000	$49,000	$52,000	$55,000	$57,500
8	251 - 275	$51,500	$53,500	$57,000	$60,000	$63,000
9	276 - 300	$56,000	$58,000	$62,000	$65,000	$68,000
10	301 - 325	$61,000	$63,500	$68,000	$71,000	$74,000
11	326 - 350	$67,000	$70,000	$74,000	$77,000	$80,500
12	351 - 375	$73,000	$76,000	$80,000	$84,000	$87,500
13	376 - 400	$79,000	$82,000	$87,000	$91,000	$95,000
14	401 - 425	$86,000	$89,000	$94,000	$99,000	$103,000
Add'l levels	25-point increments	Add $7,000	Add $7,000	Add $7,000	Add $8,000	Add $8,000

See Def. Ex. 3, page 16 at "F." If, at the next evaluation, the ADA had 160 New Student Points and 18 Quality Points, that ADA's annualized base salary would be adjusted to $41,000.[12]

Once the Matrix sets the base salary, additional adjustments are used to determine an ADA's final salary. ADAs may receive (1) a 5%-20% cost of living adjustment, depending on their location,[13] (2) an additional compensation adjustment of 3%-15% for those with at least two years of service,[14] and (3) an additional salary adjustment based upon certain oversight or management responsibilities.[15] DOE has blessed these types of adjustments, which are not based on enrollments. *See* 75 Fed. Reg. 66877 ("[S]eniority or length of employment is an appropriate

[12] Notably, ADAs with fewer New Student Points but more Quality Points could receive a higher salary than those with more New Student Points but lower Quality Points. This point is demonstrated by the hypothetical above: Despite a 16 point drop in the ADA's New Student Points, the ADA in this example would receive a salary adjustment which results in $1,000 more per year in base salary based on the increase in the ADA's Quality Points.

[13] *See* Def. Ex. 3, page 18 at "H."

[14] *Id.*, page 19 at "I."

[15] *Id.*, page 28 at "J."

basis for making compensation decisions."); Def. Ex. 4 at 13 (approving of the consideration of such factors as initiative, communication skills, and the use of technology when determining compensation).

4. Third And Subsequent Evaluations: After 18 Months, An ADA's Adjusted Compensation Always Considers Quality Factors And Is Never Based "Solely" On The Number Of Students Enrolled.

Beginning with an ADA's third evaluation, which occurs no earlier than eighteen months after hire, each ADA goes on the Matrix.[16] From then on, all of the ADA's compensation adjustments are determined exclusively under the Matrix Method, which includes consideration of Quality Factors, together with appropriate cost of living, seniority, and management adjustments.[17] Def. Ex. 3, page 27 at "K."

At no point during an ADA's tenure at EDMC is his or her compensation adjustment based solely on student enrollment. Rather at each step of the compensation process, the EDMC Plan requires consideration of multiple factors other than the number of students enrolled – factors that courts and the Government have expressly endorsed. Because the Plan never uses enrollments as the "sole" factor, it complies with the Safe Harbor.

C. The Government Is Ignoring the Plan's Terms.

Notwithstanding the important role played by the Quality Factors in setting ADA compensation, the Government contends that, *if all non-enrollment factors are held constant*,

[16] It is disingenuous for the Government to allege that ADAs "from day one" are pressured to "go on the Matrix," Compl. ¶ 102, when the Plan itself provides that ADAs cannot possibly go on the Matrix until at least 12 months after hire and do not necessarily have their adjusted salary determined by the Matrix until at least 18 months after hire. The Complaint also conspicuously provides no facts as to the tenure of any ADA other than Ms. Washington, a defect that is not only fatal from a pleading standpoint, but also concerning because the Government knows that a significant number of ADAs never advance to a tenure that allows them to go onto the Matrix.

[17] To the extent that any ADA's salary would decrease by beginning the Matrix Method, the Plan limits that decrease. Downward salary protection also depends on Quality Points. Def. Ex. 3, page 21 at "L."

then student enrollments would "solely" determine an ADA's salary under the Plan. Compl. ¶ 154. But the Plan did not hold Quality Factors constant; the Plan provided identifiable metrics to be used to calculate the Quality Points anew at each salary adjustment. *See Chubb I*, 2010 WL 1076228, at *10.

The Government essentially argues that, if an ADA happened to receive a "3" Quality Point rating in two consecutive reviews, then Quality Factors were not considered in the ADA's salary adjustment at all. The fallacy of this argument is clear. By analogy, if a baseball player's salary were determined on the basis of both his number of base hits and his number of home runs, and his home run total happened to stay the same for two consecutive years, that does not mean that home runs were not considered in determining his salary for the second season. Similarly, even when an ADA's Quality Points remain the same between review periods, that does not mean that Quality Factors were not considered in calculating the ADA's adjusted salary.

Indeed, the Government's hypothetical concedes the critical point: the Plan requires consideration of the non-enrollment-based Quality Factors in order to derive the "same" Quality Points rating in the first place. It is wrong to suggest that, just because it is possible that the total number of Quality Points might not change between two reviews, the Quality Points rating does not factor into the calculation.

Finally, the illogic of the Government's position becomes clear by examining the converse of its proposition: if New Student Points remained the same over two review periods while only Quality Points changed, then the Government would have to concede that Quality Points "solely" determined compensation and that New Student Points were irrelevant – a concession that would preclude its claims as to any such ADA. The Government is trying to

have it both ways, but its strained theory is contrary both to the plain language of the Plan and common sense.

The Court should dismiss with prejudice Counts IV and V because the Plan as designed complied with Title IV of the HEA as a matter of law. *See Chubb I*, 2010 WL 1076228, at *10.

II. THE GOVERNMENT HAS FAILED TO STATE A CLAIM THAT THE PLAN "AS IMPLEMENTED" VIOLATED THE FCA.

Notwithstanding the fact that the Plan complied as written with the Safe Harbor, the Government persists in alleging an FCA violation in Counts I-III by claiming that EDMC disregarded the Plan in practice and used it as "window-dressing" or "camouflage" to evade the incentive compensation ban. Compl. ¶ 154. The FCA requires a plaintiff to plead: "(1) the defendant presented or caused to be presented to an agent of the United States a claim for payment; (2) the claim was false or fraudulent; and (3) the defendant knew the claim was false or fraudulent." *Hutchins v. Wilentz*, 253 F.3d 176, 182 (3d Cir. 2001).[18] In addition, a plaintiff must plead "a causal connection … between loss and fraudulent conduct" as another required element of an FCA claim. *United States v. Hibbs*, 568 F.2d 347, 349 (3d Cir. 1977). The Government's claims meet none of these elements.

A. The Government Has Not Alleged And Cannot Allege How EDMC Based Compensation "Solely" On The Number Of Enrollments.

1. The Government Never Pleads How EDMC Presented A False Claim.

In pleading its FCA claims, the Government must allege how EDMC purportedly presented false claims. "'Underlying schemes and other wrongful activities that result in the

[18] The Fraud Enforcement and Recovery Act of 2009 ("FERA") modified the FCA. *See* Pub. L. No. 111-21, § 4, 123 Stat. 1616 (2009). The Government purports to bring Count I under the pre-FERA Section 3729(a)(1), Count II under post-FERA Section 3729(a)(1)(A), and Count III under post-FERA Section 3729(a)(1)(B). *See* Compl. ¶¶ 265-83.

submission of fraudulent claims … must be pled with particularity pursuant to Rule 9(b),'" and "'such pleadings invariably are inadequate unless they are linked to allegations, stated with particularity, of the actual false claims submitted to the government….'" *United States ex rel. Schmidt v. Zimmer, Inc.*, No. 00-1044, 2005 U.S. Dist. LEXIS 15648, at *12 (E.D. Pa. July 29, 2005) (quoting *United States ex rel. Karvelas v. Melrose-Wakefield Hosp.*, 360 F.3d 220, 232 (1st Cir. 2004)).

The Government fails to plead facts showing that ADA compensation was "solely" based on enrollment under the Plan "as implemented." The Government admits that ADA compensation was set "[u]sing the Matrix," Compl. ¶ 153, and its own exhibits demonstrate that EDMC disseminated guidelines for proper use of the Plan to managers, instructed them to "ensure that compensation is administered effectively, equitably, and within the scope of the plan," and trained its ADAs in the Plan. Def. Ex. 3 at 3; *see also* Compl. ¶¶ 92, 99, 100.

The Government also never alleges any specific facts to show how Quality Points were purportedly a sham or proxy for the number of students enrolled. And, once more, its own exhibits belie any such claim. The actual salary calculations provided by the Government – those of relator Ms. Washington – reflect consistent application of the Quality Factors. *See, e.g.,* Def. Ex. 6, L. Washington Performance Review, pages LW1670-71 at "A" – "E."[19] *See also Chubb I*, 2010 WL 1076228, at *10 (ordering dismissal where "the examples provided with the [complaint] demonstrate that [defendant's] compensation scale complied with the regulatory safeharbor").

The Government attempts to obfuscate the importance of the Quality Factors by pointing to scattered references to enrollments that appear in Ms. Washington's narrative reviews. Compl.

[19] Defendants' Exhibit 6 is a reproduction of Exhibit 22 to the Complaint, with select annotations.

¶ 135. But this ignores the numerous Quality Factors that also applied. Ms. Washington earned Quality Points because she, among other things, "use[d] technology effectively," "applie[d] organizational policy and procedure correctly," "accurately and completely portray[ed] the school's educational programs," "maintain[ed] composure under stress," and "accept[ed] responsibility and deal[t] constructively with her own mistakes." Def. Ex. 6, page LW1670 at "A" – "C."[20] The Government has failed to allege how any of these other, non-enrollment-based considerations were a mere "smokescreen," and thus cannot claim that Ms. Washington's compensation was based "solely" on enrollments.

The Complaint is thus bereft of the factual allegations necessary under Rule 8 – and especially under the particularity standard of Rule 9(b) – regarding how the alleged fraud supposedly happened. The Government's utter failure to plead any facts as to how the alleged fraud occurred is dispositive and requires dismissal. *Karvelas*, 360 F.3d at 232; *see also United States ex rel. Lemmon v. Envirocare of Utah*, No. 02-904, 2008 U.S. Dist. LEXIS 29619, at *72 (D. Utah Apr. 9, 2008).

2. The Government's Factual Allegations Are Constrained By Relators' Limited Knowledge.

The *only* facts that the Government does allege in support of its claims involve two relators, Mr. Mahoney and Ms. Washington, who worked at OHE in Pittsburgh for a limited period of time (in the aggregate, about three years). Compl. ¶¶ 20, 21. The allegations of these two relators, with their limited knowledge of the relevant details, do not meet Rule 8 or Rule 9(b) standards: the rules require plaintiffs to plead facts, not inferences, conclusions, or logical leaps. *United States ex rel. Pilecki-Simko v. Chubb Inst.*, No. 06-3562, 2010 WL 3463307, at *6 (D.N.J.

[20] The same analysis is true for all of Ms. Washington's other salary adjustments. *See, e.g.*, Def. Ex. 6, pages LW1655-56, LW1659-61, LW1664-67.

Aug. 27, 2010) (dismissing under Rule 9(b) because the "series of inferences [was] too tenuous" (marks and citation omitted)), *aff'd Chubb II*, 2011 WL 3890975 (holding that relators' claims also failed to meet the requirements of Rule 8); *see also United States ex rel. Feingold v. Palmetto Gov. Benefits Admin.*, 477 F. Supp. 2d 1187, 1195-96 (S.D. Fla. 2007) (ordering dismissal where relator alleged only his belief that a fraud was occurring).

Here, Ms. Washington worked in an entry level job in one division of EDMC. *See* Compl. ¶ 20.[21] Meanwhile, relator Michael Mahoney was hired as Director of Training and his job was to teach salesmanship, not to implement any compensation practices, not to train anyone on compensation practices, and not to make any compensation decisions. Compl. ¶ 130. In fact, the Complaint contains:

- *No* allegations that Mr. Mahoney or Ms. Washington had responsibility for evaluating ADAs or making compensation decisions for ADAs;
- *No* allegations that either of them had access to, let alone was able to analyze, the actual compensation awarded to ADAs, or the factors actually used to determine their compensation;
- *No* allegations that either of them worked at or with any of the 105 individual U.S. on-ground schools named as separate Defendants in the Complaint;
- *No* allegations that either of them submitted, saw, reviewed or witnessed claims or certifications to the government to obtain payment of funds;
- *No* allegations regarding any conduct before June 1, 2004 or after June 22, 2007; and
- *No* allegations of communications with those who submitted the PPAs or other alleged certifications.

[21] *See* Compl. ¶ 90 ("ADAs, including Ms. Washington, are responsible for recruiting applicants for admission to EDMC schools, including securing and managing new student inquiries, achieving enrollment and start rate goals, and participating in recruitment and enrollment activities."). It is the ADA's manager who "conduct[s] performance evaluations, obtain[s] required approvals for the salary changes determined by the plan, communicat[es] with [ADAs] about … compensation, and answer[s] … questions about the plan." Gov. Ex. 13, LW1211.

Absent competent, particularized allegations on these critical points, the Government cannot meet the requirements of Rule 8, let alone Rule 9(b). *Feingold*, 477 F. Supp. 2d at 1195-96.

In addition to lacking any supporting facts, the relators' allegations do not have sufficient indicia of reliability to support the assertion that EDMC submitted false claims any time at its Pittsburgh schools, let alone everywhere, every time since 2003. *United States ex rel. Atkins v. McInteer*, 470 F.3d 1350, 1358-59 (11th Cir. 2006) (FCA claim dismissed where the defendant had multiple facilities, but the relator (i) had never worked in facilities that were the subject of his allegations; and (ii) based his claims in part on "rumors from staff" at a single facility); *United States ex rel. Corsello v. Lincare*, 428 F.3d 1008, 1013-1014 (11th Cir. 2005) (allegations based on "information and belief" lacked reliability because the relator "did not have access to company files outside his own offices"); *United States ex rel. Westfall v. Axiom Worldwide, Inc.*, No. 06-571, 2009 WL 1424213, at **4-5 (M.D. Fla. May 20, 2009) (dismissing claims where relators did not work at physicians' offices where false claims were allegedly made).

For this reason, Judge Nora Barry Fischer of this Court dismissed with prejudice substantially similar claims under the Securities Act of 1933 and Securities Exchange Act of 1934, which alleged that EDMC based ADA compensation "solely" on the number of student enrollments. *See* Aug. 30, 2011 Report & Recommendation at 44-45 (Docket No. 93), *Gaer v. Educ. Mgmt.*, (W.D. Pa. No. 10-1061), *adopted at* Sept. 29, 2011 Order (Docket No. 97). That case relied on a confidential witness who claimed "that 'in reality … enrollment volume (measured by "a new student point range") was the sole consideration used to determine compensation levels' for ADAs." *Id.* at 44. But, the court held, the witness was only an admissions representative "at South University's Online Division for less than two years and d[id] not allege how he or she knew how all of EDMC's ADAs were compensated." *Id.* at 44-45.

This inherent lack of personal knowledge was fatal to claims that – like the FCA – required pleading reliable facts. As in *Gaer*, entry-level admissions personnel in this case have no basis for knowing company-wide practices and cannot support the Government's FCA claims. *Id.*; *see also McInteer*, 470 F.3d at 1358-59.

Moreover, the Government improperly conflates all of the individual schools and asserts its legal claims against all "Defendants." Under Rule 9(b), a plaintiff cannot "'merely lump multiple defendants together.'" *Lee*, 2011 WL 3524208, at *9 (citation omitted) (holding that FCA claims failed because the complaint did not "set forth each individual's alleged participation in the fraudulent scheme"). Rather, Rule 9(b) "'requires plaintiffs to differentiate their allegations when suing more than one defendant and inform each defendant separately of the allegations surrounding his alleged participation in the fraud.'" *Id.*; *see also Vicom v. Harbridge Merchant Servs., Inc.*, 20 F.3d 771, 778 (7th Cir. 1994) ("[I]n a case involving multiple defendants, … the complaint should inform each defendant of the nature of his alleged participation in the fraud." (citations omitted)); *In re Balko*, 348 B.R. 684, 694 (Bankr. W.D. Pa. 2006) ("Lumping multiple defendants in a group (*e.g.*, 'defendants misled the plaintiff by stating….') defeats [the] notice objective [underlying Rule 9(b)] and is therefore improper." (emphasis added)); Aug. 30, 2011 Report & Recommendation at 46 (Docket No. 93), *Gaer v. Educ. Mgmt.*, (W.D. Pa. No. 10-1061) (holding that allegations pertaining to all of EDMC's schools did not satisfy federal pleading standards because the allegations were based on employees from "only a few schools"), *adopted at* Sept. 29, 2011 Order (Docket No. 97).

The Government's Complaint fails to satisfy these requirements here. First, the Government's Complaint lacks any allegation of how and when the compensation Plan was implemented – if at all – at each school. *See, e.g.*, Compl. ¶ 6 ("EDMC" defined to include all

"Defendants"); *id.* at ¶¶ 11, 88, 89, 105, 266, 271, 276.[22] Moreover, the Complaint does not identify a single document or a single EDMC officer at any school directing that ADA compensation decisions should ignore the Plan and use only enrollment numbers, let alone a company-wide practice directed by EDMC's management.

Second, the Government asserts claims against at least 15 schools that did not exist or were not part of EDMC during the 2003 to 2009 time period alleged in the Complaint or during the three years in which the relators were employed. *See* Def. Ex. 2 at 15-21. For example, The Illinois Institute of Art – Tinley Park is named as an individual Defendant, but it did not open until 2011. *Id.* at 18. The Government's complete failure to distinguish between each of over 100 defendant institutions with any degree of particularity falls short of the requirements for pleading an FCA claim.

3. The Government's Allegations Are Contradicted By The Complaint.

The Government also cannot rely on factual allegations that are contradicted by its own exhibits. *See, e.g.*, *Del. Nation v. Pennsylvania*, 446 F.3d 410, 417 (3d Cir. 2006) (holding that a complaint failed to state a claim where critical facts were "contradict[ed by] the very allegations of the Complaint"); *Barberan v. Nationpoint*, 706 F. Supp. 2d 408, 413 (S.D.N.Y. 2010) ("[T]he Court need not feel constrained to accept as truth conflicting pleadings that make no sense, or that would render a claim incoherent, or that are contradicted either by statements in the complaint itself or by documents upon which its pleadings rely." (citations omitted)); *see also ALA, Inc. v. CCAIR, Inc.*, 29 F.3d 855, 859 n.8 (3d Cir. 1994); *Jones v. ABN AMRO Mort. Group, Inc.*, 551 F. Supp. 2d 400, 409 (E.D. Pa. 2008).

[22] *See supra*, note 5.

Here, the relators' allegations regarding EDMC's Plan are contradicted by the Government's exhibits or other allegations within the Complaint. For example, the apparent core of Mr. Mahoney's allegations is that Quality Factors were a "smokescreen" because "during the eight months that Mr. Mahoney was employed at EDMC, he never heard anyone focus on, or even discuss, the 'quality factors.'" Compl. ¶¶ 134, 136. But, this attempt to substitute "ignorance" for "knowledge" is antithetical to federal pleading requirements, and the misleading suggestion that Quality Factors were never discussed or considered is contradicted by the Government's exhibits and the other allegations within the Complaint.[23] For example:

- Ms. Washington, who was an ADA and whose compensation was determined through the Plan, recites conversations that *she* had about Quality Points (conversations that evidently were not heard by Mr. Mahoney). Compl. ¶¶ 92-93, 97-99.

- The Worksheets used to calculate adjusted ADA salaries – that employees signed – reflect the communication that Quality Points impact salary adjustments. *See, e.g.*, Def. Ex. 6.

- The narrative reviews of ADAs, which were shared with the ADAs, reflect detailed consideration of Quality Points. *Id.*

- The Plan documents provided to every employee described the Quality Points. Compl. ¶ 92; Gov. Ex. 13.

- The training developed and provided to ADAs (apparently by people other than Mr. Mahoney) discusses Quality Points. Compl. ¶ 99; Gov. Ex. 14.

The Government cannot state a claim by misleading and contradicted allegations.[24] *See Del. Nation*, 446 F.3d at 417.

[23] The assertion that Mr. Mahoney "never heard" of any "quality factors" simply underscores the fact that he was not in a position to have any relevant knowledge whatsoever. *See* Compl. ¶¶ 134, 136.

[24] As additional examples, in Paragraph 88 of the Complaint, the first sentence refers to Ms. Washington and states merely that compensation was "based upon the number of new students who enroll in EDMC institutions" – but not that compensation was "solely" or "exclusively" based on the number of enrollments. It is only the second sentence, which does not refer

B. The Government Has Not Pled And Cannot Meet The Essential Element Of Scienter.

To state a claim under the FCA, the Government also must allege with particularity that EDMC knew that the Plan (either as designed or as implemented) violated the HEA, but falsely certified compliance in connection with a claim for payment. *See, e.g., Chubb II*, 2011 WL 3890975, at *3. The FCA requires that the defendant have "actual knowledge of the information" that is allegedly false, "act[] in deliberate ignorance of the truth or falsity of the information," or "act[] in reckless disregard of the truth or falsity of the information." *Id.* (quoting 31 U.S.C. § 3729(b)(1)).

This pleading requirement is especially important for FCA claims because of the potential for draconian treble damages and civil penalties and the potential for "abuse by the government and qui tam relators" of the implied false certification theory. *United States v. Sci. Applications Int'l Corp.*, 626 F.3d 1257, 1270 (D.C. Cir. 2010). As the D.C. Circuit has held, "this very real concern can be effectively addressed through *strict enforcement*" of the scienter element. *Id.* (emphasis added). As a general matter, a "defendant corporation is deemed to have the requisite scienter for fraud only if the individual corporate officer making the statement has

(continued…)

specifically to Ms. Washington, that uses the word "exclusive." The Government appears to have been careful to avoid actually pleading that *Ms. Washington*'s own salary was ever based "solely" or "exclusively" on enrollments. Such an allegation would be untrue, as demonstrated by the Government's own exhibits, which show on their face that enrollments were not the "sole" factor in Ms. Washington's compensation.

This artful pleading is cause for concern, not comfort. The intent of the overall paragraph is to suggest that all ADAs, including Ms. Washington, were compensated "exclusively" on the basis of enrollments. The careful use of the term "oral review" in Paragraph 135 presents a similar issue. The Government was well aware that Ms. Washington's "written" reviews and Worksheets were replete with Quality Points. To carefully plead that Quality Points were not mentioned in her "oral review" to support a claim that they were not at all considered in her review is misleading at best.

the requisite level of scienter." *Zavolta v. Lord, Abbett & Co.*, No. 08-4546, 2010 U.S. Dist. LEXIS 16491, at *20-21 (D.N.J. Feb. 24, 2010) (securities litigation requiring intent under Rule 9(b)) (citations omitted). Under the FCA, courts, therefore, prohibit allegations of scienter based only on the "collective knowledge" of individuals within the corporation. *Sci. Applications*, 626 F.3d at 1273-74.

In addition, in a case substantially similar to the one here, the Third Circuit read Rule 9(b) to "require plaintiffs to 'allege facts that show the court their basis for inferring that the defendants acted with scienter.'" *Chubb I*, 2010 WL 1076228, at *7 (citations omitted). But under any pleading standard, the Complaint fails to state a claim. In *United States ex rel. Pilecki-Simko v. Chubb Inst.*, the court dismissed claims that defendant's compensation plan violated the HEA because the relators failed to "allege circumstantial facts enabling the inference that [defendant] acted with scienter by falsely certifying compliance with Title IV's incentive compensation ban." *Chubb I*, 2010 WL 1076228, at *10. In affirming, the Third Circuit found the claims impermissibly deficient even under the "more lenient standards of Rule 8." *Chubb II*, 2011 WL 3890975, at *3. The relators' failure to "state facts supporting a reasonable inference that [defendant] knew, acted in reckless disregard, or deliberately ignored that its submissions were false" precluded their *qui tam* claims. *Id.* at *5.

Notably, in finding that the plaintiffs' scienter allegations were insufficient to satisfy this standard, the Third Circuit distinguished other FCA cases based on the incentive compensation ban, in which the allegations described with specificity the school's "'established infrastructure to deceive the government,'" how the defendant "'repeatedly changed its policies to hide its fraud,'" and made "'intentional, palpable lie[s]'" to the government "'with knowledge of the falsity and with intent to deceive.'" *Id.* at *5 n.18 (quoting *Hendow*, 461 F.3d at 1175). Indeed,

the allegations in *Hendow* included secret files that were hidden from government inspectors, managers "openly brag[ging]" about the fraud they perpetrated on DOE, and intentionally altering pay scales to obscure illegality. *Hendow*, 461 F.3d at 1170. In contrast, compliance with the Safe Harbor precludes the required allegations of scienter. *Chubb I*, 2010 WL 1076228, at *10 (ordering dismissal because "an institution adhering to a federal regulation defining the contours of permissible compensation under the incentive compensation ban cannot have the requisite scienter to violate the ban"); *see also Bott*, 262 F. App'x at 812 ("If defendants complied with a facially valid regulation, relators cannot show the required scienter under the False Claims Act for actions after the safe harbor regulation was promulgated.").

The Complaint here is rife with the type of conclusory allegations about EDMC's knowledge that the Third Circuit has held are insufficient to state an FCA claim. *See id.* at *4.[25] The Government alleges no *facts* similar to those that the Third Circuit found to be critical in *Hendow* and to be conspicuously absent in *Chubb II*. In fact, the Government's allegations and exhibits show that EDMC made extensive efforts to comply with the Plan. Directors of Admission, who "serve[] as the primary recruiting and marketing manager[s]" at EDMC, were instructed on the details of the Plan, the meaning of Quality Factors, and their importance to compensation. Compl. ¶ 104; Def. Ex. 3. All ADAs, new hires, and even prospective employees were given similar information. Compl. ¶¶ 92, 99. Even under the "more lenient" pleading standard of Rule 8 – but particularly under the governing standard of Rule 9(b) – the

[25] *Compare, e.g.,* Compl. ¶ 161 ("EDMC knew that its Matrix-based compensation system and the sales culture it was implementing did not satisfy the Incentive Compensation Ban and Regulatory Safe Harbor.") *with Chubb II*, 2011 WL 3890975, at *5 (allegation that "'Chubb knows that this claim ... is false because Chubb knows its students are not eligible under the Title IV program due to Chubb's violations of the HEA incentive compensation ban" held to be impermissibly conclusory).

Government's inability to allege the required factual support is fatal to its FCA claims. *See Chubb II*, 2011 WL 3890975, at *5.

FCA plaintiffs, furthermore, may not "prove scienter by piecing together scraps of innocent knowledge held by various corporate officials, even if those officials never had contact with each other or knew what others were doing in connection with a claim seeking government funds." *Sci. Applications Int'l*, 626 F.3d at 1275. The Government offers nothing to suggest that EDMC sanctioned or ratified any purported violation of the incentive compensation ban. "The mere failure of a system to catch an error does not establish recklessness." *United States ex rel. Hefner v. Hackensack Univ. Med. Ctr.*, 495 F.3d 103, 110 (3d Cir. 2007).

For instance, the Complaint contains:

- No facts regarding EDMC's knowledge at the time that EDMC drafted and rolled out the Plan.
- No facts about the knowledge of the 111 named Defendants.
- No facts linking any person alleged to have signed the relevant PPAs to the compensation Plan or practices.
- No facts regarding whether those employees knew or believed that EDMC's Plan or practice was compliant, nor whether they reported a violation to EDMC's management.
- No facts that these employees evaluated ADAs under the Plan or made compensation decisions.

Courts require more than tenuous circumstance, and the stark deficiencies in the Government's allegations are dispositive. *Lee*, 2011 WL 3524208, at *8 (affirming dismissal where the complaint did not "clearly allege sufficient facts to support an inference or render plausible that Corinthian acted while knowing that its Compensation Program fell outside of the Safe Harbor Provision on which it was entitled to rely"); *Chubb I*, 2010 WL 1076228, at *10 (ordering dismissal because the complaint "fails to allege circumstantial facts enabling the

inference that TCI acted with scienter by falsely certifying compliance with Title IV's incentive compensation ban.").

1. Allegations Based On An Enforcement Action Brought Against A Different School Fail To Establish EDMC's Scienter.

The only *facts* alleged to support scienter appear in six paragraphs relating to the settlement of an FCA claim involving a different compensation plan at a different school altogether, the University of Phoenix.[26] *See* Compl. ¶¶ 159-64. These allegations fail to meet the Government's burden of pleading because they rest entirely on baseless speculation.

The Government's own exhibits demonstrate that this settlement agreement did not require the University of Phoenix to eliminate or change its compensation plan in any way, and the University of Phoenix did not admit any wrongdoing. *See* Gov. Ex. 44 at 1. Accordingly, there is no "strong inference" from the University of Phoenix's settlement agreement that anyone at the University of Phoenix believed its compensation plan was improper, let alone that anyone at EDMC believed that its own compensation plan was improper by analogy. *See Pichler v. UNITE*, 646 F. Supp. 2d 759, 766 (E.D. Pa. 2009) (holding that a settlement agreement with no admission of liability cannot give rise to inference that party acted with scienter). Any inference would be particularly tenuous given that EDMC's Plan on its face complies with the Safe Harbor.[27]

In addition, the former Phoenix employees joined EDMC in 2007. Compl. ¶ 163. By 2007, the *Government itself* knew of EDMC's Plan because at least two *qui tam* cases (including

[26] Even a cursory review of the two plans reveals substantial differences, and the Government has alleged no facts to the contrary. Moreover, DOE's review of the University of Phoenix's compensation plan began in 1998, years prior to promulgation of the Safe Harbor. *See* Gov. Ex. 44 at 1. The Court thus cannot infer that the activity at the University of Phoenix that was under review even related to compliance with the Safe Harbor.

[27] *See also infra*, Part II.B.2.

this one) were filed raising the same compensation ban issues. *See also United States ex rel. Buchanan v. Educ. Mgmt. Corp.*, Case No. 2:07-cv-00971-TFM (W.D. Pa.). It is ironic that the Government would suggest that Todd Nelson, Chief Executive Officer of Education Management Corporation, should have changed EDMC's Plan when, during that same time, the Government itself took no action on it.[28]

The Government's knowledge of EDMC's Plan also undermines the Government's case. One aspect of scienter under the FCA is to engage in the conduct "'while keeping the [Government] in the dark.'" *United States ex rel. Lopez v. Strayer Educ., Inc.*, 698 F. Supp. 2d 633, 637 (E.D. Va. 2010) (citation omitted). *See also United States ex rel. Burlbaw v. Orenduff*, 548 F.3d 931, 951-52 (10th Cir. 2008). Thus, when the Government learns of alleged misconduct yet continues a business arrangement, it is impossible for the other party to act with the required fraudulent intent. *Burlbaw*, 548 F.3d at 951-52. The Government could not have been in the dark when it knew of EDMC's Plan. Therefore, the Government's actual knowledge and acquiescence to EDMC's compensation practices precludes any possibility of scienter.[29] *Burlbaw*, 548 F.3d at 951-52; *United States ex rel. Costner v. United States*, 317 F.3d 883, 887-88 (8th Cir. 2003); *see also United States v. Southland Mgmt. Corp.*, 326 F.3d 669, 681-82 (5th Cir. 2003) (Jones, J., concurring).

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[28] As noted, the University of Phoenix did not admit to any wrongdoing. The discussion herein relates solely to the allegations made in that case without conceding their substantive merit.

[29] The Government's acquiescence to the Plan also prevents it from establishing materiality. For all claims, and particularly those paid after June 7, 2008, the Government must show that compliance with the incentive compensation ban was material to its decision to pay. *See* 31 U.S.C. § 3729(a)(1)(B) (2009). As a matter of law, the Government's history of paying Title IV monies despite its knowledge of the Plan prevents it from meeting that requirement. *Costner*, 317 F.3d at 887 (holding that the Government could not prove FCA liability where it continued paying defendant despite knowledge of the misconduct).

2. EDMC's Compensation Practices Were Based On A Reasonable Interpretation Of The Safe Harbor Regulation.

"Under the False Claim Act's scienter requirement, 'innocent mistakes, mere negligent misrepresentations and differences in interpretations' will not suffice to create liability." *Lee*, 2011 WL 3524208, at *8 (citation omitted). Because EDMC's interpretation and application of the compensation regulations were reasonably based on the plain English of the Safe Harbor regulation, conformed with the federal government's own views, and had never been questioned previously while DOE was engaged in vigorous enforcement efforts, the Government cannot plausibly claim now that EDMC somehow acted with the requisite scienter to violate the incentive compensation ban.[30] *See id.*; *see also Safeco Ins. Co. of Am. v. Burr*, 551 U.S. 47, 70 n.20 (2007) ("Where, as here, the statutory text and relevant court and agency guidance allow for more than one reasonable interpretation, it would defy history and current thinking to treat a defendant who merely adopts one such interpretation as a knowing or reckless violator. Congress could not have intended such a result."); *United States v. Sodexho, Inc.*, No. 03-6003, 2009 U.S. LEXIS 51469, at *53-54 (E.D. Pa. Mar. 6, 2009), *aff'd United States ex rel. Pritsker v. Sodexho, Inc.*, 2010 U.S. App. LEXIS 2645 (3d Cir. Feb. 9, 2010) (defendants not liable under FCA where they operated under a reasonable interpretation of regulations).

[30] In fact, the University of Phoenix enforcement matter and other similar enforcement actions actually negate scienter in this case. As exemplified by the University of Phoenix Program Review, the Department conducted extensive investigations and instituted enforcement proceedings against schools it suspected were in violation of the incentive compensation provisions. Between 1998 and 2009, DOE "substantiated incentive compensation violations at 32 schools." Def. Ex. 7, U.S. Gov't Accountability Office, *Higher Education, Higher Education: Information on Incentive Compensation Violations Substantiated by the U.S. Department of Education*, GAO-10-370R, at 2 (Feb. 23, 2010). In addition to these investigations, the Department of Education has "entered into settlement agreements with 22 other schools." *Id.* at 2-3. But no EDMC school was subject to any of these enforcement efforts, despite the fact that the Government has known about EDMC's Plan at least since 2007. *See id.* at 10 (listing the schools at which violations were substantiated by the Department of Education).

C. Plaintiffs Have Failed To Allege That EDMC's Allegedly Improper Compensation Practices Caused Any Injury To Them.

The Government's Complaint fails to allege how EDMC's purportedly unlawful compensation practices caused any economic harm to the Government. In the Third Circuit, "a causal connection must be shown between loss and fraudulent conduct and … a broad 'but for' test is not in compliance with the statute." *United States v. Hibbs*, 568 F.2d 347, 349 (3d Cir. 1977); *see also Wilkins*, 2011 WL 2573380, at *6 ("The primary purpose of the FCA is to indemnify the government – through its restitutionary penalty provisions – against losses caused by a defendant's fraud.") (citation omitted). It is not sufficient under the FCA to show that a defendant made false certifications; a plaintiff must also demonstrate that the falsity caused a loss that the Government would not have otherwise incurred. *Id*. at 351 (holding that there was no causation where the Government's alleged payments were not "caused by or related to the false certifications").

To satisfy the requirements of *Hibbs* and Rule 9(b), the Government must plead with particularity a "causal connection" showing that it would not have paid EDMC anything had it known about the alleged regulatory violations. But, the Government cannot make that necessary allegation because it has continued to pay EDMC for at least four years ***after*** knowing of the alleged violation. Compl. ¶¶ 76-80.

The Government does not come close to meeting its burden to allege causation of loss:

- *No* allegations identify ADAs who recruited otherwise unqualified students due to their improper compensation under the Plan.
- *No* allegations identify unqualified students, who would not have otherwise been enrolled at EDMC schools, who received financial aid under Title IV.
- *No* allegations identify the unqualified students who would not have attended another school through which the Government would have loaned or granted similar funds.

- *No* allegations show unqualified students who defaulted on student loans issued or guaranteed by the Government and also received no benefit from the education he or she obtained.

This failure is telling because the incentive compensation ban "is meant to curb the risk that recruiters will sign up poorly qualified students who will derive little benefit from the subsidy and may be unable or unwilling to repay federally guaranteed loans." *Lee*, 2011 WL 3524208, at *1 (citation omitted). Yet, the Complaint fails to allege in any tangible way that any harm occurred. This showing is critical because DOE has even admitted that "a violation of the incentive compensation prohibition [does] not result[] in monetary loss to the Department," and "[i]mproper recruiting does not render a recruited student ineligible to receive student aid funds for attendance at the institution on whose behalf the recruiting is conducted." Def. Ex. 8, Oct. 30, 2002 Memorandum of Deputy Sec'y at 1.

Particularly where the Government would have suffered "precisely the same loss … had the certifications been accurate," courts require a more tailored theory of causation. *Hibbs*, 568 F.2d at 351. The Government's inability to meet this burden alone warrants dismissal. *See United States ex rel. Sikkenga v. Regence Bluecross Blueshield*, 472 F.3d 702, 728 (10th Cir. 2006) (citing *Hibbs* and affirming dismissal of FCA claims where "[t]he chain of causation … is attenuated, and lacks sufficient factual allegations to be anything more than conjecture").

D. The Court Should Strike The Irrelevant Allegations From The Complaint Under Federal Rule Of Civil Procedure 12(f).

The Government attempts to obscure the defects in its Complaint with hyperbole in criticizing EDMC's perfectly legal conduct. These improper allegations should be stricken "to clean up the pleadings, streamline litigation, and avoid unnecessary forays into immaterial matters…." *NN&R, Inc. v. One Beacon Ins. Group*, 362 F. Supp. 2d 514, 525 (D.N.J. 2005); *see also River Road Devel. Corp. v. Carlson Corp.*, No. 89-7037, 1990 U.S. Dist. LEXIS 6201, at *7

(E.D. Pa. May 23, 1990) (striking allegations that "confuse the issues in the case"). "The function of a 12(f) motion to strike is to avoid expenditure of time and money that necessarily arises from litigating spurious issues by disposing of those issues prior to trial." *Del. Health Care, Inc. v. MCD Holding Co.*, 893 F. Supp. 1279, 1291-92 (D. Del. 1995).

A significant portion of the Government's Complaint discusses "selling" and "tracking enrollments," purportedly because "enrollment as the sole basis upon which [EDMC] determines an ADA's compensation is demonstrated by the *emphasis* EDMC places on *training its ADAs to 'sell' enrollments"* and by "the way [EDMC] tracks ADAs' success in obtaining student enrollments." Compl. ¶¶ 105, 120 (emphasis added). Aside from the fact that setting performance targets, tracking results, and even "emphasizing" them says nothing about whether they were the "sole" factor in setting ADA compensation, there is *nothing* illegal about training recruiters to recruit or tracking their success. As DOE admits, "by the very job description, a recruiter's job is to recruit," and the Safe Harbor allowed consideration of enrollments in determining compensation. Federal Student Aid Programs, 67 Fed. Reg. 67048, 67056 (Nov. 1, 2002); *see also* Compl. ¶ 42.

Not surprisingly, multiple courts – including in the Third Circuit – have held that teaching, tracking, and emphasizing recruiting is not actionable. *See Chubb I*, 2010 WL 1076228, at *10 (holding that a plan that bases performance evaluation not only on enrollment starts, but student retention, success at recruiting activities, administrative record-keeping and professionalism is within Safe Harbor); *Lee*, 2011 WL 3524208, at *6 n.6 (holding that "'Good' or 'Excellent' ratings driven by concrete merit-based metrics such as those" in *Chubb* could fall within the Safe Harbor); Aug. 30, 2011 Report & Recommendation at 45 (Docket No. 93), *Gaer v. Educ. Mgmt.* (W.D. Pa. No. 10-1061), *adopted at* Sept. 29, 2011 Order (Docket No. 97)

("[A]ggressively seeking students, monitoring financial performance, computing enrollment numbers or various alleged acts regarding recruiting, financial reporting and placement practices are not in fact fraudulent or misleading.").[31]

The Complaint's repeated references to termination of recruiters who failed to meet target enrollment numbers also focuses impermissibly on entirely lawful conduct.[32] *See Bott*, 262 F. App'x at 812 (the decision to fire an employee is not covered by the incentive compensation ban); *Lee*, 2011 WL 3524208, at *4 (holding that allegations that employees were disciplined, demoted or terminated on the basis of their recruitment numbers "does not … state a violation of the HEA incentive compensation ban, and also does not support the claim that a false statement was made"); *United States ex rel. Torres v. Kaplan Higher Educ. Corp.*, No. 09-21733, 2011 U.S. Dist. LEXIS 94003, at *12 (S.D. Fla. Aug. 23, 2011) ("Nothing in the language of the incentive compensation ban would appear to cover personnel decisions, such as whether to fire an employee."). Yet in paragraph after paragraph, the Government attacks EDMC for doing just that. Compl. ¶¶ 137, 148-49. Throughout these sections, *there is not one factual, non-conclusory allegation that EDMC based any ADA's actual salary exclusively or "solely" on new student enrollments*.

These improper allegations express nothing more than the Government's current distaste for the Safe Harbor and the consideration of enrollments that it authorized. Whether or not DOE should have created the Safe Harbor that authorized consideration of enrollments in making salary adjustments "is a policy debate that belongs in the halls of Congress, not in the hearing

[31] Additionally, these factors cannot provide the basis of an FCA claim because there was nothing "fraudulent" about them; EDMC disclosed in its SEC Form S-1 that it aggressively recruited students. *See* Def. Ex. 9, Oct. 1, 2009 Education Management Corporation's Registration Statement (Amendment No. 7 to Form S-1, Registration Statement Under The Securities Act of 1933) (filed Sept. 30, 2009) at 2, 3, 24, 48 and 78.

[32] *See* Compl. ¶¶ 137, 148-49.

room of this Court." *Powerex Corp. v. Reliant Energy Servs.*, 551 U.S. 224, 237 (2007). The Constitution "forecloses the conversion of courts of the United States into judicial … debating forums." *Valley Forge Christian College v. Am. United for Separation of Church & State*, 454 U.S. 464, 473 (1982).

The Government's Complaint also makes irrelevant factual allegations regarding EDMC President's Club and minor prizes. *See* Compl. ¶¶ 140-47. These allegations have nothing to do with how EDMC paid its ADAs under the Plan – the only purported basis for the Government's FCA claims. *See* Compl. ¶¶ 265-77 (Counts I-III). Nor is there any allegation that the gift cards and other incidental gifts allegedly distributed in specific offices were a sanctioned program throughout EDMC. As in *Chubb II*, there is no allegation to connect these gifts to any claim for payment, and the Government's meager factual allegations are insufficient to demonstrate the required scienter. *See Chubb II*, 2011 WL 3890975, at *4-5 (holding that allegations about "gifts based on their enrollment numbers … do not state a plausible claim to relief that TCI knew that its claims were false or fraudulent").

Moreover, the allegations concerning the "President's Club" are particularly inapposite because, in 1995, educational institutions sought guidance from DOE as to whether the incentive compensation ban allowed them to host "annual business meetings at desirable out-of-town location[s]," if eligibility to attend the trips is based "upon the degree to which each individual has succeeded in his or her recruitment efforts during the preceding year" and "each attendee's reasonable travel and other expenses will be either paid or reimbursed." Def. Ex. 10, Jan. 25, 1995 Letter to Dept. of Educ. Deputy Director. *Compare* Compl. ¶ 141 (alleging that "EDMC rewards the top 10% of EDMC admissions personnel, based on number of new student enrollments achieved during a given year, with an all-expenses paid 'President's Club' trip to a

desirable location"). In response, DOE advised that "paying for the travel and related expenses incurred for attendance at such business meetings would not be in violation of" the incentive compensation provision of the HEA. Def. Ex. 11, Feb. 6, 1995 Letter from Dept. of Educ. Deputy Director (emphases added).[33]

The voluminous recitation of legal conduct, dressed up to sound somehow "fraudulent," merely obscures the real issues in this case: whether or not EDMC knowingly violated the Safe Harbor and whether any violation of the Safe Harbor supports an FCA claim. The answer to both questions is no. The Safe Harbor permitted recruiter salaries that were not based "solely" on enrollment and not adjusted more than twice annually. The Safe Harbor also permitted recruiting and exhorting recruiters to recruit well. The Government might now prefer otherwise, but what the regulation "indisputably does prevails over what it ought to have done." *Powerex Corp.*, 551 U.S. at 237. Accordingly, the Court should strike these irrelevant and extraneous allegations that have no bearing on the legal claims at issue. *See* Def. Ex. 13.

[33] As the Department of Justice's own files will also reflect, in connection with an earlier examination of EDMC's compensation practices in 2000 and 2001, EDMC wrote to the Government regarding President's Club, described the program, and provided a wealth of related material, and expressed its opinion that the program was proper pursuant to the representations in DOE's 1995 letter. *See* Def. Ex. 12, Aug. 3, 2001 Letter from T. Hylden to J. Yavelberg. (Undersigned counsel's July 7, 2011 Freedom of Information Act request for this information, including the Government's copy of Defendants' Exhibit 12, remains pending as of the date of this filing, and the Government's response will be judicially noticeable. *See Krzesniak v. Cendant Corp.*, No. 05-5156, 2007 U.S. Dist. LEXIS 18811, at *6-8 (N.D. Cal. Feb. 27, 2007) (taking judicial notice of documents received pursuant to FOIA requests).) The Government never refuted EDMC's position on this issue or took regulatory action over President's Club, and following EDMC's explanation, the Government dropped its review without requesting any change in compensation practices. For the Government now to suggest that President's Club was an illegal, fraudulent program is pure hypocrisy, and its about-face dispels any notion that EDMC acted with the requisite scienter. *See Burlbaw*, 548 F.3d at 955 (finding there could be no "knowing" violation of the FCA in light of defendant's "reliance on government assurances").

III. THE GOVERNMENT CANNOT STATE AN FCA CLAIM AS A MATTER OF LAW.

A. Compliance With The Incentive Compensation Ban Is Not A Condition Of Payment Of Federal Money To EDMC.

All of the Government's FCA claims should also be dismissed because they attempt to convert what is at most a disputed technical violation of a regulation into a multi-billion-dollar, intentional fraud claim. As the courts have universally recognized, the FCA is not a "'blunt instrument to enforce compliance with *all* … regulations.'" *United States ex rel. Rodriguez v. Our Lady of Lourdes Med. Ctr.*, 552 F.3d 297, 304 (3d Cir. 2009) (emphasis added)); *see also Wilkins*, 2011 WL 2573380, at *12. "'Tripping up on a regulatory complexity does not entail a knowingly false representation.'" *Chubb I*, 2010 WL 1076228 at *6 (citation omitted). "[T]o plead a claim upon which relief could be granted under a false certification theory" in the Third Circuit, "a plaintiff must show that compliance with the regulation which the defendant allegedly violated was a condition of payment from the Government." *Wilkins*, 2011 WL 2573380, at *11 (citing *Rodriguez v. Our Lady of Lourdes Med. Ctr.*, 552 F.3d 297, 304 (3d Cir. 2008)).

Earlier this year, in *Wilkins*, the Third Circuit distinguished between a "condition of payment," which may serve as a basis for an FCA claim, and a "condition of participation," which is grounds for eligibility in a government program but not grounds for an FCA claim.[34] As the Third Circuit explained, although violations of particular regulations may lead to termination of the provider's contract with the Government, the regulations which do "not require perfect compliance as an absolute condition" to receiving payment cannot serve as a basis for an FCA claim. *Id*. at *12 (quotation marks and citation omitted). Instead, "the

[34] *Wilkins* involved a healthcare provider that certified its compliance with certain marketing regulations when it contracted with the government for Medicare reimbursements. *See* 2011 WL 2573380, at *1. Plaintiffs alleged that the provider had knowingly violated those regulations and knowingly provided false certifications of compliance that gave rise to FCA liability. *Id.* The district court dismissed that claim under Fed. R. Civ. P. 12(b)(6), and the Third Circuit affirmed.

Government has established an administrative mechanism for managing and correcting [these regulatory] violations which includes remedies for violations other than the withholding of payment otherwise due." *Id.* (emphasis added).

According to the Third Circuit, allowing false certification claims based on noncompliance with regulatory conditions of participation would give rise to an impermissibly "broad theory of FCA liability" and would replace agency discretion and administrative procedures with federal litigation for even the most insignificant and unwitting regulatory transgression. *Id.* at *12. The court observed that

> [f]ederal agencies are unquestionably better suited than federal courts to ensure compliance with [such] regulations. In the circumstances, we believe that by permitting *qui tam* plaintiffs to file suit based on the violation of regulations which may be corrected through an administrative process and which are not related directly to the Government's payment of a claim, courts unwisely would shift the burden of enforcing the … regulations to themselves even though the administration of the vast and complicated [administrative] program is best left to the administrators.

Id. at *12.[35]

The Third Circuit, thus, held that the FCA cannot be used to "short-circuit the very remedial process the Government has established to address non-compliance with those regulations." *Id.* Nor can the Government compel perfect compliance at the threat of FCA liability. "'It would … be curious to read the FCA, a statute intended to protect the government's fiscal interests, to undermine the government's own regulatory procedures.'" *Id.* (quoting *United States ex rel. Conner v. Salina Reg'l Health Ctr., Inc.*, 543 F.3d 1211, 1221 (10th Cir. 2008)).

[35] Lax construction also would provide a perverse incentive to employees: rather than report violations internally to supervisors or hotlines, they will race to court in the hope of enormous personal gain.

Accordingly, the Third Circuit held that a violation of the regulations at issue – although defendants specifically agreed to comply with them – could not support an FCA claim because those provisions were a condition of the provider's *participation* in Medicare, but not a condition of *payment* for the provider's reimbursement claims. *Id.* at *10-12. They may support agency regulatory action but not an FCA claim. *Id.*

Likewise, here, the prohibition on incentive compensation in the HEA is one of many conditions of participation in Title IV programs, but not a condition of payment by the Government. In a PPA, the institution agrees to abide by hundreds of federal regulations or statutes, including the incentive compensation ban. Many of these requirements are administrative in nature.[36]

The PPA, however, does "not require perfect compliance [with the incentive compensation ban] as an absolute condition" to receiving payment. *Wilkins*, 2011 WL 2573380, at *12. The regulations do not automatically make the institution ineligible to receive federal funds or require the return of previously received funds upon a regulatory violation. Rather, DOE regulations give the agency broad discretion in how to address possible violations. The agency has discretion to impose a variety of different sanctions, including no sanction at all. *See* 34 C.F.R. §§ 668.84, 668.85, 668.86, 668.95.

DOE, in practice, has exercised its discretion to continue to allow institutions to receive federal funds even when programs do not strictly comply with the PPA, including the incentive compensation provision. DOE has not limited, suspended or terminated HEA funding at any of

[36] For example, institutions must agree to "[e]stablish an on-going drug-free awareness program"; "establish[] a campus security policy"; and notify DOE within ten days after being notified that an employee was convicted of a drug-related crime in the workplace. *Id.* Institutions must also agree to comply with laws, such as Title IX and the Rehabilitation Act, which have countless detailed and technical regulations implementing them.

the educational institutions at which it has substantiated violations of the incentive compensation ban from 1998 to 2009. *See* Def. Ex. 7, U.S. Gov't Accountability Office, *Higher Education: Information on Incentive Compensation Violations Substantiated by the U.S. Department of Education*, GAO-10-370R, at 4-6 (Feb. 23, 2010). Indeed, as the Government alleges, DOE conducted an extensive investigation into the compensation practices at the University of Phoenix, resulting in a Program Review that uncovered the alleged wrongdoing and led to a settlement agreement. *See* Compl. ¶¶ 159-61; *see also* Gov. Exs. 43-44. Yet the Government fails to note that, after that settlement, DOE took no other action and continued making HEA payments to the University of Phoenix and its students. *See* Gov. Ex. 44 at 2.

The Government has had actual knowledge of EDMC's Plan since at least 2007, when Ms. Washington filed this case, but it has not conducted any Program Review of EDMC similar to its investigation of the University of Phoenix. And at no time has DOE refused to pay EDMC or limited its ability prospectively to receive Title IV funding. *See* Def. Ex. 7 at 4-6; *see also* Gov. Ex. 10 (listing current PPAs between DOE and EDMC-affiliated schools). By its own conduct within the industry at large and as relates to EDMC in particular, the Government has demonstrated that regulatory compliance is not a prerequisite to payment.

For the Government now – after four years of uninterrupted payments to EDMC and failure to cut funding at 32 other schools at which the Government has substantiated violations – to suggest that compliance with the incentive compensation ban was a *condition* of those payments is not plausible. Imposing such a condition now after payments were made would be unlawfully retroactive, lacking fair notice to EDMC. As the University of Phoenix Program Review demonstrates, DOE's administrative process can effectively investigate and redress alleged Title IV violations. The Government cannot now use FCA litigation to end-run that

process and past policies.[37] *See Heckler v. Chaney*, 470 U.S. 821 (1985) (holding that the FDA's decision not to institute enforcement proceedings is not judicially reviewable); *Buckman Co. v. Plaintiffs' Legal Comm.*, 531 U.S. 341, 347-48 (2001) (holding that "[t]he relationship between a federal agency and the entity it regulates" is beyond the purview of civil tort litigation). The Government's attempt to seek billions of dollars under the FCA rather than complying with its own rules and regulations is unprecedented and impermissible.

B. The Government Cannot Retroactively Apply 2009 Amendments To The FCA.

In addition, Count III of the Complaint independently fails to the extent that the Government is retroactively applying recent amendments to the FCA. Count III states a claim under Section 3729(a)(1)(B), applying the post-FERA version of the FCA to all claims for payment made "[f]rom July 1, 2003 to the present." Compl. ¶ 276. However, the FERA amendments only took effect "as if enacted on June 7, 2008." Pub. L. No. 111-021 § 4(f)(1), 123 Stat. at 1621. "[A]pplication of FERA's amendments to claims for money or property that were submitted to and paid by the government before the effective date of the amendments … raises serious ex post facto concerns." *United States ex rel. Putnam v. E. Idaho Reg'l Med. Ctr.*, 696 F. Supp. 2d 1190, 1196 (D. Idaho 2010). As such, EDMC's constitutional rights prevent such retroactive application of the law, and the Government is precluded from seeking relief under Count III on the basis of any money it paid prior to June 7, 2008. *Id.*; *see also Hopper v. Solvay*

[37] The question of whether or not the incentive compensation ban is a condition of payment has previously split the judiciary. *Compare United States ex rel. Graves v. ITT Educ. Servs., Inc.*, 284 F. Supp. 2d 487 (S.D. Tex. 2003) (holding that the incentive compensation ban was a condition of participation, not a condition of payment) and *United States, ex rel. Gay v. Lincoln Tech. Inst.*, No. 01-505, 2003 U.S. Dist. LEXIS 25968 (N.D. Tex. Sept. 3, 2003) (same) *with Hendow*, 461 F.3d 1166 *and United States ex rel. Main v. Oakland City Univ.*, 426 F.3d 914 (7th Cir. 2005). Each of these cases was decided before *Wilkins*, however, and none followed the analytical framework that the Third Circuit adopted. Of these cases, the only one that even considered DOE's extensive administrative scheme in the manner that *Wilkins* instructs held that the ban was a condition of participation, not payment. *See Graves*, 284 F. Supp. 2d at 502.

Pharm., Inc., 588 F.3d 1318, 1323 n.2, 1327 n.3 (11th Cir. 2009); *United States ex rel. Sanders v. Allison Engine Co., Inc.*, 667 F. Supp. 2d 747, 752 (S.D. Ohio 2009).

IV. THE GOVERNMENT'S EQUITABLE CLAIMS ARE LEGALLY FLAWED.

Implicitly acknowledging the weakness of its FCA claims, the Government attempts to repackage its challenge to the design of the Plan under the ironic rubric of "equity," alleging theories of unjust enrichment and payment by mistake of fact.[38] Compl. ¶¶ 278, 284. The Government's equitable claims arise from the same allegedly fraudulent conduct as its FCA claims, and its claims are equally deficient under Rules 8 and 9(b). *See Va. Sur. Co*., 2009 U.S. Dist. LEXIS 90603, at *31. The Government's common law claims are barred, as a matter of law, for additional, unique reasons as well.

First, Congress has delegated the authority to seek retroactive repayment for statutory, regulatory, or contractual violations of Title IV to the Secretary of Education. *See* 20 U.S.C. § 1094(c)(1)(F) (vesting authority in Secretary of Education); 34 C.F.R. Part 668, Subpart G (setting forth detailed punitive and remedial scheme). Therefore, the Government's common law claims are precluded because codified federal law already provides a vehicle by which to secure the same relief. *See Buckman*, 531 U.S. at 348-53 (precluding state law tort claims where Congress vested enforcement authority in FDA and where FDA had enacted a "detailed regulatory regime"); *Am. Elec. Power Co., Inc. v. Connecticut*, ___ U.S. ___ ,131 S. Ct. 2527, 2538 (2011) ("[T]he delegation [by Congress] is what displaces federal common law."); *Jordan*

[38] As this Court is aware from the issuance of its order dated April 12, 2011, EDMC drafted and implemented the Plan with the assistance of independent, outside lawyers and consultants. The Government's failure to plead these facts and its blatant attempt to end-run the FCA, for which advice of counsel is a complete defense (*see United States v. Martorano*, 767 F.2d 63, 66 (3d Cir. 1985), is disingenuous.

v. Fed. Express Corp., 116 F.3d 1005, 1018 (3d Cir. 1997) (dismissing common law claims that encroached on the "extensive regulatory network" Congress had established).

Second, because the Government's common-law equity claims arise from an alleged breach of contract (violation of the PPAs), they are strictly prohibited. *See, e.g.*, Compl. ¶¶ 168, 173-76, 197-201, 330-31. In each PPA, the EDMC institution and DOE agreed that participation in Title IV, HEA Programs was "subject to the terms and conditions set forth in [the] Agreement," including the incentive compensation ban. *See, e.g.*, Gov. Ex. 1. The PPAs grant DOE enforcement authority and authority to seek damages for non-compliance with contract provisions. *Id.*; *see also* 34 C.F.R. Part 668, Subpart G. The existence of this contractual relationship precludes the Government's equitable claims. *See Wayne Moving & Storage of N.J., Inc. v. School Dist. of Phila.*, 625 F.3d 148, 153 n.1 (3d Cir. 2010); *Van Orman v. American Ins. Co.*, 680 F.2d 301, 312 (3d Cir. 1982); *Crews v. Central States, Se. & Sw. Areas Pension Fund*, 788 F.2d 332, 337 n.3 (6th Cir. 1986) (unjust enrichment claim limited by terms of the contract between the parties and federal statute).

Third, the Government has received the benefit of its bargain – the education of students. Allowing the Government to recover under its equitable claims would be an impermissible double recovery. *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 297 (2002) ("[I]t 'goes without saying that the courts can and should preclude double recovery by an individual.'") (quotation omitted); *see also United States v. Occidental Chem. Corp.*, 200 F.3d 143, 149 (3d Cir. 1999) (noting "the prohibition against double recovery found in the common law").

The Government has known about the Plan for years, yet has continued to allow students to borrow money to pay EDMC to attend its schools. During this time of the Government's inaction, EDMC schools have accepted federal funds to educate tens of thousands of students.

Because the students, the Government, and EDMC cannot be restored to their original positions, the Government may not recover at common law. *Coplay Aggregates, Inc. v. Bayshore Soil Mgmt. LLC*, No. 11-1059, 2011 U.S. Dist. LEXIS 54830, at *19 (E.D. Pa. May 23, 2011).

V. THE COURT SHOULD ALSO DISMISS THE STATES' CLAIMS.

The deficiencies in the Government's claims are equally fatal to the States' claims brought under their own false claims statutes ("State FCA"). The State FCA statutes are interpreted consistently with the federal FCA in all material respects.[39] For the same reasons that their federal counterparts fail, as well as independent reasons unique to each State, the mirror-image State FCA claims cannot survive scrutiny under Rule 12(b)(6).

A. Defendants' Compliance With The Safe Harbor Regulation Compels Dismissing the State FCA Claims With Prejudice.

Each State FCA claim fails at least in part because it depends on the alleged violation of federal HEA regulations and the federal incentive compensation ban. *See* Compl. ¶¶ 176-77 (California); *id.* at ¶ 263 (Indiana); *id.* at ¶¶ 303, 309 (Florida); *id.* at ¶ 331, 409 (Illinois); *see also* Minn. Compl. ¶ 32. However, unlike the Government, the States do not distinguish

[39] **Illinois**: *See* Ill. False Claims Act, 740 ILCS 175/1 *et seq*. (effective July 27, 2010) and its predecessor the Ill. Whistleblower Reward and Protection Act, 740 ILCS 175/1 *et seq.* (1992); *United States ex rel. Batty v. Amerigroup Illinois, Inc.*, 528 F. Supp. 2d 861, 871 n.8 (N.D. Ill. 2007) ("[C]ase law interpreting the [Federal] FCA is also applicable to [Illinois's FCA equivalent]."). **California**: *See* Cal. False Claims Act, Cal. Gov't Code § 12650 *et seq.*; *State v. Altus Finance, S.A.*, 36 Cal.4th 1284, 1299 (Cal. 2005) ("[T]he CFCA 'is patterned on similar federal legislation' and it is appropriate to look to precedent construing the equivalent federal act." (citation omitted)). **Indiana**: *See* Ind. False Claims and Whistleblower Protection Act, Ind. Code. § 5-11-5.5-2(b)(1), (2), and (8); *Adolph v. Indiana Gaminb Com'n*, No. 09-1396, 2010 WL 3447554, at *2 (S.D. Ind. Aug. 30, 2010) (relying on federal case law "[b]ecause Indiana's false claims act mirrors its federal counterpart in all material respects."). **Florida**: *See* Fla. False Claims Act, § 68.028(2)(a); *United States ex rel. Heater v. Holy Cross Hosp.*, Inc., 510 F. Supp. 2d 1027, 1034 n.5 (S.D. Fla. 2007) (applying the same standard in its evaluation of the federal and Florida FCA claims (citation omitted)). Minnesota's false claims statute just became effective last year, and its courts have not yet ruled on its consistency with the federal FCA. *See* Minn. Stat. § 15C.02(a) (2010). However, the relevant provisions of the Minnesota FCA track the federal Act and should be interpreted consistently.

between the Plan as designed and the Plan as implemented. *See, e.g.*, Compl. ¶¶ 387, 433; Minn. Compl. ¶ 31. For all the reasons discussed above, the Court should dismiss with prejudice Counts VI, VII, IX, X, XI, and XIV of the Complaint, and Count I of Minnesota's Complaint.

B. The States Have Not Alleged Claims For Relief Because They Have Not Cited A False Certification Of A Condition Of Payment.

No State FCA claims can survive because the federal incentive compensation ban is not a condition of payment for state financial aid funding. *See supra*, Part III.A; *Wilkins*, 2011 WL 2573380 at *9-12. In addition, unique aspects of each State's laws and regulations render the State FCA claims deficient under any standard for false claims liability. In effect, the States would have this Court turn false claims act claims into exactly the kind of impermissible "blunt instrument" for enforcing regulatory compliance that the Third Circuit forbids. *See Wilkins*, 2011 WL 2573380, at *9.

For instance, the Illinois PPA includes only a general certification that "[t]he Institution agrees to comply with all provisions of applicable laws and regulations, … including, but not limited to: the Higher Education Act of 1965…." Gov. Ex. 51 at 1, Ill. PPA. The California PPA is similarly general. *See* Compl. ¶ 174 (quoting the California PPA as requiring that the institution "agree[s] to be subject to and comply with 'all current and applicable federal and state law and regulations….'"). And in Indiana, Florida, and Minnesota, the PPAs and related state laws neither refer to the federal incentive compensation ban, nor require broad compliance with all generally applicable federal laws and regulations.[40]

[40] The State laws, regulations, and PPAs – none of which refers to the incentive compensation ban – also preclude the States from arguing that compliance with that particular federal regulation was material to their decisions to pay. The State FCA claims fail for that reason alone. *See* 31 U.S.C. § 3729(a)(1)(B) (2009); *Costner*, 317 F.3d at 887.

False claims liability cannot arise from what are, at best, general catch-all provisions. *See, e.g., Conner*, 543 F.3d at 1218-19 (holding that false claims act claims should be dismissed where a certification of legal compliance with underlying laws and regulations "contain[ed] only general sweeping language" and did not specify any particular law or regulation as a condition of payment). Moreover, permitting the States' claims would necessarily and impermissibly supplant carefully tailored regulatory regimes and agency expertise, in favor of a broad strict liability regime to enforce every technical regulatory non-compliance. *Wilkins*, 2011 WL 2573380, at *9; *United States ex rel. Mikes v. Straus*, 274 F.3d 687, 699 (2d Cir. 2001). This deficiency is particularly pronounced with respect to the state FCA claims because the state financial aid agreements, laws, and regulations make no reference whatsoever to the incentive compensation ban.

Permitting FCA liability based on each State's generalized admonitions to comply with federal DOE regulations would be improper for other specific reasons:[41]

- Indiana, Illinois, and Minnesota premise their State FCA claims on the allegation that EDMC falsely certified the existence of a valid federal PPA with DOE as a condition of receiving state funds. *See* Compl. ¶ 201 (Indiana); *id*. at ¶¶ 327, 409 (Illinois); Minn Compl. ¶ 23. But the Government concedes that EDMC had and still has valid PPAs from DOE. *See* Compl. ¶ 65; Gov. Ex. 10. There could be nothing false about these claims. *United States ex rel. Vigil v. Nelnet, Inc.*, No. 10-1784, 2011 WL 1675418, *3 (8th Cir. May 5, 2011).

- Notwithstanding Minnesota's allegations to the contrary, eligibility under its financial aid programs does not strictly require participation in the federal Pell Grant Program. *Compare* Minn. Compl. ¶ 32 *with* Minn. Stat. § 136A.103(b)(3)(ii) (2011). Compliance with the incentive compensation ban thus could not be a condition of payment under Minnesota law. Moreover, Minnesota

[41] Among the dozens of similar *qui tam* cases that have been brought against other educational institutions asserting violations of the incentive compensation ban, research has not uncovered any where separate recovery was permitted under a State FCA statute. This likely reflects a consensus that States may not rely on the HEA and the federal PPA to substantiate their claims, but must be able to put forward state-specific provisions that constitute a false certification and a condition of payment – something the States here are unable to do.

did not enact its false claims act until 2010, and it is precluded from recovering thereunder based on claims that were made prior to that date.[42]

- California cannot plausibly claim that compliance with the incentive compensation ban was a condition of payment because *it allowed schools to pay incentive compensation*, including via "commission, commission draw, bonus, [or] quota." *See* Cal. Educ. Code § 94832(e) (2001). While California allowed that law to become inoperative on July 1, 2007, no substitute regime was in place until January 1, 2010. Cal., Senate Approp. Comm., Cal. Bill Analysis, Assemb. Bill 48, 2009-2010 Regular Session (Aug. 17, 2009).[43]

- Florida repealed its incentive compensation ban. Florida law previously contained a specific compensation provision applicable to nonpublic postsecondary institutions that stated: "An agent shall not be compensated by commissions or bonuses based upon the number of students recruited." Fla. Stat. Ann. § 246.081(4) (2001). This provision was repealed effective January 7, 2003 – months *before* any claim in this case allegedly arose – and no similar state provision has been adopted since.

Under the broadest conceivable theory of false claims act liability, each State must still allege not only that EDMC violated a statute or a regulation, but also that EDMC certified its compliance with that statute or regulation to the state government, and that the certification was a condition of payment. The very terms of the state laws and agreements at issue bar any such claim here. The States' inability to identify any cognizable condition of payment compels dismissal of Counts VI, VII, IX, X, XI, and XIV of the Complaint and Count I of the Minnesota Complaint with prejudice.

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[42] Both Minnesota and Indiana are improperly trying to apply their false claims legislation retroactively. The relevant statutes contain no retroactive provision, and this alone requires dismissal of all claims for financial aid funds that Indiana paid before 2005, and that Minnesota paid before 2010. *See* Minn. Stat. § 15C.01 (effective July 1, 2010); *United States ex rel. McCoy v. Madison Ctr.*, No. 10-259, 2011 WL 1791710, at *2 (N.D. Ind. May 9, 2011); *Putnam*, 696 F. Supp. 2d at 1196 (holding that retroactive application of the law violates the *Ex Post Facto* Clause).

[43] California's claim for treble damages also violates its own participation agreement, which limits the State's recovery to "the actual amount of Cal Grant funds that the Institution is not entitled to retain." California IPA, Art. IV(C)(3)(x).

C. The States' Fraud-Based FCA Claims And Equitable Claims Are Not Pled With Particularity.

All of the States' claims should also be dismissed because the States have failed to plead particularized allegations as Fed. R. Civ. P. 8 and 9(b) demand, just as the Government has failed to meet its pleading obligations. *See supra*, Part II.

D. No State May Recover In Equity.

The States' equity claims also fail as a matter of law for the same reasons as the federal common law claims. *See supra*, Part IV. Regardless of what law applies, each jurisdiction shares certain common elements with the federal common law claims that preclude Counts VIII, XII, XIII, and XVI of the Complaint, and Count II of the Minnesota Complaint. *See, e.g.*, *Zarwin v. Montgomery County*, 842 A.2d 1018, 1021 (Pa. Cmwlth. Ct. 2004) (holding that recovery in equity is precluded where legal damages are available); *California Medical Ass'n, Inc. v. Aetna U.S. Healthcare of California, Inc.*, 114 Cal. Rptr. 2d 109, 125 (Cal. Ct. App. 2001) (same); *Guinn v. Hoskins Chevrolet*, 836 N.E.2d 681, 704-05 (Ill. Ct. App. 2005) (same); *Sapp v. Flagstar Bank, FSB*, __ N.E. 2d __, 2011 WL 3715281, at *7 (Ind. Ct. App. 2011) (same); and *Curtis v. Atria Group, Inc.*, 792 N.W. 2d 836, 852-53 (Minn. Ct. App. 2010) (same).[44]

VI. RELATOR MAHONEY'S CLAIMS SHOULD BE DISMISSED AS A SECOND-FILED RELATOR.

The claims of the second relator Michael Mahoney fail under 31 U.S.C. § 3730(b)(5): "When a person brings an action under" the FCA, "no person other than the Government may intervene or bring a related action based on the facts underlying the pending action." The first-

[44] In addition, California does not recognize an independent claim for unjust enrichment, and the failure of Illinois' state FCA claim is dispositive of its claim for unjust enrichment as well. *See McKell v. Washington Mut., Inc.*, 49 Cal. Rptr. 3d 227, 254 (Cal. Ct. App. 2006) ("There is no cause of action for unjust enrichment."); *Martis v. Grinnell Mut. Reinsurance Co.*, 905 N.E.2d 920, 928 (Ill. Ct. App. 2009) (holding that "[u]njust enrichment is not a separate cause of action," and "[b]ecause there was no valid underlying fraud claim, the trial court properly dismissed plaintiff's unjust enrichment claim").

to-file rule is jurisdictional and requires dismissal under Rules 12(b)(1) and 12(b)(6) of any action where an original relator amends her complaint to add a second relator. This jurisdictional bar is "exception-free … and cannot be circumvented simply by amending the complaint to add … a relator when his claims would have been barred had they been brought on their own." *United States ex rel. Duxbury v. Ortho Biotech Prods.*, 551 F. Supp. 2d 100, 110 (D. Mass. 2008) (Section 3730(b)(5)), *rev'd on other grounds*, 579 F. 3d 13, 28-29 (1st Cir. 2009); *see also United States ex rel. Wilson v. Bristol Myers Squibb, Inc.*, No. 06-12915, 2011 WL 2462469, at *8 (D. Mass. June 16, 2011) (denying leave to amend the complaint to add a second relator); *United States ex rel. Manion v. St. Luke's Reg'l Med. Ctr., Ltd.*, No. 06-498, 2008 WL 906022, at *6-7 (D. Ida. Mar. 31, 2008) (dismissing a second relator added through an amendment to the original complaint); *United States ex rel. Fry v. Guidant Corp.*, No. 03-842, 2006 WL 1102397, at *4-6 (M.D. Tenn. Apr. 25, 2006) (same). Mr. Mahoney's claims, accordingly, should be dismissed with prejudice as a second-filed action.

VII. THE COMPLAINT SHOULD BE DISMISSED WITH PREJUDICE.

Each of the Complaint's factual and legal defects is independently dispositive of the Government's and States' claims. Collectively, they illustrate the extent to which the Government is sacrificing principles of accuracy and fairness for the lure of FCA treble damages and penalties. The Government and States have had *four years* to investigate their allegations. Yet, their claims remain legally flawed and factually deficient beyond repair. They were not able to plead their claims with anywhere near the required particularity, and they failed to even tailor their list of defendants to those that were actually in existence during the relevant time period. This type of undue delay and futility should foreclose any option for amendment. *See, e.g.*, *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d at 1434; *Corsello*, 428 F.3d at 1014. For all of these reasons, the Court should dismiss the Complaint with prejudice.

CONCLUSION

The U.S. Attorney's office has announced that it is now "Open for Business" to partner with private plaintiffs to bring qui tam actions. Def. Ex. 14, *Qui Tam Litigation Western District of Pennsylvania* (Feb. 17, 2011). Quoting *Hughes Aircraft v. United States ex rel. Schumer*, 520 U.S. 939 (1997), the U.S. Attorney's office declared that the "most effective means of preventing fraud on the Treasury is to make [alleged perpetrators] liable to actions by private citizens acting … under the strong stimulus of personal ill will or the hope of gain." *Id.* at 13.

Unlike private relators, however, due process demands that the Government's actions not be driven by the potential for financial gain. As the Supreme Court noted in *Hughes*, "[a]s a class of plaintiffs, qui tam relators are different in kind than the Government. They are motivated primarily by prospects of monetary reward rather than the public good," and they are "less likely than is the Government to forego an action arguably based on a mere technical noncompliance with reporting requirements that involved no harm to the public fisc." *Hughes*, 520 U.S. at 949. In contrast, "'the Government wins its point when justice is done in its courts.'" *Brady v. Maryland*, 373 U.S. 83, 87 (1963) (citation omitted).

In its newfound zeal to do "business" with private relators, the Government has fallen woefully short of *Brady*'s standard. The mere accusation of fraud, with the draconian FCA damages and penalties that entails, causes harm and severe ramifications, especially, as the Government knows, to publicly traded companies. Yet, far from substantiating its strident accusations after four years, the Government could do no better than to adopt, largely verbatim, the relators' speculative, implausible allegations. As a result, the Complaint fails to state any legally or factually sufficient claim.

As the Complaint and its exhibits demonstrate, the Plan complied with the Safe Harbor. No factual allegations show how EDMC supposedly submitted false claims for payment, acted

with the required scienter, or caused the Government any injury. DOE's own regulations, contracts, and continued payment of federal funds to EDMC's schools and their students also undercut the attempt to plead common law equitable claims and make clear that compliance with the incentive compensation ban is not a condition of payment of government financial aid.

The "hope of gain," unsupported by fact or law, does not permit the Government to bring a massive, nationwide fraud claim as leverage with which to fill its coffers. The Government should not be allowed to ignore its own law, its own conduct, its own exhibits, and the pleading rules of this Court to make a groundless grab for money to which it is not entitled under any theory. For all the reasons stated above, the Complaints in Intervention should be dismissed with prejudice.

Respectfully submitted,

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