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¶ 50 FEATURE COMMENT: False Claims Act Liability Based On A DEI Program? Let's Think It Through

One of the more attention-grabbing aspects of Executive Order 14173, "Ending Illegal Discrimination and Restoring Merit-Based Opportunity," is the specter of False Claims Act liability for federal contractors based on their Diversity, Equity, and Inclusion (DEI) programs. Many workplace DEI programs have been viewed as a complement to federal anti-discrimination law—a tool for reducing the risk of discrimination lawsuits. The new administration, however, views DEI programs as a potential source of discrimination. EO 14173 proclaims that "critical and influential institutions of American society ... have adopted and actively use dangerous, demeaning, and immoral race- and sex-based preferences under the guise of so-called 'diversity, equity, and inclusion' (DEI) or 'diversity, equity, inclusion, and accessibility' (DEIA) that can violate the civil-rights laws of this Nation." To counteract this potential "illegal" use of DEI programs, the Trump administration is leveraging the FCA, a powerful anti-fraud statute, to enforce its policy within the Federal Government contractor community.

We discuss below the framework of the FCA, how it might apply to federal contractor DEI programs under the administration's orders, and potential hurdles the Government may face in pursuing FCA claims based on a contractor's allegedly illegal DEI program. We recommend steps contractors can take to mitigate potential FCA risks when evaluating their own DEI programs.

How Does the False Claims Act Work?—The FCA creates civil monetary liability for those who submit to the Government (1) a false or misleading claim or statement, (2) while knowing that the claim was false, and where (3) the false claim or statement is material to the Government's payment decision.

The courts have recognized a number of circumstances that can give rise to FCA liability. As relevant to EO 14173, the Government might assert that a contractor submits a "legally false" claim when it knowingly fails to comply with a contractual or legal requirement, even if the contractor otherwise performs the services or provides the goods that are the subject of the contract. This theory, endorsed by the Supreme Court in *Universal Health Servs., Inc. v. U.S. ex rel. Escobar*, 579 U.S. 176 (2016), posits that the contractor "impliedly certifies" its compliance with a material term or requirement at the time it submits its claim for payment.

The consequences of FCA liability can be significant. The statute allows the Government to recover treble

damages (i.e., three times the amount that the Government was harmed), plus civil penalties that attach to each false or fraudulent claim. See 31 USCA § 3729(a)(1). Government contractors also may find themselves facing severe collateral consequences, as a finding of FCA liability often leads to suspension and debarment proceedings, which threaten the contractor's eligibility for future federal awards.

One of the unique features of the FCA is its whistleblower provisions, which allow a private person (or company) to file an FCA lawsuit on behalf of the Government. Such qui tam lawsuits are filed in court, but under seal—i.e., not available to the public—to allow the Government to investigate the claims and decide whether to participate in the whistleblower's claims. The FCA provides strong financial incentives to would-be qui tam plaintiffs, by allowing them to share in any recovery to the Government and to recover their attorney's fees and costs incurred in bringing the action.

Whistleblower-initiated FCA activity is on the increase. Recent data shows that nearly 1,000 qui tam actions were filed in fiscal year 2024. Further, of the $2.9 billion that the Government recovered through the FCA in 2024, more than $2.4 billion resulted from qui tam cases. Whistleblowers received more than $400 million through these recoveries.

How Might Federal Contractor DEI Programs Give Rise to FCA Liability?—EO 14173 requires every Government agency to include in every contract or grant award a provision confirming that the contractor understands and agrees that "its compliance in all respects with all applicable Federal anti-discrimination laws is material to the government's payment decisions," for purposes of the FCA. Those agreements must also require contractors and grantees to certify that they do "not operate any programs promoting DEI that violate any applicable federal anti-discrimination laws." By citing the FCA and specifically invoking the element of materiality requiring certification, EO 14173 signals that the administration intends to enforce its policies through the FCA.

Of course, how the Government will include the envisioned certification into federal grants and contracts is not yet clear. Initially, some contractors received proposed bilateral contract modifications with certification language (each slightly differently worded). However, EO 14173 is being challenged in the courts, and on Feb. 21, 2025, the U.S. District Court for the District of Maryland issued a nationwide preliminary injunction that precludes the Government from imposing a DEI certification requirement for the duration of the plaintiffs' legal challenge. See *Nat'l Ass'n of Diversity Officers in Higher Educ. v. Trump,* 2025 WL 573764 (D. Md. Feb. 21, 2025). Several other federal lawsuits challenging EO 14173 are also pending.

If the certification envisioned by the EO is eventually permitted, the potential exists for the Government or a whistleblower to initiate an FCA action on the theory that the contractor's DEI program violates federal anti-discrimination law. Some Government contractors may think they should immediately abolish their DEI programs in order to neutralize the potential risk of costly FCA investigations and litigation. But as we explain below, actually winning an FCA case on the basis that the contractor's DEI program violates applicable federal law will not be a slam dunk.

What Are Some Potential Hurdles to Proving an FCA Violation Based on a DEI Program?—The plaintiff, whether the Government or a whistleblower, bears the burden of proving each element of the alleged FCA violation. The elements of falsity, scienter, and materiality could each face obstacles of proof in establishing liability based on an allegedly improper DEI program.

Falsity: To establish falsity, the Government must show that the defendant contractor submitted a claim for payment to the Government without disclosing that its DEI program violated federal anti-discrimination laws. The Government may try to argue that some portion of the contractor's DEI program is manifestly unlawful, but federal courts are divided as to whether contemporaneous, good faith differences in interpretation related to a disputed legal question (e.g., what constitutes "illegal DEI") are "false" under the FCA. A number of courts require that an alleged statement or "implied certification" is objectively false.

Adding to the uncertainty here, neither the EO nor the various agency versions of the contractor certification proposed before the district court's injunction went into effect define key terms such as "promoting," "DEI," and "illegal DEI." The administration's apparent view that certain DEI programs violate anti-discrimination statutes, such as Title VII of the Civil Rights Act, may not receive the deference that the courts once extended to the Executive Branch. See *Loper Bright Enters. v. Raimondo*, 603 U.S. 369, 412–13 (2024) (holding that courts should not defer to administrative agencies' interpretations of statutes that are clear and unambiguous).

Scienter: A false statement or certification is not actionable under the FCA unless the contractor "knew"—or at a minimum, recklessly disregarded—the falsity at the time its claim was submitted. A contractor's honestly held, good faith belief in the truthfulness of its certification is a strong defense to liability. *U.S. ex rel. Schutte v. SuperValu, Inc.*, 598 U.S. 739, 749 (2023) ("The FCA's scienter element refers to respondents' knowledge and subjective beliefs—not to what an objectively reasonably person may have known or believed."); 65 GC ¶ 166. Where contractors are required already to comply with federal anti-discrimination laws, it seems likely that they hold a good faith belief that their DEI programs are consistent with, and not contrary to, those laws. We expect that the Government will face significant hurdles in proving that contractors "knowingly" engaged in "illegal" DEI programs.

Materiality: While EO 14173 expressly invokes materiality language in its anticipated contract and grant provisions, that alone is insufficient to establish the materiality element under the FCA. Indeed, the Supreme Court has held specifically that a contract provision or regulation requiring compliance as an express condition of payment is not dispositive on materiality. *Escobar*, 579 U.S. at 190 ("not every undisclosed violation of an express condition of payment automatically triggers liability. Whether a provision is labeled a condition of payment is relevant to but not dispositive of the materiality inquiry."). Instead, establishing the materiality element under the FCA requires consideration of a variety of factors, including whether the Government continued to pay the contractor's claims in full, knowing that there were questions as to the legality of the contractor's DEI program. Given the demanding standard required to establish materiality, contractors should not feel pressured to readily concede this element merely because of a DEI certification in their contracts.

What Steps Should Federal Contractors Take to Reduce Their Risk?—Despite these likely obstacles to establishing FCA liability, EO 14173 will no doubt engender FCA investigations and whistleblower complaints in the upcoming months. To prepare for the new legal landscape, contractors should take the following precautions.

Conduct a Thorough, Privileged Analysis of All Aspects of the DEI Program: Contractors may think that abolishing their DEI program will erase the FCA risk. However, the Government has cautioned that those who try to hide DEI activities by "misleadingly relabeling" them, will still face scrutiny. See, e.g., Ending Radical And Wasteful Government DEI Programs And Preferencing—The White House (Feb. 5, 2025), available at *www.whitehouse.gov/presidential-actions/2025/01/ending-radical-and-wasteful-government-dei-programs-and-preferencing/*; Dep't of Justice, Office of Attorney General Memorandum (Feb. 5, 2025) available at *www.justice.gov/ag/media/1388501/dl?inline*. Accordingly, FCA whistleblowers may be undeterred by the absence of a specific program called DEI, particularly if such an initiative existed previously.

To be clear, even under EO 14173, it is not illegal to have a DEI program. If a contractor has such a program, now is the time to undertake a comprehensive review to ensure that it comports with current anti-discrimination laws. There are several benefits to engaging counsel to conduct this review, even if the contractor believes its DEI program is lawful. First, evaluating the program through the more critical lens of the current administration can identify any aspects that should be amended to mitigate misunderstanding and risk. Second, engaging in such a review can help establish the contractor's good faith belief in the truthfulness of its DEI certification. Third, the review can allow a contractor to explain to the Government, if necessary, the legality and business value of each element of its DEI program.

Conduct a Privileged Assessment of Public-Facing DEI Messaging: Federal contractors also should undertake a privileged review of all public-facing DEI messaging and disclosures. These can appear in various places including on a company's website, in its SEC filings, in recruiting materials, and on intranet platforms. Again, this evaluation can identify and mitigate the risk that any portion of the DEI program appears unlawful, even if it is not in practice or substance. Changes to descriptions of a company's DEI program or its commitments to non-discrimination should be made in consultation with counsel and appropriate internal and external stakeholders, to avoid inadvertent legal admissions or the perception that a company has abandoned its previously stated commitment to compliance with the law.

Maintain Real-Time Awareness and Develop a Strategy Regarding the Certification: Agencies already have begun sending their own versions of a DEI certification to contractors as proposed bilateral modifications to existing contracts, often with a demand for a response within just a few days. For new contracts, the Government may include the new certification in a portal with other representations and certifications that a contractor must complete in connection with maintaining eligibility or submitting proposals. It is critical to anticipate, identify, and be ready for the moment when a DEI certification becomes applicable to the contractor organization. Contractors should identify the person(s) within their organization likely to receive the certification requests and provide them with instructions and training on how to respond.

We also recommend consulting legal counsel in connection with making any proposed certification. Contractors may be able to present alternative responses to agency requests, rather than immediately agreeing to an ill-defined certification. For instance, the contractor might bring the ambiguities in the certification language to the attention of the contracting officer, while contemporaneously memorializing the basis for the contractor's reasonable interpretation of the ambiguous certification to assist in the defense of a future FCA claim.

Do Not Retaliate Against Employees (or Anyone) Asking Questions About the Legality of the DEI Program: In the coming months, potential whistleblowers may be sizing up whether there is a possibility for an FCA action. In so doing, they may raise questions or concerns about a contractor's DEI program. The FCA includes anti-retaliation provisions that can expose a company to an employment lawsuit, even if a substantive FCA violation cannot be established. Anticipating how to address questions about the DEI program (and documenting such exchanges) may help avoid potential legal challenges. Contractors should also confirm that employees have multiple, safe avenues to report, and provide managers and human resources professionals with guidance for responding appropriately.

Review and Consider Updates to Internal Company Policies on DEI: Contractors should consider whether to update internal policies to reflect that they contemporaneously reviewed the requirements of EO 14173 and made efforts to comply with its directives. For instance, internal policies could be amended to more clearly state that employment decisions are based on merit and not on protected characteristics. Policies could be developed that expressly disallow race or gender-based quotas, workforce balancing, required composition of hiring panels, diverse slate policies, or DEI training relying on stereotypes. Having recently updated policies that align with the new EO may provide greater protection in the event of a Government investigation, particularly if contractors can demonstrate that these new policies are subject to an internal control schedule to test for compliance.

Conclusion—We anticipate the administration will seek to vigorously enforce the requirements of EO 14173. Indeed, the EO contemplates civil compliance investigations of numerous entities ranging from publicly traded corporations to institutions of higher education. Although contractors should remain vigilant about compliance, they should also keep in mind that FCA liability for an allegedly "illegal DEI" program is not a foregone conclusion, even in the face of a certification regarding materiality. The Government (or whistleblower) must still establish an FCA violation on the specific facts at issue and likely will face challenges given the many ambiguities in the EO and in the certifications and provisions proposed to date. Even a meritless FCA suit quickly dismissed, though, is

something contractors will want to avoid. Thus, it is critical to undertake steps to mitigate the risk of a qui tam action.

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