

DOJ Civil Division Issues New Guidance on Inability-to-Pay Assessments

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The U.S. Department of Justice (DOJ) Civil Division has published new Guidance on how it will evaluate the assertions of parties who claim they are unable to pay judgments or penalties in False Claims Act (FCA) and other civil enforcement cases. While the Justice Manual already identified inability-to-pay as an independent ground justifying “compromising or closing” of civil claims in specified circumstances, see Justice Manual § 4-3.200, the new Guidance further clarifies its practice of considering an entity’s inability to pay when negotiating damages, penalties, and other liabilities. In addition to reiterating DOJ’s general policy on inability-to-pay claims, it provides a road map for companies that may be considering that approach by detailing the process and listing a number of factors that Civil Division attorneys should evaluate when considering such claims.

As a general matter, an entity’s monetary liability for a civil claim may be reduced if they offer to pay the maximum amount they can afford while still meeting their “ordinary and necessary” business or living expenses. The entity bears the burden of demonstrating an inability to pay the full amount owed, and thus must complete an extensive Financial Disclosure Form and provide any additional materials DOJ might request including tax returns, financial statements, and access to personnel with relevant knowledge. Significantly, anyone claiming an inability to pay must certify as much under penalty of perjury and may be required to provide periodic updates regarding their ability to pay until a final settlement with the Government is reached.

When analyzing inability-to-pay claims, the new Guidance instructs Civil Division attorneys – often with the help of qualified financial experts – to consider the Financial Disclosure Form and any relevant

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records in conjunction with a list of seven factors. These factors are non-exhaustive, and not every factor will apply to every claim.

1. Background on Current Financial Condition

DOJ will consider the facts giving rise to the person or entity's inability to pay. This includes whether the party "engaged in related party transactions," "removed capital," or could "reduce discretionary expenses," such as executive bonuses.

2. Alternative Sources of Capital

Attorneys will determine whether the party could raise or borrow sufficient funds to meet its liability and evaluate other sources of capital such as reserves or planned acquisitions. They will also investigate whether the party has any claims for insurance coverage or indemnification.

3. Timing of Payments

In addition to evaluating what the party can pay immediately, DOJ will consider the ability to pay over the following 3-5 years. It may agree to accept payments over an extended period of time if doing so will increase the Government's total monetary recovery. If payments are made in installments, interest will be charged and entities will generally be required to provide some form of security.

4. Tax Deductibility

DOJ will consider whether the party's payments are tax deductible.¹

5. Contingency Arrangements

In some circumstances, DOJ may consider escalation or acceleration agreements, contingent on future sales, earnings, or other growth.

6. Collateral Consequences

Attorneys will consider whether a resolution exceeding the party's ability to pay will have consequences beyond financial hardship. Such consequences might include an individual's inability to support family members, a company's inability to continue operations, or an entity's inability to comply with applicable laws and regulations. The Guidance makes clear, however, that not all collateral consequences are relevant to the Civil Division's evaluation. Specifically, the Civil Division generally will not consider adverse impacts on growth or future opportunities, product lines, dividends, executive compensation, bonuses, and hiring/retention.

7. Third Party Liability

Finally, DOJ will evaluate whether any third parties may be liable for some or all of the outstanding liability.

All in, the Guidance improves the transparency of the Civil Division's assessment of inability-to-pay assertions and reinforces that it can be a powerful settlement tool – but not one that can be yielded without merit or risk. An entity seeking to use inability to pay must be able to demonstrate that it meets the stated standards, which can prove both substantively and logistically difficult. The Guidance follows a similar publication last year from the Criminal Division on how it evaluates a business's assertion that it is unable to pay criminal fines or penalties.

Of course, there is a chance that the Government will review the Financial Disclosure Form and conclude that the company can pay an amount in excess of what the company thinks it can pay, or put forth a settlement offer larger than the submitting party previously contemplated. And, as with any investigation, there is always a risk that an extensive examination by investigators will reveal other issues. To counter those risks, companies would be wise to consider hiring financial professionals to do a thorough assessment of their condition prior to embarking on the inability-to-pay process. Moreover, to minimize the risk that the Government will use a company's financials against it when crafting a settlement offer, companies should try to lock down an agreed-upon damages cap in advance of the inability-to-pay process.

The mere act of submitting a certified Financial Disclosure Form can be a hurdle to engaging in the inability-to-pay assessment under these Guidelines. Certifying that a company's financials are correct – including past financial audits – can be an inherently risky proposition. This is particularly true when the claim to be settled relates to improper recordkeeping or expenses that were not properly accounted for when the financial statements were prepared. While companies in such situations may be able to reduce the risk of potential criminal sanctions for making false representations to the Government by being upfront with their concerns and working with DOJ to establish a mutual understanding about caveats to the certification, each case is different and there may be instances in which the risk of disclosing or certifying corporate finances prohibit an entity's engagement in the inability-to-pay assessment process.

Also, while providing a detailed description of the Civil Division's analytical framework for evaluating inability-to-pay assertions, the Guidelines do not completely address when that analytical framework will apply. For example, while the Guidelines are published by the Civil Division, they reference only the civil section of the Justice Manual, leaving unanswered whether they will apply to plea discussions with the Civil Division's Consumer Protection Branch or resolutions of civil actions involving only U.S. Attorney's Offices.