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New Mexico Court Dismisses State *Qui Tam* Suit as Unconstitutional Due to Retroactive Application of the State False Claims Statute

As more states have passed or amended state false claims laws, many state attorneys general and state *qui tam* relators have attempted to retroactively apply these punitive statutes. Last week, however, in one of the first state court decisions to address this issue, the New Mexico state court put a brake on these efforts by dismissing a well-publicized state false claims act case on constitutional grounds.

In *New Mexico ex rel. Foy v. Vanderbilt Capital Advisors, LLC*, No. D-101-CV-2008-1895 (N.M. Dist. Ct. Apr. 28, 2010), the New Mexico state district court dismissed a *qui tam* suit brought under New Mexico's Fraud Against Taxpayers Act ("FATA") on the grounds that it impermissibly sought to apply FATA retroactively to alleged misconduct which predated FATA. The state court concluded that the effect of FATA was punitive—even more punitive than the federal FCA—and held that its retroactive application would violate the Ex Post Facto clauses in both the United States and New Mexico Constitutions. The court heavily relied on the decision in *United States ex rel. Sanders v. Allison Engine Co.*, 667 F. Supp. 2d 747 (S.D. Ohio 2009), where the U.S. district court held that applying a substantive amendment to the federal FCA to conduct pre-dating the 2009 amendment would violate the constitutional prohibition against retroactive punishment. See [FraudMail Alert No. 09-10-28](#). The New Mexico decision bolsters precedents prohibiting retroactive application of recent substantive amendments to the federal FCA, and the ruling is an important first salvo in attempts to prevent the unwarranted retroactive application of state false claims laws. (The reader should note that the authors' firm represented some of the defendants in the *Foy* case.)

The *Foy* decision is particularly significant for several reasons. First, a number of larger states, such as New York, have attempted to apply their laws retroactively. These efforts have been factors in some settlements because the threat of a state FCA suit, with its treble damages and penalty provisions, is a powerful weapon in settlement discussions. Second, the Deficit Reduction Act of 2005 ("DRA") has been interpreted to require states to enact false claims laws that are at least as effective as the federal FCA in order to qualify to receive a Medicaid incentive.

See DRA, 42 U.S.C. § 1396h (2006). This qualification process is complicated by the fact that major amendments to the FCA's liability and *qui tam* provisions were enacted recently in the Fraud Enforcement and Recovery Act of 2009 ("FERA") as well as in the Patient Protection and Affordable Care Act ("PPACA"), but many states have enacted false claims laws that conform to the federal FCA prior to these amendments. See FERA, Pub. L. No. 111-21, 123 Stat. 1617 (2009) (amending 31 U.S.C. §§ 3729-3733); PPACA, Pub. L. No. 111-148, 124 Stat. 119 (2010) (amending 31 U.S.C. § 3730(e)(4)). See also [FraudMail Alert Nos. 09-05-21](#) and [10-03-24](#). Senator Grassley recently asked HHS and DOJ to review state qualifications for the Medicaid incentive under these changed circumstances. See Letter from Sen. Grassley to D. Levinson, HHS Inspector General, and E. Holder, Attorney General (Apr. 28, 2010) (requesting review of HHS guidance to states and state compliance with the DRA). The qualification process is further complicated by disputes over the interpretation of the "claims" to which the effective date for one of FERA's major liability amendments applies, as well as by challenges to the constitutionality of applying FERA's amendment retroactively to conduct predating the amendment. See, e.g., *Allison Engine*, 667 F. Supp. 2d at 751-52 (defining "claims" as payment under the statute); *United States v. Science Applications Int'l Corp.*, 653 F. Supp. 2d 87, 106-07 (D.D.C. 2009) (same); *United States v. Aguillon*, 628 F. Supp. 2d 542, 549-51 (D.Del. 2009) (same); *United States ex rel. Stephens v. Tissue Sci. Labs.*, 664 F. Supp. 2d 1310, 1315 n.2 (N.D. Ga. 2009) (applying Section 3729(a)(1)(B) to suit pending on June 7, 2008). See also [FraudMail Alert Nos. 09-10-28](#) and [09-09-16](#).

The *Foy* decision should also signal to other state legislatures contemplating enacting or amending their state false claims laws that increasing the punitive nature or effect of these laws can have significant adverse consequences for state enforcement.

Key Holding: New Mexico's False Claims Law is Clearly Punitive

New Mexico's state false claims law was enacted in 2007, with an effective date of July 1, 2007. Section 44-9-12(A) specified that:

[a] civil action pursuant to the Fraud Against Taxpayers Act may be brought at any time. A civil action pursuant to the Fraud Against Taxpayers Act may be brought for conduct that occurred prior to the effective date of that act, but not for conduct that occurred prior to July 1, 1987.

In *Foy*, the court found that this section expressly authorized FATA's retroactive application to conduct prior to its effective date, but the court noted that, even with this express declaration of retroactive effect, the statute still must be able to withstand *ex post facto* scrutiny under the United States and New Mexico Constitutions. See U.S. Const., art. I, § 9, cl.3 (directive to Congress); U.S. Const., art. I, § 10, cl. 1 (directive to states); N. M. Const., art. II, § 19. The relators in *Foy* (and the state Attorney General via an amicus brief) argued that FATA was a civil statute with a remedial effect and that the constitutional prohibition on *ex post facto* laws applied to penal, not civil, statutes. The court flatly rejected these arguments.

The court instead concluded that FATA's effect was punitive, and that applying FATA retroactively would violate the constitutional protection against punishment for past acts. The court based its

conclusion on an analysis of FATA's purpose and effect, using the factors set forth in *Kennedy v. Mendoza-Martinez*, 372 U.S. 144, 168-69 (1963). Applying the first factor, the court in *Foy* found that the FCA's sanctions have historically been regarded as punishment, and its finding relied on the Supreme Court's conclusion in *Vermont Agency of Natural Resources v. United States ex rel. Stevens*, 529 U.S. 765 (2000) that the FCA's treble damages provisions are punitive:

The U.S. Supreme Court's view that the FCA's treble damages provisions are punitive in nature tilt strongly in favor of concluding that the treble damages provision of New Mexico's counterpart "has been regarded in our history and traditions as a punishment."

Among the other factors weighing in favor of finding FATA punitive was that FATA's sanctions were "excessive" and went beyond those necessary to compensate the government for fraud. Notably, liability under FATA is joint and several, which could exacerbate the disproportionality between the sanctions under FATA (as well as under other state false claims laws that impose joint and several liability) and any non-punitive statutory purpose, because a defendant who plays a minimal role in a fraud could be punished excessively under the statute. See N.M. Stat. § 44-9-13. See also N.J. Stat. § 2A:32C-3. Additional reasons cited by the court for finding FATA punitive included FATA's lack of regulatory purpose outside of its "one objective—to define and prosecute violations of the FATA itself" and the unworkable nature of FATA's other statutory requirements (e.g., reporting requirements for state employee *qui tam* relators) if retroactively applied. The court also noted that the plaintiffs themselves had "gone to great lengths to emphasize how much more onerous the FATA [was] than the FCA." Slip op. at 21.

Quoting from the Supreme Court's decision in *Hughes Aircraft Co. v. United States ex rel. Schumer*, 520 U.S. 939, 949 (1997), the court refuted the plaintiffs' arguments that FATA did not create a cause of action for previously permissible conduct:

The extension of an FCA cause of action to private parties in circumstances where the action was previously foreclosed is not insignificant. As 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.

Moreover, the court noted that applying FATA retroactively went far beyond the circumstances in *Hughes*—where the Court rejected an attempt to retroactively apply a revision to the public disclosure bar—because, under New Mexico law prior to FATA, the possibility of *qui tam* actions did not exist. Even the relators in *Foy* themselves had recognized that FATA was "a radical new statute to make it easier" to recover "substantial damages" with "broader concepts" that went "beyond the strict common law elements for fraud."

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