CIVIL FALSE CLAIMS ACT: Senate Proposes Substantial FCA Penalty Increase to $15,000 Per False Claim

Just when it seemed impossible that the threat of False Claims Act liability could be any more oppressive, language slipped into the version of the Medicare Prescription Drug Bill recently passed by the Senate exacerbates already-pressing concerns about the constitutionality of FCA damages and penalties. The Prescription Drug and Medicare Improvement Act of 2003, passed by the Senate on June 26, 2003, contains text that significantly increases the civil penalties that may be assessed under the FCA. See S. 1, 108th Cong. § 612 (2003). The Senate bill increases the statutory minimum penalty from $5,000 per violation to $7,500. The statutory maximum is also increased from $10,000 to $15,000 per false claim. The changes, if included in the final version of the legislation that emerges from conference and is approved by the President, would apply to violations occurring on or after January 1, 2004. Similar language does not appear in the House version of the Medicare bill. News sources are reporting that the conference period is likely to be drawn out and contentious, but that the White House is exerting pressure for a final bill to be presented to the President before the August recess. The Senate is expected to go into recess on or around August 4, while the House is scheduled to begin its recess on July 28.

In 1986, the $2,000 penalty found in the original 1863 version of the False Claims Act was increased to between $5,000 and $10,000 per invoice. Pub. L. 99-562 (S. 1562), 100 Stat. 3153 (Oct. 27, 1986). On August 30, 1999, FCA penalties were adjusted for inflation under the Federal Civil Penalties Inflation Adjustment Act of 1990 to a minimum of $5,500 and a maximum of $11,000, for violations occurring after September 29, 1999. See note following 28 U.S.C. § 2461; 28 C.F.R. § 85.3(a)(9) (2002). Each false bill or voucher is generally considered by courts to constitute a separate violation, generating liability for one penalty.

It is ironic that Congress is increasing the penalties at the same time that there are increasing questions about the constitutionality of the way in which they are assessed. Each demand for payment is a separate basis for the imposition of a mandatory penalty under the False Claims Act. As a result, a government contractor or Medicare provider that causes only a few thousand dollars in actual damages, but submits many claims to the government, may be subject to FCA penalties in the tens or hundreds of millions of dollars.

Just this year, the Supreme Court clarified Congressional intent that consequential damages, pre-judgment interest, and investigative costs are not recoverable under the FCA (see Cook County v. United States ex rel. Chandler, 123 S. Ct. 1239, 1247 (2003)), but the Act contains a treble damages provision that are viewed by the Supreme Court as "rough" means of ensuring that the government is made whole. Id. See also United States v. Halper, 490 U.S. 435, 446 (1989). Together, FCA damages and penalties can...
FCA Damages and Penalties Are Punitive

The Supreme Court recently acknowledged for the second time that there is a punitive component to treble FCA damages. See Cook County v. Chandler, 123 S. Ct. at 1246. Other courts have acknowledged that FCA penalties are also punitive, and subject to constitutional limitations. See, e.g., Hays v. Hoffman, 325 F.3d 982 (8th Cir. 2003); United States v. Mackby, 261 F.3d 821 (9th Cir. 2001).

Due Process Limitations on Punitive Damages Awards

In State Farm Mutual Automobile Insurance Co. v. Campbell, 123 S. Ct. 1513 (2003), a 6-3 majority of the Supreme Court overturned a $145 million punitive damages award imposed in a case in which the jury assessed $1 million in compensatory damages. The Court declined to establish a bright line ratio, but questioned whether it was possible to justify punitive damages in excess of 10 times actual damages. It also held that “in practice, few awards exceeding a single digit ratio between punitive and compensatory damages . . . will satisfy due process.” Id. at 1524.

In the State Farm case, the Supreme Court also addressed a situation that commonly arises under the FCA, when damages are relatively low, but large numbers of false claims (and hence, penalties) give rise to a total judgment many multiples of single damages. The Court stated that higher ratios of punitive to compensatory damages “might” (emphasis in the original) satisfy due process. Id.

However, it also stated that higher ratios would pass Constitutional muster only in situations where, for example, the conduct was “a particularly egregious act,” but resulted in little economic harm. Id. The Court continued, “When compensatory damages are substantial, then a lesser ratio, perhaps only equal to compensatory damages, can reach the outermost limit of the due process guarantee.” Id.

Therefore, as actual damages increase, a much lower multiplier more than fully compensates the government (even when considering any possible intangible injuries and costs not recoverable under the FCA, like consequential damages), and even trebling may be excessive. State Farm suggests that regardless of how a multiplier is characterized, the constitutional test under the Fourteenth Amendment’s Due Process Clause is whether a judgment is reasonable and proportionate to the wrong committed. For a more complete discussion of this issue, see FraudMail Alert® No. 03-04-10.

Excessive Fines Implications

In another recently decided case, a unanimous panel of the Eighth Circuit Court of Appeals severely limited most of the civil FCA penalties imposed by the district court. See Hays v. Hoffman, 325 F.3d 982 (8th Cir. 2003). The defendant gave apples to employees over the holidays and entered the cost as “resident food” in the general ledger accounts. Employee gifts are not reimbursable under Medicaid, and the costs should have been “adjusted out,” but the relator alerted the agency processing the claim, which refused reimbursement. The relator in Hays argued that there were 200 falsely inflated claims for the cost of the apples, and sought FCA penalties for each. The Court of Appeals found that the relevant conduct was the decision to purchase the gifts and then claim Medicaid reimbursement, and that conduct was reflected only in the annual cost reports of eight of the defendant’s facilities. The court rejected the relator’s penalties analysis and held that the $1.68 million penalty imposed by the trial court under relator’s theory bore “no rational relationship to the false claim misconduct” resulting from the submission of a $6,000 overcharge. Id. at 993. The panel noted that the district court’s calculation of penalties was “laced with Excessive Fines Clause implications,” and cited approvingly United States v. Krizek, 111 F.3d 934, 940 (D.C. Cir. 1997). Id.

Both Hays and State Farm therefore clearly support the argument that the FCA should be read to avoid irrational penalty schemes. Nevertheless, Congress’s amendment of the FCA’s civil penalties serves to the increase penalty assessments that already are constitutionally suspect. In spite of the growing Due Process and Excessive Fines implications, Section 612 of the Senate bill, if passed, would only increase the likelihood that growing numbers of FCA judgments will be reversed or substantially reduced on appeal as unconstitutionally excessive.

The Senate also appears not to be aware of other consequences that may follow if its proposed penalty increases are made into law. First, faced with even more draconian penalties and higher settlement demands from the government, more defendants are likely to litigate and in fact
win cases that they currently choose to settle. Second, the fact that more judgments will ultimately be reversed on appeal increases the litigation risks and costs for the government, as well. Finally, the government's contracting partners, already pushed to the brink by an onerous and unfair FCA enforcement environment, may finally succeed in gaining enough momentum for significant reform of the False Claims Act. As more municipalities and their taxpayers also face the brunt of this increasingly harsh regime, Congress may find a groundswell of protest on its hands that will ultimately force a pendulum swing in the other direction.

If you would like to receive a copy of the language in Section 612 of the Senate bill discussed above, or if you have questions regarding this area, please contact us at fraudmail@ffhsj.com or (202) 639-7220.

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