

Skyrocketing FCA Penalties Ripe For Constitutional Challenges

Law360, New York (July 12, 2016, 1:15 PM ET) --

The U.S. Department of Justice recently announced dramatically higher civil penalties under the False Claims Act, pursuant to authorization in the Bipartisan Budget Act of 2015. The announced increases make the FCA's already draconian penalties even more so, particularly in cases involving individual claims for small dollar amounts. To date, constitutional objections to outsized FCA judgments have experienced little success. But the higher penalty ranges may change the calculus of how courts view constitutional challenges to FCA civil penalties, creating opportunity for defendants finally to gain traction in arguing for constitutional limits to FCA penalties.

Since 1999, the amount of civil penalties under the FCA has ranged from \$5,500 to \$11,000 per claim, regardless of the damages sustained by the government. The Bipartisan Budget Act of 2015 requires federal agencies to make annual adjustments to the civil monetary penalties over which they have jurisdiction, based on changes in the Consumer Price Index. H.R. 1314, 114th Cong. § 701(b). Unless an agency chooses to go through an onerous exceptions process, all federal agencies must implement the same adjustment through interim final rulemaking that is effective no later than Aug. 1, 2016. On June 29, 2016, the DOJ announced that effective Aug. 1, 2016, the range of civil penalties would practically double, resulting in a range of \$10,781 to \$21,563 — again, regardless of the amount of actual damages.

Even before this near-doubling, FCA penalties often dwarfed the government's actual damages, leading some defendants to argue that the severe penalties they face violate the Eighth Amendment's prohibition on excessive fines. In conjunction with the FCA's treble damages provision, some defendants have also argued that aggregate financial awards under the FCA violate due process protections.

The U.S. Supreme Court has never ruled on whether the Excessive Fines Clause applies to FCA penalties. In weighing the merits of Eighth Amendment challenges, lower courts have generally looked to *United States v. Bajakajian*, 524 U.S. 321 (1998), which held that fines are payments that are "punitive" in nature, and they are excessive where "grossly disproportional to the gravity of the defendant's offense." The majority of circuit courts faced with the question have held that FCA penalties are intended at least partially to be punitive, and therefore subject to challenge under the Eighth Amendment. See *United ex rel. Bunk v. Gosselin World Wide Moving, N.V.*, 741 F.3d 390 (4th Cir. 2013); *Hays v. Hoffman*, 325 F.3d 982 (8th Cir. 2003); *United States v. Mackby (Mackby I)*, 261 F.3d 821 (9th Cir. 2001); but see *United States v. Rogan*, 517 F.3d 449 (7th Cir. 2011) (declining to rule on whether petitioner's penalties under the FCA were subject to attack under the Eighth Amendment). But successfully establishing that FCA penalties are "grossly disproportional" to the underlying fraud has been a difficult hurdle to clear.

The fact that the FCA provides for both civil penalties and treble damages makes for a complex analysis. The Supreme Court has recognized that at least some portion of the FCA's treble damages provision is punitive. See *Vt. Agency of Natural Res. v. United States ex rel. Stevens*, 529 U.S. 765, 784 (2000). But circuit courts are still grappling with how exactly to

count those trebled damages in the analysis, particularly in comparing the disparity between actual harm and punitive damages. Compare *United States v. Mackby* (*Mackby II*), 339 F.3d 1013, 1019 (9th Cir. 2003) (stating that some portion of the FCA trebles damages and civil penalty is remedial), with *United States v. Aleff*, 772 F.3d 508, 512 (8th Cir. 2014) (finding FCA treble damages in combination with the per-claim penalties purely punitive for the Excessive Fines Clause analysis).

This area of ambiguity is significant because when considering the permissibility of punitive damages under the Due Process Clause, the Supreme Court has instructed lower courts to consider three factors functionally similar to the *Bajakajian* test: “(1) the degree of reprehensibility of the defendant’s misconduct; (2) the disparity between the actual or potential harm suffered by the plaintiff and the punitive damages award; and (3) the difference between the punitive damages awarded by the jury and the civil penalties authorized or imposed in comparable cases.” *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 418 (2003).

Last year, the Fourth Circuit conducted a thorough analysis of when treble damages and statutory penalties together implicate the scope of Eighth Amendment and Due Process Clause protections. See *United States ex rel. Drakeford v. Tuomey*, 792 F.3d 364 (4th Cir. 2015). The *State Farm* factor most critical to the court’s analysis was the disparity between the actual damages and the magnitude of the punitive damages award. The court clearly separated out two components of FCA damages as compensatory, rather than punitive: the government’s single (actual) damages and the relator’s share of the treble damages. The remainder (double damages minus the relator’s share) plus civil penalties represented the punitive component of the financial judgment.

The court compared the punitive portion to the compensatory portion, which yielded a 3.6:1 ratio. *Tuomey*, 792 F.3d at 389. Although the Supreme Court has avoided promulgating a bright line rule on this factor, in *State Farm* the Supreme Court explained that “few awards exceeding a single-digit ratio between punitive and compensatory damages, to a significant degree, will satisfy due process.” 538 U.S. at 425. Furthermore, the court pointed to two earlier cases that implied even a 4:1 ratio “might be close to the line of constitutional impropriety.” *Id.* The *Tuomey* court upheld the FCA judgment largely on the basis of *State Farm*’s dicta regarding permissible ratios.

The Fourth Circuit’s *Tuomey* analysis collapses into a simple equation laying out a roadmap for calculating punitive-to-compensatory ratios under prong two of the *State Farm* test:

$$((\text{double damages} - \text{relator's share}) + \text{civil penalties}) / (\text{single damages} + \text{relator's share}).$$

According to Supreme Court dicta, where the resulting ratio is 4:1, constitutional protections may be implicated, and certainly where the ratio exceeds single digits, defendants will have particularly strong challenges under the Due Process Clause. Because the Bipartisan Budget Act of 2015 nearly doubled the civil penalties component of the numerator, it likely broadened the circumstances in which FCA judgments create constitutionally suspect disparities. For example, had the new statutory minimum penalty of \$10,781 been applied in *Tuomey*, the ratio of punitive to compensatory damages would have been 5.9:1. Similarly, in the Ninth Circuit’s *Mackby* case, the ratio would have moved from 11.5:1 to 22.6:1, well in excess of the threshold at which the Supreme Court has indicated an award may raise constitutional issues. See *Mackby II*, 339 F.3d at 1015.

One issue courts will likely need to grapple with under the *State Farm* construct is the extent to which reprehensibility justifies punitive ratios above four, particularly as they veer

toward double digits. While the State Farm court implicitly acknowledged that, under prong one, purely economic crimes are less reprehensible than violent or reckless ones, it also set forth factors shaping the contours of economic reprehensibility: whether “the target of the conduct had financial vulnerability; the conduct involved repeated actions or was an isolated incident; and the harm was the result of intentional malice, trickery, or deceit, or mere accident.” State Farm, 538 U.S. at 419. See, e.g., Aleff, 772 F.3d at 512–13 (finding defendants’ actions to be reprehensible when it included a scheme to defraud the government that spanned two states and more than six years); Tuomey, 792 F.3d at 389 (noting that defendant’s conduct was reprehensible because of “the sheer breadth of the fraud Tuomey perpetrated upon the federal government” and the deliberateness of the fraud); see also Saunders v. Branch Banking & Trust Co. of Va., 526 F.3d 142, 153 (4th Cir. 2008). The government can be expected to argue in cases alleging fraud on federal healthcare programs that such crimes are particularly reprehensible given that these programs typically serve vulnerable populations.

Given how relatively few FCA cases proceed to judgment, it will likely take many years for these constitutional issues to play out in courts. In the meantime, however, existing case law provides a strong basis for defendants to resist exaggerated calculations of potential exposure by DOJ or relators, at least where those exposure estimates implicate constitutional limitations.

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