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OVERVIEW OF FALSE CLAIMS AND FRAUD LEGISLATION

HEARING

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

NINETY-NINTH CONGRESS

SECOND SESSION

ON

LEGISLATION TO COMBAT THE GROWTH OF FRAUD AGAINST THE FEDERAL GOVERNMENT THROUGH THE FILING OF FALSE CLAIMS BY GOVERNMENT CONTRACTORS

JUNE 17, 1986

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TUESDAY, JUNE 17, 1986

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The committee met, pursuant to notice, at 11:07 a.m., in room SD-226, Dirksen Senate Office Building, Hon. Strom Thurmond (chairman of the committee) presiding.

Present: Senators Hatch, Grassley, and Specter.

Staff present: Randy Rader, counsel; Abigail Kuzma, counsel; and Mike Regan, counsel.

OPENING STATEMENT OF CHAIRMAN STROM THURMOND

The CHAIRMAN. The committee will come to order.

The Senate Judiciary Committee today considers legislation to combat the growth of fraud against the Federal Government through the filing of false claims by Government contractors. The Congress has held numerous hearings, has thoroughly examined this troublesome problem, and has concluded that remedial legislation is necessary. I am disturbed by the seemingly constant news reports of allegations of excessive profits taken by contractors under contracts with the Federal Government.

Nonetheless, I believe that remedial legislation must be fair and mindful of the constitutional protections that all in this country enjoy. To that end, I sincerely hope that the Congress will carefully examine all false claims legislation to ensure that tbese protections are preserved.

Some have raised questions about whether fraud and misrepresentation, whicb are based in common law, should be adjudicated before agencies without benefit of a jury trial. Additionally, concern has been expressed about the use of negligence as a lisbility standard and the preponderance of the evidence as the burden of proof in these fraud cases.

We have a distinguished list of witnesses appearing before this committee today, and I look forward to receiving their testimony, as we work toward a fuller understanding of the fraud problem and the development of tbe best solution.

Now, we are marking up a defense bill, the annual defense bill in the Armed Services Committee and I am going to have to turn this hearing over to Senator Hatch in a few minutes. I will take pleasure of reading the statements later, because this is a very important matter.

The first witness today I believe is Mr. Richard Willard, Assistant Attorney General. Mr. Willard, can you take about 5 minutes and put the rest of your statement in the record? We have a lot of witnesses here.

You may proceed.

STATEMENT OF RICHARD K. WILLARD, ASSISTANT ATTORNEY GENERAL, CIVIL DIVISION, DEPARTMENT OF JUSTICE

Mr. WILLARD. Thank you, Mr. Chairman.

It is a pleasure to be here today to testify with regard to the two antifraud bills which the administration has recommended and which have been introduced by Senator Cohen as the Program Fraud Civil Remedies Act, and by Senator Grassley as the False Claims Act Amendments. We appreciate the strong bipartisan interest that has been shown for the legislation, and the leadership which Senators Cohen and Grassley have shown in introducing them. I am particularly interested in discussing with members of the committee, including Senator Hatch, questions which have come up with regard to this legislation.

We think the antifraud bills are a good package generally. We are very supportive of the bills and we know members of this committee are very interested in having an effective civil fraud remedy available to the Government. Yet at the same time we want to answer questions that may have come up with regard to these packages.

Many of the questions have come up with regard to the administrative civil fraud remedy that is contained in Senator Cohen's bill. Fortunately, we have a model we can look to in this area, and that is the civil money penalty law under which the Department of Health and Human Services has been operating for several years now, recovering over $21 million of money which had been defrauded from the Government in the Medicare and Medicaid Programs. Inspector General Kusserow is here today to testify about how that program is operated and we think that their successful experience provides a model which Congress can use to extend for use in remedying civil fraud against the Government.

The administrative procedures contained in this act are procedures which we believe fully protect the due process rights of individuals and companies that are subject to these administrative proceedings. These are modeled on the Administrative Procedure Act and provide the same kind of due process protections that have been repeatedly upheld by the courts in administrative-type proceedings.

In particular, there is the protection of judicial review by the article III courts, which is a standard feature of the administrative law and which we think will further ensure that proceedings under this administrative remedy are conducted fairly with due regard for the procedural right of anyone who is subject to these proceedings.

We do not believe, in light of the *Atlas Roofing* decision by the Supreme Court, that this kind of administrative proceeding violates anyone's seventh amendment right to trial by jury under our Constitution. The Supreme Court held in *Atlas Roofing* that Congress

had the power to create new kinds of statutory rights and remedies and that those would not be subject to the common law right to trial by jury as it existed at the time the seventh amendment was adopted. We believe that same reasoning would apply equally to this kind of proceeding for a civil remedy following administrative procedures.

One of the issues that has come up, Mr. Chairman, is the standard of intent with regard to enforcement of this act. Our proposal in Senator Cohen's bill as paralleled in Senator Grassley's proposed amendments to the False Claims Act, is to clarify what we think is the better view of the existing law as to the appropriate standard of intent.

The courts bave been divided on what is and should be the standard of intent which the Government must show to prove a violation of the False Claims Act. What we hope to do is to eliminate some of this confusion by having legislation clarify the level of intent; and in this regard we are trying to steer a middle course between two extremes.

On the one hand, we do not think that mere negligence should provide a basis for a civil fraud remedy. I do not think anyone believes that. On the other hand, we do not think that we should have to prove a criminal standard of specific intent to defraud the Government. That is the kind of standard which is associated with criminal penalties, rather than civil penalties, and we think would be difficult to prove in many cases.

We have tried to recommend an intermediate course, a standard that would require knowledge of the false claim and would provide that there is some duty on the part of the contractor to ascertain when they make a claim against the Government that there is a reasonable basis for it. But this standard would not impose liability for an innocent mistake or mere negligence.

I think that the legislative history can clarify this intent and ensure that these remedies are not used to penalize honest mistakes. We certainly hope the legislative history will clearly reflect that that would not be the intent of Congress in enacting either of these laws.

There is one other aspect of the bill I would like to comment on, and that is the issue of the investigative subpoena for inspectors general. The administration has oppesed the inclusion of a testimonial subpoena power on the ground that this is not normal for investigative agencies. The FBI does not have testimonial subpoena power and, therefore, we do not think it should be included for the inspectors general.

If it is included, though, we are satisfied that giving the Attorney General power to control the use of it would at least prevent it from being subject to any abuse.

In conclusion, I think that the legislation that the committee is considering, both the Cohen and Grassley bills would be very productive contributions to our efforts to pursue civil fraud litigation on behalf of the Government. Moreover, the bills would help to clarify many of the legal issues that have diverted the enforcement effort in recent years as the courts have come up with differing interpretations of the existing law.

In particular, the administrative remedy would allow many cases to be brought that otherwise would be too small to be profitably pursued in Federal courts. For that reason we strongly support both bills and hope that the Senate will give them favorable consideration.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Willard follows:]

STATEMENT

OF

RICHARD K. WILLARD
ASSISTANT ATTORNEY GENERAL
CIVIL DIVISION
DEPARTMENT OF JUSTICE

Mr. Chairman and Members of the Subcommittee:

It is a pleasure to be here today to discuss the Administration's anti-fraud legislation. As you know, Mr.Chairman, the two bills which are the heart of our legislative initiative -- Senator Cohen's Program Fraud Civil Remedies Act and Senator Grassley's False Claims Act Amendments--are similar to the administration's bills, which were announced by the Attorney General at a press conference last September and transmitted to the Congress as part of the President's Management Improvement Legislative Program of last summer. They are a major part of our continuing war on economic crime and I an happy to see that they have received bipartisan support in the Congress.

In prior appearance before this Committee, the Governmental Affairs Committee and the House Judiciary Committee, the Department has presented extensive testimony on this relatively complex legislation. Rather than reiterate our elaborate comments on this legislation, I would like to take this opportunity to discuss briefly some of the more critical issues raised by the two bills -- particularly the Program Fraud legislation, with which this Committee is perhaps less familiar.

The Program Fraud Civil Remedies Act, S.1134, is the product of a lengthy and very careful legislative development in the Governmental Affairs Committee. I note that previous versions of the bill date back to the 97th Congress, which were, in turn, based on draft legislation prepared by the Justice Department.

Justice Department officials, representatives of the Inspectors General, and the private bar have all been consulted and had input into the final product, which was reported by the Governmental Affairs Committee last November. It is, in our view, a very good bill.

We believe that a mechanism for resolution of many fraud matters through administrative proceedings is long overdue. Many of the government's false claims and false statement cases involve relatively small amounts of money compared to matters normally subject to litigation. In these cases, recourse in the federal courts may be economically unfeasible because both the actual dollar loss to the government and the potential recovery in a civil suit may be exceeded by the government's cost of litigation. Moreover, the large volume of such small fraud cases which could be brought would impose an unnecessary burden on the dockets of the federal courts.

Fortunately, legislative efforts in this area can be guided by the experience of the Department of Health and Human Services under the Civil Money Penalty Law, 42 U.S.C. 1320a-7a, a similar administrative money penalty statute which has been in effect for several years. Under that law, HHS has recovered over $21 million under the Medicare and Medicaid programs. Inspector General Kusserow and the entire Department are to be commended for their efforts. HHS's successful experience testifies to the great savings which could be achieved if this authority were extended government-wide.

The administrative proceedings outlined in section 803 of S. 1134 preserve full due process rights, including the rights to notice, cross examination, representation by counsel and determination by an impartial hearing officer, and thus will withstand constitutional challenge. The use of a hearing

examiner, or Administrative Law Judge, to compile a factual record and make an initial determination is a common, legally unobjectionable method to administer federal programs. Critics of the use of hearing examiners can point to no legal precedent questioning this administrative hearing mechanism, and, in fact, it has been upheld consistently against court challenge. See, Butz v. Economou, 438 U.S. 478, 513-4 (1978); NLRB v. Permanent Label Corp., 687 F.2d 512, 527, (Aldisert, C.J., concurring).

Criticism of the hearing examiner's supposed lack of independence ignores these well established precedents as well as several protections built into S. 1134. While the hearing examiner would be an employee of the agency, section 803(f)(2)(C) of the bill assures the hearing examiner an appropriate level of independence by providing that he shall not be subject to the supervision of the investigating or reviewing official, and could not have secret communications with such officials. The bill thus incorporates the generally accepted protections required by the Administrative Procedure Act. And, of course, any adjudication of liability under this bill would be subject to independent review in the Court of Appeals by an Article III judge.

In light of the Supreme Court's holding in Atlas Roofing Co. v. Occupational Safety and Health Administration, 430 U.S. 442 (1977), we do not believe that these proceedings would violate the Seventh Amendment's guarantee of trial by jury. In Atlas Roofing, the Court rejected a Seventh Amendment challenge to the administrative penalty provisions of the Occupational Safety and Health Act of 1970 because it concluded that Congress had created new rights which did not exist at common law when the Amendment was adopted. The Court held that:

> when Congress creates new statutory "public rights," it may assign their adjudication to an administrative agency with which a jury trial would be incompatible, without violating the Seventh Amendment's injunction

> that jury trial is to be "preserved" in "suits at common law".

430 U.S. at 455. The rights created here are not co-extensive with any common law cause of action known when the Seventh Amendment was adopted. In addition, we believe that this statute may, like the False Claims Act, be characterized as a "remedial" statute imposing a "civil sanction". See United States ex rel. Marcus v. Hess, 317 U.S. 537 (1943). Given these considerations, the administrative proceedings do not deny unconstitutionally trial by jury.

Perhaps the most significant issue in the debate over S. 1134 is one which goes to the heart of the civil enforcement provisions of the Act: the standard of knowledge required for a violation of the Act. As a civil remedy designed to make the government whole for losses it has suffered, the False Claims Act currently provides that the government need only prove that the defendant knowingly submitted a false claim. However, this standard has been misconstrued by some courts to require that the government prove that the defendant had actual knowledge of the fraud, and even to establish that the defendant had specific intent to submit the false claim. Eg., United States v. Mead, 326 F.2d 118 (9th Cir. 1970). This standard is inappropriate in a civil remedy, and S. 1134 -- as well as S.1562, the bill reported from this Committee -- would clarify the law to remove this ambiguity.

The standard contained in the bills would punish defendants who knowingly submit false claims. The bills define the key term "knowingly" to punish a defendant who:

> (A) has actual knowledge that the claim or statement is false, fictitious or fraudulent or;
>
> (B) acts in gross negligence of the duty to make such inquiry as would be reasonable and prudent to conduct under the circumstances to ascertain the true and accurate basis of the claim or statement;

S. 1134, §801(a)(b). Essentially the same formulation, with slight wording changes, is included in S. 1562, new section 3729(c).

This standard achieves two goals. First, it makes clear that something more than mere negligence is required for a finding of liability. Second, it reaffirms the widely shared belief that anyone submitting a claim to the government has a duty -- which will vary depending on the nature of the claim and the sophistication of the applicant -- to make such reasonable and prudent inquiry as is necessary to be reasonably certain that he is, in fact, entitled to the money sought. This concept of an inherent duty to make reasonable inquiry before submitting a claim to the government is reflected in the better reasoned caselaw. See, eg., United States v. Cooperative Grain Supply Co., 472 F.2d 47 (8th Cir. 1973). A more detailed explanation of the Department's endorsement of this standard is set forth in the attached December 11, 1985 letter to Senator Charles McC. Mathias.

We believe that this standard reflects well-developed scienter concepts which would fully protect honest individuals in their dealings with the government. The False Claims Act has been in place since 1863, and we are unaware of any case under the Act in which a contractor or other recipient of government funds has been punished for an honest dispute with the government. In particular, we would strongly oppose any effort to engraft upon the existing scienter standard another requirement that a knowingly false claim must be accompanied by an intent to defraud. In our experience, intent requirements in the civil area lead to confusion and impose an overly stringent burden upon the government. The False Claims Act is not generally interpreted to require a showing of intent, see, eg., Cooperative Grain & Supply Co., and we do not believe that such an intent requirement should be imposed here.

Questions have also been raised as to the effect which a finding of liability under this Act would have on a subsequent administrative proceeding to suspend or debar a contractor. Some have suggested an amendment to prevent the use of a civil penalty judgment in debarment or suspension proceedings. However, in our view, amending the bill to deny any evidentiary value to a civil penalty judgment in any administrative, civil or criminal proceeding is wholly inappropriate. The civil penalty proceedings envisioned by the bill will afford a full measure of due process protections, as well as the opportunity for judicial review of the proceedings. In view of this consideration, we believe that there is no justification for disturbing the normal rules of res judicata and collateral estoppel, and requiring another tribunal to go through the costly exercise of retrying the same facts that have already been established under the same standard of proof in a civil penalty proceeding.

In addition, it is important to note that a contractor would always be free to argue the question of remedy in a suspension or debarment proceeding. According res judicata or collateral estoppel effect to the facts underlying a civil penalty judgment in a later suspension or debarment proceeding would not necessarily establish that suspension or debarment was the appropriate remedy. A contractor would still have the opportunity to argue that he should not be suspended or debarred and that some lesser sanction -- or no sanction at all -- should be imposed.

In one respect, however, S. 1134 could still be improved. The Department continues to have strong objections to section 804(a)(2), which permits Inspectors General and other investigatory officials to use compulsory process to obtain testimonial evidence as part of an investigation. Under the existing provisions of the Inspector General Act of 1978, Inspectorm General are authorized to compel production of

documentary evidence. Neither the Inspectors General, nor the Federal Bureau of Investigation -- the government's principal law enforcement investigatory agency -- currently issue investigative subpoenas to compel testimony. The potential for the unlimited exercise of testimonial subpoena powers during investigations might raise due process issues as well as interfere with the criminal investigation process. In addition, although the Attorney General is granted 45 days to review and veto any such subpoena, this short period would prove inadequate to ensure consistency of standards and implementation. Given the proliferation of ongoing grand jury investigations targeted at fraud, there would be a serious potential for conflict with testimonial subpoenas issued by the IG's. In this manner, section 804(a)(2) could adversely affect coordinated law enforcement. Consequently, the Administration strongly urges the Congress to delete section 804(a)(2).

Finally, let me speak briefly to S.1562, Senator Grassley's False Claims Act Amendments. This bill, ordered reported from the Judiciary Committee in December, incorporates nearly all of the Administration's proposed amendments. It would modernize the Act, clarify the standard of knowledge and the burden of proof (which are subject to conflicting circuit court interpretations), and give the Civil Division the authority to issue Civil Investigative Demands (CID), a much needed investigative tool. Our previous statement fully explains the justification for each of the changes included in the bill. However, there is one point relating to the CID authority which I would like to stress. I think it is important that the Justice Department be able to share information which it acquires through a CID with other agencies for use in exercising their statutory responsibilities. Evidence of fraud on the government could implicate a host of other statutory concerns unrelated to the public purse. For instance, substandard goods provided to the government might also

be in violation of health and safety regulations enforced by other federal agencies. As long as there are appropriate safeguards to prevent indiscriminate dissemination -- such as the requirement in S. 1562 that Justice obtain a court order authorizing sharing with another agency -- we believe that sharing CID information is in the public interest.

Perhaps the most complex issue raised during Committee consideration of the False Claims Act amendments was the proposed amendments to the "qui tam," or citizen suit, provisions of the Act. Because of the demonstrated, consistent misuse of the current qui tam statute to bring frivolous, politically-motivated lawsuits, the Justice Department has strong reservations about any effort to further liberalize this provision. Nevertheless, we recognize that many Members of Congress believe that changes in the statute are needed to encourage the efforts of "whistleblowers" who may have inside knowledge about fraud in the government. In an effort to advance this legislation, we entered into discussions with the proponents of the qui tam changes, and ultimately reached a reasonable compromise which is embodied in S. 1562 as ordered reported from the Committee. While we continue to have some reservations about these changes, we believe that the compromise contains adequate protections against misuse and frivolous litigation. We do not believe that concerns about S. 1562's relatively marginal changes in the qui tam statute should stand in the way of prompt passage of the bill.

That concludes my prepared statement and I would be happy to answer questions about the Administration's two bills.

The CHAIRMAN. Thank you very much.

I overlooked calling on the able chairman of the Subcommittee on the Constitution to see if he had a statement.

Senator HATCH. I will just put my statement in the record, Mr. Chairman.

The CHAIRMAN. We also have statements of Senators Grassley and McClure for the record.

[Prepared statements follow:]

PREPARED STATEMENT OF SENATOR ORRIN G. HATCH

The purpose of this hearing is to examine legislation within the 99th Congress responding to the problem of freud and false claims and statements against the Federal Government. I want to thank Senators Cohen and Levin for their extensive work in this area and for their willingness to join the Judiciary Committee in examining this important issue. I also want to thank Senators Hawkins and McClure for their comments.

The seriousness of Government program freud is well documented. A 1981 General Accounting Office report documented over 77,000 cases of fraud and other illegal activities reported in 21 agencies during a 3-year period. While the tremendous impact of such fraud during a three-year period. While the tremendous impact of such freud is clear, particularly in light of efforts to trim the burgeoning Federal deficit, the establishment of a broad based administrative procedure to punish fraud and false claims has many important implications.

Legislation introduced within the 97th, 98th and 99th Congresses has proposed legal mechanisms and penalties to respond to this difficult problem. The procedural provisions of each of these bills have elicited objections, many of them constitutional in natura.

Firet, seventh amendment questions have been raised. The seventh amendment provided that "In suits at common law, where the value of controverey shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by jury shall be otherwise re-examined in any court of the United States, than according to the rules of the common law." This concern is relevant to legislative proposals that do not provide for a jury trial but instead establish an alternative mechanism in the form of an administrative procedure to pureue false claims. With seventh amendment concerns in mind we must examine the nature of the protections guaranteed by the seventh amendment. Given the "criminal-like" espects of fraud and the stigma associated with a finding of liability for fraud, is an administrative procedure adequate under the seventh amendment?

Concerns involving the due process of the fifth amendment are equally important. The concept of due process of law under the fifth amendment embraces a broad range of procedural and substantive requirements intended to preserve "Those canons of decency and fairness which express the notions of justice of english-speaking peoples." This requirsment of fundamental fairness involves basic rights of notice and a fair public hearing before an impartial tribunsl, of discovery of the evidence and cross-examination of witnesses, judicial review of the action of administrative officers. With these concerns in mind, I look forward to hearing the testimony at today's hearing.

PREPARED STATEMENT OF SENATOR CHARLES E. GRASSLEY

Mr. Chairman, the "False Claims Act" is the Government's primary weapon against fraud, yet is in need of subetantial reform. A review of the current environment is sufficient proof that the Government needs help—lots of help—to adequately protect the Treasury against growing and increasingly sophisticated fraud.

I appreciate the opportunity to participate in this hearing on Government fraud remedies. We have spent a considereble amount of time in the Subcommittee on Administrative Practice and Procedure examining different types of frauds which steal away much needed taxpayer funds. In the face of our current Federal debt crisis, it is more important than ever that we maintain an efficient, fair and most of all, effective enforcement system to protect our Federal dollars from fraud and abuse.

No single piece of legislation can absolutely guarantee an efficient, fair and effective enforcement system. We would be deluding ourselves to assume that security. However, to the extent we can strengthen weaknesses in the law which allow frauds

to go undetected or unaddressed and fraudulently obtained funds uncollected—that is the type of legislative remedy we should enact without delay.

As the chairman knows, there are fraud reform measures supported by the administration which are pending now in the Senate. With congressional interest high and the President's solid support, this is an ideal opportunity for legislators, the grass roots public, and the Government contracting industry, to work together to enact meaningful reforms.

There is no question that the current state of affairs begs for reform. Fraud allegations are climbing at a steady rate while the Justice Department's own economic crime council last year termed the level of enforcement in defense procurement fraud "inadequate."

No one knows, of course, exactly how much public money is lost to fraud. Estimates range from hundreds of millions of dollars to more than $50 billion per year. Sadly, only a fraction of the fraud is reported and an even smaller fraction of the funds recovered.

Part of the solution is to develop a way for frauds of lesser significance or lesser dollar amounts to be remedied. Too many minor fraud cases slip through the cracks or simply are refused by the Justice Department due to a judgment that pursuance of the cases would not be cost effective.

I strongly support and am a cosponsor of S. 1134 introduced by Senator Cohen and reported favorably by the Governmental Affairs Committee. The "Program Fraud and Civil Penalties Act" expands, Government wide, an administrative system for addressing small dollar fraud—a system that has produced impressive results at the Department of Health and Human Services.

Another part of the solution—something I consider essential to any meningful improvements in cutting down fraud—is the establishment of a solid partnership between public law enforcers and private taxpayers. The Federal Government has a big job on its hands as it attempts to ensure the integrity of the nearly $1 trillion we spend each year on various programs and procurement. That job is simply too big if Government officials are working alone.

The concept of private citizen assistance is embodied in S. 1562, the False Claims Reform Act which was reported favorably by the Senate Judiciary Committee last December. This bill, which I sponsored along with bipartisan cosponsors including my colleagues on this committee, Senators DeConcini, Hatch, Metzenbaum, Leahy and Specter, is supported also by the administration and its amendments have received endorsements from both the Packard Commission and the Grace Commission's committee against Government waste.

I look forward to hearing from today's witnesses. As we listen to their testimony I think we should keep in mind that fraud flourishes where incentives encourage it. If our interest is in saving taxpayer dollars through decreasing fraud, our emphasis should be on ensuring that cheating the Government does not pay.

Thank you, Mr. Chairman.

Prepared Statement of Senator James A. McClure

Mr. Chairman, I deeply value the opportunity to commend this Committee, its Chairman and the distinguished Senator from Utah, Senator Hatch, for holding these hearings and for agreeing to study the constitutionality and other aspects of the various false statement or false claims bills which may come before the Senate in this session.

As the distinguished acting Chairman is aware, on March 14, 1986, I asked Senator Thurmond to arrange for this hearing and study because of my own uncertainty concerning the constitutionality of certain salient aspects of the proposed laws.

In a general sense, my chief reservation is that both S. 1134 and S. 1562 would permit the imposition of very large so-called "civil fines" on an individual but deny the citizen being penalized any recourse to a jury trial or even to a court trial without a jury.

Although I am aware that certain existing statutes permit the imposition of small civil penalties in cases involving false claims made against the government, I am also aware that those statutes are very limited in scope and have been deemed by the courts to be essentially compensatory to the government rather than punitive to the individual . The legislation now contemplated seems to me to be very much broader in scope and clearly intended to be more in the nature of a device for imposing criminal fines than for recovering civil damages.

Although I make no claim to be a constitutional scholar, my intuition as a lawyer and student of American History tells me that there is something fundamentally wrong about permitting a

government bureaucrat to assess cumulative fines of $100,000 or more against an individual with no safeguard whatsoever of the fundamental right of each of us to be tried before a jury of our peers or at least to have our case heard in a duly constituted court as trier of fact.

This point brings me, Mr. Chairman, to another central difficulty that I believe the Committee should examine. The proposals under study all involve what has come to be called "court stripping." This term means depriving the Article III courts of statutory jurisdiction to hear certain types of cases and controversy through the authority of Congress to establish and thereafter to specify by statute the jurisdiction of the federal courts in those areas where jurisdiction is not specifically granted to the Supreme Court by the Constitution.

Most often we have heard the term "court stripping" used in connection with debates on prayer in school, right to life, busing, and similar controversies. In this case, that is of the false claim legislation, "court stripping" would be used to prevent trial court jurisdiction and authority and to allow only highly limited appeal to the Federal Courts of Appeals from arbitrary or capricious decisions. Obviously, if this procedure can be followed with respect to alleged false statements made to a government bureaucrat, then it can also be followed in the other areas I have mentioned.

This aspect of the legislation should therefore receive close scrutiny before this Committee because there will undoubtedly be Senators who will wish to use the "court stripping" provisions in these bills as a vehicle for reducing or prohibiting the jurisdiction of federal courts in other areas.

A final aspect of these proposals which I find anomolous is the overall lack of equity in the powers given the government and the powers given to a citizen subjected to the procedures specified. Although there are many horror stories concerning citizens and businesses taking unfair or illegal advantage of the government in a wide variety of government programs, there are also countless similar occasions in which the government or government bureaucrats have abused citizens and private businesses. No Senator can long serve in this body without having brought to his attention incredible examples of abuse of power by government officials resulting in significant economic or emotional harm to private individuals and small business.

Perhaps the Committee should consider whether there is not some way in which the legislation can be balanced so that a citizen or business damaged by a false claim or statement of a government official could not also collect a $10,000 "civil penalty" from the Treasury or from the official individually or from both.

Maybe you should consider an amendment to make the liabilities of the legislation clearly applicable to false statements, oral or written, made by any government official through which a citizen is damaged. Obviously, the amendment would not apply to statements made in constitutionally protected debate.

In conclusion I again thank this distinguished Committee and my good friend who is Chairing this hearing for the work you have undertaken. I recognize that the scope of your review is limited to constitutional and court-related implications and to claims against the United States.

I take this opportunity, however, to advise the Committee that, as a member of the Subcommittee on Defense Appropriations,

I have asked the Department of Defense to provide a report on the practical effects of the enactment of S. 1134 and S. 1562 on the defense procurement process. In particular I have asked for a report on the actual number of statements covered by the legislation made daily to agencies operating under budget function 050. I suspect this number will be enormous and that guarding against liability under these proposals could so greatly increase the cost of doing business with the government that many small businesses will drop from competition and that procurement costs generally will increase.

I mention this report because I am sure members of the Committee will have an interest in it, even though it would not be strictly within the subject matter before you. I have already received some of the information I am seeking and will transmit it to the Committee after the facts have been fully developed.

Mr. Chairman, again thank you very much, and I look forward to the views and advice of the Committee based on the record developed here.

The CHAIRMAN. Senator Hatch.

Senator HATCH. Yes, let me ask a couple of questions, Mr Willard. The Supreme Court, in *Atlas Roofing, Inc.* v. *Occupational Safety and Health Review Commission*, found that in cases involving new public rights created by statute, the seventh amendment does not prohibit Congress from assigning the factfinding function and the initial adjudication to an administrative forum. However, it seems to me we have to examine whether an action for fraud is distinct from procedures found suitable for administrative review. Findings of fraud carry a criminal-like stigma, whether we like it or not, and in fact may be prosecuted through a criminal procedure.

Now, do you see any distinction between a case involving the imposition of civil penalties for employers maintaining unsafe working conditions and a case alleging that an employer defrauded the Federal Government?

Mr. WILLARD. For purposes of the seventh amendment right to trial by jury, Senator Hatch, I do not see a distinction. I think that the allegation that an employer has maintained an unsafe, dangerous workplace also carries with it some kind of a stigma as well.

But we have repeatedly sought to characterize the False Claims Act remedies as being noncriminal and nonpunitive, but rather, remedial in nature. The Supreme Court has agreed with our characterization of these remedies as being remedial and not criminal in nature. That is why we do not think there should be a high burden of proof in these cases. Basically, they are designed to make the Government whole for its losses and not to impose punishment.

When we want to impose punishment, of course, we proceed criminally, as we do in many of these cases. We have no doubt that there should be a right to trial by jury for criminal fraud prosecution. But as to the civil remedy, it is designed to make the Government whole, and we think that under *Atlas Roofing* such a case can be appropriately handled by an administrative tribunal.

Senator HATCH. The Supreme Court in the *Atlas* case held that the seventh amendment does not prohibit Congress from creating new public rights and remedies by statute when it concludes that remedies available in the courts of law are inadequate to cope with any particular problem within Congress' power to regulate.

Now, given that the False Claims Act currently provides for the same remedy for fraud and false claims as that established in this bill, S. 1134, can we say that this action which provides for a jury trial is inadequate?

Mr. WILLARD. I am not sure I quite understand your question, Senator.

Senator HATCH. Well, are we merely replacing an adequate procedure within the False Claims Act with an unneeded administrative procedure? I think maybe that sums it up.

Mr. WILLARD. Senator, in our view, the False Claims Act is itself a statutory remedy which was unknown to the common law that existed at the time of the seventh amendment. So for that reason, what we are providing here is an alternative to what was a statutory remedy, rather than a common law remedy. It would be different if we tried to provide an administrative tribunal to handle an

action which was known to the common law at the time the seventh amendment was adopted.

Senator HATCH. OK. I am concerned that this administrative procedure places the accused at a disadvantage when compared to the protections afforded him during a normal civil trial in this country.

For example, under this bill the accused has a right to discovery only to "the extent that the hearing examiner determines that such discovery is necessary for the expeditious, fair and reasonable consideration of the issues." Under this expeditious hearing standard, the accused could be denied the right to obtain copies of transcripts taken pursuant to the testimonial subpoena of witnesses or to documents which are subpoenaed. If you could, would you explain the due process protections afforded the accused within this administrative procedure, and do they solve that concern of mine?

Mr. WILLARD. Well, Senator, let me start first by saying that there is obviously a difference in procedural rights of a trial by jury under the False Claims Act and the administrative proceeding here. That is, of course, part of the idea behind the bills; to provide a form of, if you will, alternative dispute resolutions to handle these smaller cases more efficiently and cheaply for all concerned. If you were to make the procedural rights in the administrative proceeding identical to those in the District Court proceeding, then you would be defeating the major purpose of this legislation, which is to provide a quicker, faster alternative dispute resolution mechanism for the smaller cases.

We do believe, though, that the level of procedural rights provided in the administrative proceeding are adequate. In fact, it is unusual to have any kind of discovery rights in administrative proceedings. The APA does not normally grant a right to any discovery. This act, as we understand it, would create limited discovery right and, while it is not as full as under the Federal Rules of Civil Procedure, it is actually more generous than is normally the case in administrative proceedings.

Senator HATCH. Let me just ask one other question, and that is under S. 1134, the agency's inspector general may compel personal appearance and testimony without even notifying the subject of the subpoena or the nature of the questioning itself or even the purpose for the investigation. So the person subpoenaed is not even given notice that he may be accused of any particular wrongdoing. Now, do you not think that this lacks a procedural due process protection?

Mr. WILLARD. Senator, first of all, as I mentioned in my opening statement, the administration did not initially propose giving testimonial subpoena power to inspectors general. We do not think it is really necessary. The FBI does not have a testimonial subpoena power as a general matter.

But if such a right is granted, we think that it can be exercised subject to the control of the Attorney General in a way that will allow it to operate fairly. I think that the question about what kind of notice to provide and so forth is better handled through administrative guidelines promulgated by the Attorney General, rather than to have the legislation try to lock in an unnecessary level of procedural detail. That is why I think that the question you have raised about the fair way to provide notice is one that ought to be

considered, but we think would be better handled under guidelines from the Attorney General, rather than trying to write all of the detailed rules into the legislation. Although, once again, we would be happy to work with the committee if you want to try to do that.

Senator HATCH. I have other questions, but I think I will submit them in writing. I appreciate your responses.

[The prepared questions of Senator Hatch follow:]

United States Senate

COMMITTEE ON THE JUDICIARY
WASHINGTON, DC 20510

July 3, 1986

The Honorable Richard Willard
Assistant Attorney General
Civil Division
Department of Justice
10th and Constitution Ave., N.W.
Washington, D.C. 20201

Dear Richard:

As indicated in the Commiteee's hearing on June 17, 1986, concerning S. 1134, false claims and fraud legislation, I would appreciate your written responses to the attached question. Please return your answers to the Committee in 212 Senate Dirksen Office Building, Washington, D.C. 20510 not later than the close of business on July 15, 1986 . If your have any questions please contact Jean Leavitt at (202) 224-8191.

QUESTION: As you know, the courts today are split among three different views of the appropriate standard of knowledge or intent for fraud actions, varying from a "constructive knowledge" test, adopted only by the eighth circuit, to actual knowledge with specific intent to defraud the United States, a position held by the fifth and ninth circuits. The majority of circuits rejected both of these positions and have adopted the view that proof of actual knowledge is required but specific intent to defraud the United States is not. I have concerns that both S. 1134 and S. 1562, contain a very liberal gross negligence standard. The American Bar Association and others have recommended a definition of knowledge which includes actual knowledge, deliberate ingorance and reckless disregard for the truth. Can you respond to these concerns that a gross negligence standard for a fraud action is inappropriate ?

With kindest regards and best wishes,

Sincerely,

Orrin G. Hatch
Chairman
Subcommitter on the Constitution

U.S. Department of Justice

Office of Legislative and Intergovernmental Affairs

Office of the Assistant Attorney General

Washington, D.C. 20530

29 JUL 1986

Senator Orrin Hatch
Chairman, Constitution Subcommittee
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

This is in response to your letters of June 19 and July 3, 1986 to Assistant Attorney General Richard K. Willard transmitting questions for the record relating to S. 1134 and S. 1562, the two civil fraud bills pending before the Senate. For your convenience, the questions are repeated along with the answers.

Question 1: S. 1134 would create a new administrative mechanism in Title 5 for imposing civil penalties on persons who make false claims and statements to the United States. What remedies currently are available to the Government in such cases, and what would be the interrelationship of the new provisions and the existing remedies?

Response 1: Currently, the government's civil remedies in fraud cases are limited to those causes of action which we may assert in a suit in district court. In such suits, we allege violations of the False Claims Act, 31 U.S.C. 3729, as well as related common law causes of action, such as breach of contract and unjust enrichment.

The only existing administrative remedy for the submission of false claims to the government is that available to the Department of Health and Human Services under the Civil Money Penalty Law, 42 U.S.C. 1320a-7a. That statute is limited to cases of medicare and medicaid fraud.

The administrative remedy of suspension and debarment does not recoup the money which the government lost. Rather, it is an exercise of the government's business judgment, reflecting the decision to avoid contracting in the future with firms and individuals who have a record of committing fraud on the United States.

Enactment of S. 1134, the Program Fraud Civil Remediee Act, would give the government two remedies for the same fraudulent conduct: suit in district court under the False Claims Act or an adminietrative proceeding under S. 1134. The government would utilize only one of these remedies in each case of fraud--we would not bring a civil action to recover damages for the same fraud in two different forums. The Juetice Department, in the course of its review of agency referrale under section 803, would decide which cases the agencies could bring administratively and which cases Justice Department attorneys would bring in district court.

Finally, the government currently has no civil remedy for the knowing submission of a false statement which does not relate to a claim for money. Our remedy is limited to criminal prosecution under 18 U.S.C. 1001, which, given resource constraints, may not be a realistic option in many cases. A simple civil remedy such as that provided under Section 802 (a)(2) of S. 1134 would be a valuable deterrent to many types of government program abuse.

Question 2: Will the administrative proceedings mandated by the proposed legislation be cost effective, in terms of the involvement of the Department of Justice?

Response 2: We believe that the new administrative proceedings authorized by S. 1134 will be a highly coet effective mechanism for prosecuting the emaller fraud cases which may not warrant litigation in the district courts. The Juetice Department would of course have to reviewv cases before authorizing an agency to bring suit, but this would only involve a small fraction of the time which we would spend in litigating a case. Hence, we believe that the proceedings would conetitute a cost-effective mechanism for the resolution of the smaller fraud cases. Certainly, this has been the experience of the Department of Health and Human Services under its statute.

Finally, in your letter of July 3, 1986, you asked about the standard of knowledge in the two bills:

Queetion: As you know, the courts today are split among three different views of the appropriate standard of knowledge or intent for fraud actione, varying from a "constructive knowledge" test, adopted only by the eighth circuit, to actual knowledge with specific intent to defraud the United States, a position held by the fifth and ninth circuits. The majority of circuite rejected both of these positions and have adopted the view that proof of actual knowledge is required but specific intent to defraud the United States is not. I have concerns that both S. 1134 and S. 1562, contain a very liberal gross negligence standard. The American Bar Association and others have

recommsnded a definition of knowledge which includes knowledge, deliberate ignorance and recklese disregard for the truth. Can you respond to these concerns that a gross negligence standard for a fraud action is inappropriate?

Reeponse: Ae you know, it haa always been the view of the Juetice Department that Congress, in crafting a standard of knowledge, should be guided by a few basic principles. First, in a civil fraud case, the government should not have to prove epecific intent to defraud, a requiremsnt that, in our view, ie only appropriate in criminal caees. On the other hand, the government should not be able to establish civil liabiiity under the Act where the false claim is the result of honest mistake or simple negligence. The appropriate etandard of scienter ehould, therefore, be eomewhere between negligence and specific intent. These fundamental principles have, in our view, been shared by all of the participants in the debate on theee two bills. The only iseue has been how best to implement thie ehared conseneue.

The two bills currently contain a variation of a gross negligence standard, defining "knows or has reason to know" as one who has actual knowledge of the fraud or who:

> acts in gross negligence of the duty to make such inquiry as would be reasonable and prudent to conduct under the circumstances to ascertain ths true and accurate basis of the claim or statement.

An alternate formulation, supported by the American Bar Aeeociation, would modify the definition to impoee liability on one who "acts in reckless disregard of the truth or falsity of the claim or statement." In our view, thsre is little if any difference between "gross negligence" and "reckless disregard" as a etandard of scienter. Certainly, the lengthy and elaborate legislative history reflscting the Congressional intent to establish a standard of scienter somewhere between intent and negligencs is of considerably greater significance than this mere change in terminology.

In conclusion, we feel strongly that, in civil fraud prosecutione under the False Claims Act, or the analogous provieione of S. 1134, the government should not have to prove actual knowledge of the fraud in every case. Instsad, where it is clear that the defendant deliberately insulated himself from knowledge of the fraud being committed, the government should be able to impute knowledge in order to establieh liability. The question of whether knowledge may be imputsd to a defendant will, inevitably, depend on the facts of each case. We belisve that a reckless dieregard standard, fully as much ae a grose negligence standard, adequately sets forth ground rulee to guide courts in making this determination.

The Office of Management and Budget advises us that there is no objection to the submission of this report from ths standpoint of the Administration's program.

Sincerely,

John R. Bolton
Assistant Attorney General

The CHAIRMAN. The distinguished Senator from Iowa.

Senator GRASSLEY. Mr. Willard, we have had some indication that people are confused on one aspect of the legislation bringing in the administrative remedy. There is a feeling that there could be double recoveries, one because of administrative remedy, the other because of judicial remedy. Do you see that that is possible?

Mr. WILLARD. I do not think it is possible at all, Senator, and I think the legislative history could certainly be clear to reflect that understanding. We have always felt, and the courts have always held that the Government is entitled to one remedy. That is the burden we have operated under in the past, where we might have multiple remedies under different statutory theories Usually we only got one recovery. In fact, I am not aware of any case where we have had duplicative recoveries awarded to Government.

Senator GRASSLEY. OK. Well, as long as we are making legislative history, I want to make clear that it is not my intent in S. 1562 that there be double recovery.

On another point, and I would like to refer to the House Judiciary Committee's action on recently marking up H.R. 4827, and that also amends the False Claims Act, that bill as amended would allow the fraud actions to be delayed until the final resolution of claims filed under the Contract Disputes Act. I would like to know what you think the effect of that provision might be.

Mr. WILLARD. I think that provision would be a big step backward in the Government's ability to pursue civil fraud, because that would impose a new limitation on our ability to pursue civil fraud claims that is not now in existence. It would allow the subjects of civil fraud actions to delay the initiation of legal action against them by invoking the Contract Disputes Act mechanism.

Senator GRASSLEY. It sounds like it would just about gut the bill.

Mr. WILLARD. Well, I think it would impose a severe detriment on the Governmedt's ability to use the legislation and for that reason we are very concerned about that provision. Certainly, we would encourage the Senate not to do likewise.

Senator GRASSLEY. OK. Now, my last point would be in regard to the number of fraud deferrals. I think 2,700 each year that your division receives, and yet the number of complaints filed is only around 35, and the number of settlements or judgments is right around 50. Are some of those many cases not brought, would those be cases that would involve smaller dollar amounts and the Department might find it not cost-effective to pursue them?

Mr. WILLARD. That is certainly true, Senator, and that is one of the major reasons we support the creation of an administrative remedy. Basically, our job is to try to get the most money for the taxpayers as we can under these programs and we have to focus our resources, which are of course limited, on the cases that we think will have the biggest dollar payoff. It is not possible for us to go after some of the smaller cases and that is why I think this administrative remedy would be very helpful.

Senator GRASSLEY. So then that would cause a large share of those from slipping through the cracks?

Mr. WILLARD. That is correct, Senator.

Senator GRASSLEY. Mr. Chairman, that is all the questioning I have of Mr. Willard.

The CHAIRMAN. Thank you very much.

Thank you, Mr. Willard, for your presence and your testimony.

Senator GRASSLEY. Mr. Chairman, I do have an opening statement that I want to give?

The CHAIRMAN. A what?

Senator GRASSLEY. An opening statement that I want to give.

The CHAIRMAN. Without objection, that will be placed in the record.

Senator GRASSLEY. I want to read it.

The CHAIRMAN. Do you mind letting us take Senator Cohen so he can get back?

Senator GRASSLEY. No, if Senator Cohen has got a very busy schedule, I do not have to be any place for 20 minutes, I will wait.

The CHAIRMAN. Senator Cohen, we are very glad to have you with us. I believe you have a reputation of being one of the most articulate Members of the Senate and it is an honor to have you here.

Senator COHEN. Well, I am about to disprove that, Mr. Chairman.

The CHAIRMAN. I want to say in the beginning that a few years ago we had a housing bill that attempted to fine people without a trial by jury and I strongly opposed it. I am a great believer in trial by jury. I think a lot of you personally, but you have to do a lot of convincing to get me to go along with fining people without a trial by jury, and I wanted to make that statement to start with.

Senator COHEN. I am going to make my very best effort, Mr. Chairman.

I would like to say at the beginning that Senator Levin, as you know, Mr. Chairman, we are in the course of a markup on the defense bill and Senator Levin is now actively engaged in debate over there and I am going to offer his statement for the record.

The CHAIRMAN. Without objection, we will put the entire statement in the record.

[The prepared statement of Senator Levin follows:]

STATEMENT OF SENATOR CARL LEVIN

BEFORE THE

SENATE JUDICIARY SUBCOMMITTEE ON THE CONSTITUTION

Mr. Chairman, it is a privilege to follow so able a Senator and so comprehensive and thoughtful a statement of the issues. Senator Cohen has worked long and hard on the Program Fraud Civil Remedies Act, and it's been rather thankless work. When enacted, it will save the federal government and, therefore, the U.S. taxpayers tens of millions of dollars. But that kind of reward gets lost in the nitty-gritty, day-to-day details of getting a technical bill like this passed. Senator Cohen has been willing to commit the time and resources required to do the job, and for that thoroughness and commitment, he deserves our respect and praise.

I understand the basis for this Committee's interest in the Program Fraud bill, because it is, to a large extent, an administrative reincarnation of the False Claims Act. The False Claims Act falls within the jurisdiction of this Committee, and in fact, the bill strengthening that Act has been reported by this committee to the full Senate for floor consideration. I am pleased that you have taken that action, since I am a cosponsor of that bill, too. But I am somewhat perplexed by recently stated concerns over the constitutionality of S. 1134. I am perplexed, because I find it difficult to understand just what in this bill could be constitutionally suspect.

The Program Fraud bill provides an elaborate administrative process for the civil recovery of monies fraudulently obtained from the federal government. It is a civil statute, not a criminal statute. It requires

a knowing misrepresentation for liablity and not just negligence or inadvertence. It provides for an administrative hearing before an impartial hearing examiner, who is required to be, in fact, an independent administrative law judge. It contains numerous checks to guarantee procedural fairness on the outcome of the administrative process and the preceding investigation. It allows for federal court review of the final agency action.

Mr. Chairman, I don't know of anything more that the Constitution requires in this situation. In fact, the Constitution would probably be satisfied with less. And that opinion is held not only by Senator Cohen and me, but by well-respected members of the legal community. To quote again from Professor Harold Bruff of the University of Texas Law School:

> "The outcome is a bill that provides substantially (emphasis added) more protection to the interests of affected individuals and firms than due process minima would require."

And he concludes his discussion of S. 1134 by saying:

> "In sum, from the standpoint of the constitutional and administrative lawyer, I think this is not only an acceptable bill, but a good one. I hope that Congress will enact it, so that small frauds against us all will no longer go unredressed."

In drafting this bill, the cosponsors have worked very hard to be extremely fair to the persons who may be subject to this statute. Its passage would allow

us to also be fair to the American taxpayer and the legitimate participants in federal programs.

No one should expect to get away with defrauding the federal government, no matter how small the amount involved. Corruption of any kind undermines the public's support for the victimized programs and unfairly jeopardizes those in a program who follow the rules. Corruption in defense contracting hurts the honest contractor; corruption in food stamps hurts the hungry; corruption in housing programs hurts the homeless.

The Program Fraud Bill will allow us to go after fraud cases under $100,000 in a manner less costly and therefore far more likely to be used than a full-blown case in federal district court. By so doing, it will provide better protection for the integrity of our programs and the expenditure of our taxpayer dollars.

A 1981 GAO report on fraud in federal programs identifies a sorry state of affairs that demand an immediate remedy. From a review of 77,000 fraud cases, GAO found that of those referred to the Justice Department, more that 60% were not criminally or civilly prosecuted. In more than 60% of the already identified cases of fraud, the federal government simply walked away from its losses.

I am here with Senator Cohen today to demonstrate my support for quick passage of this legislation. I appreciate the opportunity to deliver my comments on this important bill. Thank you.

STATEMENT OF HON. WILLIAM S. COHEN, A U.S. SENATOR FROM THE STATE OF MAINE

Senator COHEN. Mr. Chairman, I will try to be as brief as possible to articulate the objectives of the bill and to respond to some of the questions that you may have.

As you know, there are 14 other Senators who have cosponsored this legislation, along with Senator Levin and myself. I think it is important to emphasize at the outset of my testimony that we would not create a new category of offenses through this legislation. This is not something new.

It simply establishes an administrative alternative, patterned largely after the civil False Claims Act, that would capture the conduct already prohibited by current law. So, in other words, we are establishing a new remedy for old wrongs. This is not something new that we are doing under the law, Mr. Chairman.

I think you have already heard testimony to the effect that the imputus for this legislation is that a lot of money is currently being lost—falling through the cracks as Senator Grassley has just articulated—by the tens if not hundreds of millions of dollars because of the fact that the Justice Department does not have the resources to litigate cases under $100,000. It simply costs more money to prosecute those cases than they can possibly recover. For that reason, they are not prosecuting the cases which prompts the need for an administrative-type remedy as provided in my legislation.

So we came up with a solution that I believe is both effective and fair. The Program Fraud Civil Remedies Act marks the culmination of our effort to try and balance the needs of the Government to collect money that currently is being lost with the need to protect the individuals who might be subject to these procedures.

This bill is strongly supported by the major players in the fight against fraud. The Justice Department, for one, strongly supports the bill, and I know, Mr. Chairman, the Justice Department would not be in favor as strongly as they are if the bill was going to deprive individuals of their rights to a jury trial, as you suggested.

The General Accounting Office favors the measure. The inspectors general, the Administrative Conference of the United States, the Federal Bar Association, and last the Packard Commission came out with a recommendation urging adoption of this kind of procedure.

All of those organizations, it seems to me, lend fairly heavy support to the need for this type of procedure. First, it would allow the Government to recover money that it is currently losing; second, it is going to provide for a much more expeditious and less expensive procedure to recoup those losses, and, third, it is going to provide a deterrent against future fraud by dispelling the perception that these small dollar cases are simply going to be let go with impunity.

An additional benefit, Mr. Chairman, is that we know it can work. Under the Civil Monetary Penalties Law, the Department of Health and Human Services is authorized to impose penalties and assessments administratively against health care providers who knowingly or have reason to submit claims for services never provided. Since we implemented this particular law, the Department

of Health and Human Services has been able to recover some $22 million from over 175 cases. So we already have a procedure on the books, which Health and Human Services is already implementing, recovering millions of dollars in these types of cases.

In the interest of time, Mr. Chairman, I would like to address some of the issues of interest to this committee; namely, the constitutionality and the adequacy of due process protections under S. 1134.

Now, in preparation for the hearing, I asked a number of distinguished legal scholars for their opinions on the legislation. They were unanimous in their view that the bill easily passes constitutional muster. We have Prof. Harold Bruff, of the University of Texas, who said that "no serious constitutional question attends this bill."

We have the American Law Division of the Congressional Research Service who echoed Mr. Bruff's conclusion, saying "the program fraud bill does not raise constitutional issues." The Justice Department, in addition to these scholars, has rejected the argument raised by opponents of the bill that establishing an administrative remedy for small frauds violates the seventh amendment right to a jury trial.

In 1977, the Supreme Court unanimously rejected the constitutional challenge in the *Atlas Roofing* case, which was cited by Senator Hatch, upholding a civil penalty scheme with the same essential features that we have in this legislation.

There was another constitutional challenge which I find even less convincing, and that is the contention that this bill thoroughly strips the Court of jurisdictional authority. This simply is not the case.

As Joseph Kennedy, who is chairman of the Committee of Administrative Judiciary of the Federal Bar Association, has stated:

> The fact that the administrative remedy is subject to oversight by Article III courts under the provision for judicial review insures the constitutionality of this measure, for it has long been recognized that so long as the essential attributes of judicial review such as review of the agency's findings and enforcement of agency orders remain in Article III courts, there is no constitutional impediment to the power of Congress to vest initial adjudication of such rights in Article I courts and administrative agencies.

So what he is saying essentially is as long as there is a right of review which would be in the Court of Appeals, there is no denial of due process under the Constitution in proceeding initially administratively.

Furthermore, nothing in the bill precludes the Justice Department from litigating in Federal court any false claim or false statement, whether it involves $99,000 or $2.

Now, there are a few critics who characterize this bill as a court-stripping bill, and they point to the Supreme Court's decision in *Northern Pipeline Construction* v. *Marathon Pipeline* for their support. I would like to take just a moment to tell you why that is not a valid point.

In the *Marathon* decision, the Court held unconstitutional the provisions of the Bankruptcy Reform Act with which I know you, Mr. Chairman, are familiar. In 1978, when we passed that law, they granted to bankruptcy judges, who are article I judges, juris-

diction over all civil proceedings arising under the Bankruptcy Act of the United States.

The Supreme Court held that suits involving private rights—in this case, breach of contract—are solely within the jurisdiction of article III courts, and so they struck that down by trying to confer article III powers on article I judges. That, however, dealt with private rights.

In this particular case, we establish an administrative remedy to deal with public rights; that is, suits between the Government and others.

I would like to include in the hearing record, Mr. Chairman, a copy of the Justice Department's testimony before the Government Affairs Subcommittee as well as other documents in support of the bill's constitutionality.

[The material referred to follows:]

STATEMENT

OF

RICHARD K. WILLARD
ACTING ASSISTANT ATTORNEY GENERAL
CIVIL DIVISION
DEPARTMENT OF JUSTICE

It is e pleasure to appear before the Subcommittee to present the Administration's views on S. 1134, the Program Fraud Civil Penalties Act, a bill to provide for en administrative remedy for false and fraudulent claims submitted to the government. We strongly support this legislation, Mr. Chairman, and want to compliment you and Senator Roth for your leadership in this area. I should stress at the outset that the Administration fully shares Congress's concern about false claims and statements made to the government. In order to strengthen our remedies against such wrongdoers, the Administration will soon send to Congress the "Fraud Enforcement Act of 1985," a major legislative initiative to reinforce our anti-fraud efforts. We look forward to working with the Committee on this proposal, as well es S. 1134.

I.

Before turning to the provieions of your bill, Mr. Chairman, I would like to place this legislation into context by reviewing the Justice Department's role in the investigation and prosecution of false and fraudulent claims. The need for S. 1134 becomes epparent when seen in relation to the Juetice Department's large and growing responsibilities for the prosecution of complex, white-collar fraud cases. It is critical that we be able to delegate the smaller civil fraud cases to departments and agencies if we are to meet our other obligetions.

In the last fiscal year, the thirty attorneys in the fraud section of the Civil Division obtained judgments and settlements in excess of $60 million, a significant improvement over prior years. We have 853 cases currently pending in the Civil Division and our recoveries average in the neighborhood of $1 million for each case which we deem to warrant civil action. Additional hundreds of False Claims Act cases are delegated to the United States Attorneys' offices each year.

As you know, Mr. Chairman, the United States has both civil and criminal remedies which it may pursue in prosecuting fraud. While we should never neglect the potential for criminal sanctions, especially in particularly egregious cases, civil sanctions can be equally powerful. As a general rule, our civil fraud prosecution effort is only as good as the criminal and administrative investigations on which nearly all civil fraud cases are based. FBI reports are one major source of leads. However, in recent years, the Inspectors General have provided a growing share of our civil fraud referrals.

The various civil remedies available to us provide a substantial deterrent to the submission of false and fraudulent claims. Because of the double-damages remedy in the False Claims Act, the government can often recover substantial sums in such prosecutions. Finally, because it requires a lower burden of proof, a civil action may be a more realistic course in close cases.

A diligent and tenacious anti-fraud effort serves to reinforce public confidence in the integrity and efficiency of government programs. At a recent speech in Boston, the Attorney General reiterated the need to aggressively prosecute white-collar crime. He noted that fraud committed against the United States, particularly fraud in defense procurement, has and will continue to receive high priority by the Department.

With that as background, Mr. Chairman, I will now turn my attention to S. 1134.

II.

S. 1134, like S. 1566, the predecessor bill introduced in the last Congress, would establish an administrative forum to prosecute the submission of false claims and false statements to the United States. We believe that a mechanism for resolution of many fraud matters through administrative proceedings is long overdue. Many of the government's false claims and false statement cases involve relatively small amounts of money compared to matters normally subject to litigation. In these cases, recourse in the federal courts may be economically unfeasible because both the actual dollar loss to the government and the potential recovery in a civil suit may be exceeded by the government's cost of litigation. Moreover, the large volume of such small fraud cases which could be brought would impose an unnecessary burden on the dockets of the federal courts.

Several cases illustrate the types of matters for which these administrative proceedings are best suited.

> --In the first case, we brought a False Claims Act suit against several real estate brokers and a mortgage company for fraudulently inducing the Veterans Administration to guarantee three mortgage loans. The VA sustained damages of $13,100 on the three loans. While we ultimately recovered well in excess of that amount under the False Claims Act, the congested nature of the district court's docket meant that the litigation took over six years to conclude.
>
> --Numerous matters are referred to the Department involving, for example, FHA-insured home improvement loans obtained through fraud, social security or CHAMPUS benefits obtained through misrepresentations regarding eligibility, or fraudulent overcharges on small contracts in which traditional civil and criminal litigation are simply impracticable because of the size of the government's claims and the large number of such cases.

Administrative resolution of such small cases will, in our view, address this problem by establishing an expeditious and inexpensive method of resolving them. At the same time, administrative resolution of smaller cases would permit a more efficient allocation of the resources of the Department of

Justice, thus enhencing the Administration'a efforts to control program fraud.

Fortunetely, legisletive efforts in this eree can be guided by the experience of the Department of Health end Humen Ssrvices under the Civil Money Penalty Law, 42 U.S.C. 1320a-7a, a similar administrative money penalty statute which has been in effect for several yeers. Under that law, HHS has recovered over $15 million in fraudulent overcharges under the medicare and medicaid programs. Inspector General Kusserow and the entire Department ere to be commended for their efforts. HHS'a successful experience testifies to the great aevings which could be echieved if this authority were extended government-wide.

A particulerly important isaue posed by this legislation is the element of scienter necessary to prove e violation. Section 802 does not require the imposition of civil penalties simply beceuse a claim or statement is false. As subsection (a) provides, a false claim or statement must be knowingly made, or knowingly caused to be made, before liability attaches. This element of scienter -- in this context, knowledge of the falsity of the claim or statement -- is central to the liability-defining provisions of section 802. It hes long found expression in the False Claims Act, and insures that the bill will not punish contractors who have honest disputes with the government. Under the bill, just as under the False Cleima Act, a contractor who, through negligence or misinformation, submits erroneous dete to the United Stetee, would not be aubject to liability. However, a contractor who submits erroneous data would be lieble if hs knew, or had reason to know, that it was erroneous when he submitted it.

We believe that these well-developed scienter concepts in section 802 fully protect honest contractors. The False Claims Act, upon which section 802 draws, has been in place since 1863, and we are uneware of eny case under the Act in which a contractor has been punished for en honest dispute with the

government. We accordingly aee no need to engraft upon the axisting acianter atandard in section 802 another requirement that a knowingly false claim must be accompanied by an intent to defraud. In our experience, intent requirements in tha civil area lsad to confusion snd impose an overly-stringent burden upon the government. The Falsa Claims Act is not generally interpreted to require a showing of intent, sea, e.g., United States v. Cooperative Grain & Supply Co., 476 F.2d 47 (8th Cir. 1973), and we do not believe that such an intent requirement should be imposed here.

We balieve that the administrstive proceedings outlined in section 803 preserve full due proceaa rights, including the rights to notice, crose examination, representation by counsel and determinstion by sn impartial hearing officer, and thus will withatsnd constitutional challenge. Ths uae of a hesring examinar, or Administrativs Law Judge, to compile a factusl record and mske an initial determination is a common, legslly unobjectionable method to administer federal progrems. Critics of the uee of hearing axaminsrs cen point to no legal pracedent questioning this administrative hearing machanism, and, in fact, it has consietently been uphald sgainst court challenge. See, Butz v. Economou, 438 U.S. 478, 513-4 (1978); NLRB v. Permensnt Lebel Corp., 687 F.2d 512, 527, (Aldisert, C.J., concurring).

Criticism of the hearing exsminer's auppoaed lack of independence convaniently ignorea thesa well eatabliahed precedents as well as saveral protections built into S. 1134. While the hearing examiner would be an employee of the agency, section 803(f)(2)(C) of tha bill assures the hearing examiner an appropriate level of independence by providing that he shall not be aubject to the supervision of the investigating or reviewing official, and could not have secret communications with auch officiels. The bill thus incorporatea the generally acceptad protections required by the Administrative Proceduraa Act. And,

of course, any adjudication of liability under this bill would be subject to independent review in the Court of Appeals by an Article III judge.

In light of the Supreme Court's holding in Atlas Roofing Co. v. Occupational Safety and Health Administration, 430 U.S. 442 (1977), we do not believe that these proceedings would violate the Seventh Amendment's guarantee of trial by jury. In Atlas Roofing, the Court rejected a Seventh Amendment challenge to the administrative penalty provisions of the Occupational Safety and Health Act of 1970 because it concluded that Congress had created new rights which did not exist at common law when the Amendment was adopted. The Court held that:

> when Congress creates new statutory "public rights," it may assign their adjudication to an administrative agency with which a jury trial would be incompatible, without violating the Seventh Amendment's injunction that jury trial is to be "preserved" in "suits at common law".

430 U.S. at 455. The rights created here are not co-extensive with any common law cause of action known when the Seventh Amendment was adopted. In addition, we believe that this statute may, like the False Claims Act, be characterized as a "remedial" statute imposing a "civil sanction". See United States ex rel. Marcus v. Hess, 317 U.S. 537 (1943). Given these considerations, the administrative proceedings do not deny unconstitutionally trial by jury.

With respect to this last point, I note that some have suggested that because S. 1134 provides for double damages, it can no longer be viewed as "remedial" and, instead, must be classified as "punitive", presumably requiring a criminal standard of intent and burden of proof. However, this analysis of the bill is overly-simplistic and does not comport with traditional practice and applicable precedent, including several decisions of the Supreme Court.

Double damages serve an appropriate remedial purpose in several respects. Because of the deceptive and concealed nature

of fraud, the government will rerely be able to prove the entiraty of ite loss. Thus, by establishing a form of "liquideted damagea," this provision insures thet the government will be made whole. Second, the double-damagee provieion partially compensatea the government for its costs of investigation and prosecution. Finally, this provision hae a socially useful detarrent effect.

In 1943, the Supreme Court wes callad upon to decide just this issue relative to e nearly identical provision in the Felae Claims Act. The Court unequivocally ruled that the double damage provision of that Act wae a permissible statutory enactment, civil and remedial in nature and consistent with other statutes, such as the treble damage provisions of the civil antitrust laws. Writing for the Court, Justice Bleck stated:

> We cannot say that the remedy now before us requiring payment of a lump sum end double damages will do more than efford the government complete indemnity for tha injuries done it. *** Quite aside from its interest es preserver of the paace, the government when spending its money has the same interest in protecting itself from fraudulent practices as it has in protecting any citizen from the frauds which may be practiced upon him.

U.S. ax. rel. Marcus v. Hess, 317 U.S. 537, 549-50 (1943). See also, Day v. Woodworth, 54 U.S. (13 Howard) 361, 371 (18561); Missouri Pecific Railway Co. v. Humes, 115 U.S. 512, 523 (1885).

Finally, questions were raiaed in the last Congraee ae to the effect which a finding of liability under thia Act would have on a eubsequent administrative proceeding to euepend or debar a contractor. In the past, such an emendment haa been proposad with the stated objective of preventing the uaa of a civil penalty judgment in debarment or euepeneion proceedinga. We believe that emending the bill to deny any avidentiery valua to e civil penalty judgment in any adminietrative, civil or

criminal proceeding is wholly inappropriate. The civil penalty proceedings envisioned by the bill will afford a full measure of due process protections, as well as the opportunity for judicial review of the proceedings. In view of this considaration, we believe that there is no justification for disturbing the normal rules of rea judicata and collateral estoppel, and requiring another tribunal to go through the costly exercise of retrying the same facts that have already been established under the same standard of proof in a civil penalty proceeding.

In addition, we believe that it is important to note that a contractor would always be free to argue the question of remedy in a suspension or debarment proceeding. According res judicata or collateral estoppel effect to the facts underlying a civil penalty judgment in a later suepension or debarment proceeding would not neceeearily eatablish that suspension or debarment was the appropriate remedy. A contractor would still have the opportunity to argue that he should not be suspended or debarred and that some lesser sanction -- or no sanction at all -- should be imposed.

III.

While we thua endorse many of the eseential provisions of S. 1134, we believe that the bill could be improved along certain linea.

First, we urge the Committee to reconsider the desirability of aection 804(a)(3), which permits Inspectors General snd other investigatory officials to uee compulsory process to obtain testimonial evidence as part of an investigation. Under the existing provisions of the Inspector General Act of 1978, Inspectors General are authorized to compel production of documentary evidence. Neither the Inspectors General, nor the Federal Bureau of Investigation -- the government's principal law enforcement investigatory agency -- currently issue

investigative subpoenas to compel testimony. The potential for the unlimited exercise of testimonial subpoena powers during investigations might raise due process issues as well as interfere with the criminal investigation process. In addition, there would be no central coordinating authority so as to ensure consistency of standards and implementation. In this manner, section 804(a)(3) could adversely affect coordinated law enforcement. The Administration urges that the Committee delete section 804(a)(3) from the bill.

Second, in the civil fraud area, collection of sums owed is often as difficult as winning a judgment itself. Last year's bill, S. 1566, recognized this difficulty and provided the United States with setoff authority to aid in collections, thus clarifying and reinforcing our setoff authority under common law. The government should be authorized to collect judgments obtained under the Program Fraud proceeding by deduction from amounts otherwise owed by the United States. We were disappointed to see that this provision was not included in S. 1134, and would urge the Committee to restore it. Incidentally, under section 2653 of the Deficit Reduction Act of 1984, the United States was given authority to collect debts owed to it (including judgments such as this) from tax refunds.

Third, section 803(f)(2)(F) of the bill provides that if the agency chooses to adopt regulations governing hearings (as opposed to simply following the requirements of the APA), such regulations, in addition to the full due process rights provided by section 803, must provide for a right of discovery, "to the extent that the hearing examiner determines that such discovery is necessary for the expeditious, fair and reasonable consideration of the issues." The right to diacovery is not provided under the APA and is rarely available in administrative hearings. We believe that discovery is inappropriate in administrative proceedings and will unduly delay the process. Opening this streamlined administrative process to the abuses

inherent in civil discovery would defest the purpose of such an alternative dispute resolution mechanism. We do not believe that the right of discovery should be svailable here.

Fourth, becauae it is not our intention to use this administrative mechanism as a substitute for criminal prosecution, we suggest that the bill be amended to clarify that it does not alter existing obligations of agency officials (especially the IGs) to report evidence of criminsl conduct to the Attorney General. The investigating official should report evidence of fraud to the Department of Justice as soon as it comes to his attention, and certainly at the same time that he refers s case to a reviewing official. Consistent with the IGs' existing responsibilities under the 1978 Inspector General Act, this would permit us to determine not only whether the case should be prosecuted civilly under the False Cleims Act, but also whether to bring a criminsl frsud prosecution. Similarly, the reviewing official should not be able to settle a case without informing the Depsrtment of Justice.

Finally, we have some concern about the amount of the penalty which may be assessed under S. 1134. The False Claims Act provides a $2,000 forfeiture (in addition to double damages) for each false claim. We egree that this amount (which has been unchanged since 1863) should be adjusted upward, but believe that s $5,000 forfeiture would be more appropriate than the $10,000 amount contained in the bill.

More seriously, we are uncertain about the scope of the double-damages remedy. The bill provides that a person convicted "shall also be subject to an assessment, in lieu of damages sustained by the United States because of auch claim, of not more than twice the amount of such claim." § 802(a)(1) and (2). This phrase is subject to two interpretations: the damages are equal to either twice the entire amount of the claim, or to twice the amount of the fraudulent portion of the claim. We feel that the latter reading, which is consistent

with judicial interpretations of the government's remedies under the False Claims Act, is the preferred one. Under the jurisdictional section, § 803(c), this Act may be used for any claim where the amount fraudulently requested is less than $100,000. Thus, a claim for a $20-million airplane which includes a fraudulent request in the amount of $5,000 could be adjudicated under S. 1134. While such fraud should be punished, we think that a $40-million, double-damage assessment clearly would be excessive. We believe that the amount of the penalty should also reflect this jurisdictional limit, lest it be used to assess truly disproportionate penalties.

That concludes my prepared statement, and I would be happy to answer any questions.

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April 11, 1986

The Honorable William S. Cohen
United States Senate
Chairman, Subcommittee on Oversight of Government Management
Senate Committee on Governmental Affairs
Washington, D. C. 20510

Dear Senator Cohen:

I am pleased to respond to your request for my views on the constitutionality of S. 1134, the Program Fraud Civil Remedies Act. Perhaps I should preface my remarks by summarizing my qualifications. I have taught courses in administrative and constitutional law for a decade, and have published a number of articles in those fields, as my enclosed resume indicates. I am also one of the authors of a casebook, Robinson, Gellhorn & Bruff, The Administrative Process (West, 3d ed. 1986).

I have reviewed S. 1134 and the ably prepared report of the Committee that accompanies it. No serious constitutional question attends this bill. Indeed, the Committee is to be commended for its effort to respond to concerns voiced by those subject to the bill's processes. The outcome is a bill that provides substantially more protection to the interests of affected individuals and firms than due process minima would require. And that is as it should be-- Congress does well to respond to concerns about fairness in a more sensitive way than can courts that are articulating mandatory constitutional requisites. S. 1134 not only passes due process scrutiny: from a broader policy-based standpoint, it goes as far to protect those charged with fraud as is possible without impairing the Government's efforts to obtain remedies that will protect the public fisc.

S. 1134 employs (or parallels) the Administrative Procedure Act's processes for full-scale adjudication, 5 U.S.C. §§ 554-57, and adds some protections for the respondent. There can be little doubt that APA procedures would themselves satisfy due process criteria. No one has seriously suggested that the APA falls short of due process in situations where, as here, evidentiary hearings are appropriate. Instead, the cases deal with such issues as the propriety of interim deprivations of property while APA hearings are pending, e.g., Mathews v. Eldridge, 414 U.S. 319 (1976). Moreover, S. 1134 goes well beyond the APA in response to the concerns of prospective respondents, for example in its provision for discovery. Thus, the Committee has adapted generally applicable procedures to the special needs of the program fraud context. The Supreme Court has made it clear in the leading Eldridge case that Congressional judgments on such matters are entitled to substantial deference from courts deciding due process challenges. Therefore, if there is a due process infirmity in this bill, it will have to be in something other than its use of APA procedures, modified in ways advantageous to the respondent.

Some special concern has been expressed about the bill's use of a preponderance as the standard of proof. The Supreme

Court has recently held that a preponderance is the generic standard of proof in APA adjudications, and that it is appropriately used in determining whether the antifraud provisions of the securities laws have been violated. Steadman v. SEC, 450 U.S. 91 (1981). That should put the matter to rest in this context.

Nevertheless, related issues of fairness concerning the proof of fraud may arise. In particular, I think use of the preponderance standard is of less importance than substantive requirements for what is required to be proved, procedural guarantees of the independence of the adjudicator, and appellate provision for review of the determination of fraud. I will consider each of these in turn.

First, the bill has been altered to require proof of either actual knowledge of the fraudulence of a claim or gross negligence in not examining the basis of a claim. This is a tough standard of substantive proof; it clearly eliminates simple mistake or ordinary negligence. Given the difficulty of proving knowledge, the Government should bear no higher burden.

Second, guarantees of the independence of an adjudicator are probably more important assurances of fairness than the proliferation of formal process, as the late Judge Friendly observed in "Some Kind Of Hearing," 123 U.Pa.L.Rev. 1267, 1279 (1975). Here, the use of an Administrative Law Judge or someone similarly qualified is an effective guarantee of independence. Moreover, there are two administrative checks on the charging decision, one by the reviewing official within the agency, and the other by the Department of Justice. It is hard to know what more could reasonably be asked.

Third, appellate review of the determination of fraud follows the normal pattern in administrative law. First, review by the agency head provides another administrative check on fairness. Second, judicial review is provided under the normal criteria of the substantial evidence rule. Again, this is the normal maximum set of protections for affected individuals.

Another question that has been raised concerns whether the Seventh Amendment might require a jury trial in the program fraud context. This is, quite simply, not a serious contention. In Atlas Roofing Co. v. Occupational Safety and Health Review Commission, 430 U.S. 442 (1977), the Supreme Court unanimously rejected a Seventh Amendment challenge to a civil penalty scheme with the same essential features as this one. The Court comprehensively reviewed its precedents, which certainly foreshadowed the result in Atlas Roofing, and rejected any requirement for juries in administrative penalty proceedings, using strong language which is quoted in the report of your Committee. One would have to think that the Court did not mean what it said and held in Atlas Roofing and a host of earlier cases to think there is a serious argument for a right to a jury here. In passing, I would note that one reason for the Court's reluctance to extend jury rights into the administrative context is the presence of other controls on the fairness of factfinding, of the sort that S. 1134 contains.

In sum, from the standpoint of the constitutional and administrative lawyer, I think this is not only an acceptable

bill, but a good one. I hope that Congress will enact it, so that small frauds against us all will no longer go unredressed.

Sincerely,

Harold H. Bruff
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RESUME

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Government Service:

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Legal adviser to officers of the Department, the White House, and the Executive Agencies on issues of constitutional and administrative law.

Consultant to the Chairman, President's Commission on the Accident at Three Mile Island, September-October 1979.

Law Teaching:

Arizona State University, Assistant Professor of Law, 1971-73; Associate Professor, 1973-76; Professor, 1977-79.

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Administrative Law; Constitutional Law; Presidential Power Seminar; Regulatory Reform Seminar; Environmental Law; Local Government; Federal Courts; Land Use Planning; Private Real Estate Development; Conflicts of Law; Texas Government; Torts

Publications:

Articles:

Unconstitutional Conditions Upon Public Employment, New Departures in the Protection of First Amendment Rights, 21 Hastings Law Journal 129 (1969).

Arizona's Inferior Courts, 1973 Law and the Social Order 1.

Presidential Exemption from Mandatory Retirement of Members of the Independent Regulatory Commissions, 1976 Duke Law Journal 249.

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Presidential Power and Administrative Rulemaking, 88 Yale Law Journal 451 (1979).

Judicial Review and the President's Statutory Powers, 68 Virginia Law Review 1 (1982).

Legislative Formality, Administrative Rationality, 63 Texas Law Review 207 (1984).

Casebook:

The Administrative Process (with Glen O. Robinson and Ernest Gellhorn) (third ed., 1986).

Work in Progress:

Casebooks:

The Law of Presidential Power (with Peter M. Shane) (draft ed. 1985).

Texas Government (draft ed. 1985).

Article:

On Oversight of the Regulatory Agencies, forthcoming 1986, American Univ. Law Review. (Paper presented at American University Conference, April 4, 1986).

Consulting:

Administrative Conference of the United States, 1975-77. ABA Commission on Law and the Economy, 1977-78.

Testimony:

Committee on Government Operations, U.S. Senate, May 19, 1976.
Subcommittee on the Rules and Organization of the House, Committee on Rules, U.S. House of Representatives, May 3, 1978.
Subcommittee on Administrative Law and Governmental Relations, Committee on the Judiciary, U.S. House of Representatives, December 10, 1979.
Subcommittee on Administrative Law and Governmental Relations, Committee on the Judiciary, U.S. House of Representatives, July 21, 1983.
Committee on Rules, U.S. House of Representatives, March 21, 1984.

Litigation:

Brief amicus curiae for the United States, in Consumer Energy Council of America v. FERC, 673 F.2d 425 (D.C. Cir. 1982) (holding a legislative veto provision unconstitutional), affirmed, 103 S. Ct. 3556 (1983).

April 18, 1986

Honorable William S. Cohen
Chair, Subcommittee on Oversight of Government Management
Committee on Governmental Affairs
U.S. Senate
Washington, DC 20510

Dear Senator Cohen:

This responds to your letter of April 9, 1986, requesting my views of the constitutionality of S. 1134, 99th Cong., 1st Sess. (1985). This is the proposed Program Fraud Civil Remedies Act, which would add a new Chapter 8 to Title 5, U.S. Code. The chapter would provide for an administrative system under which civil monetary penalties could be imposed for false claims and statements to the United States by recipients of property, services, or money from the United States, including parties to government contracts. The bill's objective is to supplement existing provisions for criminal and civil actions brought by the United States for fraud in relationships involving the government. Cf. 31 U.S.C. §3729 and 18 U.S.C. §§ 287 & 1001. As stated in your letter, because of the costs of litigation and the need to make a reasonably efficient use of enforcement resources, "small dollar" cases, defined as those involving a claim of less than $100,000, are often not pursued by the United States. This bill is designed to provide a system of administrative remedies that can be used by agencies to pursue such relatively smaller claims.

Two major constitutional issues have been raised about this bill. First, it has been asked whether the use of an administrative adjudicatory system -- without the apparatus of the common law trial by jury -- would violate the Seventh Amendment's guarantee of a jury trial "[i]n suits at common law, where the value in controversy shall exceed twenty dollars . . . ." A subordinate but related question is whether, even if the Seventh Amendment's protection does not apply here, the Sixth Amendment's guarantee of an impartial jury in "all criminal prosecutions" might pertain, on the theory that the bill's remedies might be deemed penal in nature. Second, it has been asked whether the bill's procedures for adjudicating cases involving alleged false claims to the United States satisfy the requirements of due process.

While I have had only a brief time in which to review the bill, I am happy to provide my reactions and reasons for them. To summarize, I do not believe that the bill has a constitutional deficiency. The law relating to the Seventh Amendment jury trial requirement is quite generous in the leeway granted to Congress in establishing administrative remedies for violations of public duties. This bill seems well within the scope of such Congressional power. Moreover, since this bill expressly provides for civil monetary penalties for false claims made to the United States, I believe that the Seventh, not the Sixth, Amendment contains the pertinent jury trial provision. Furthermore, the bill's provisions for notice, opportunity to be heard, and related protections do appear fully to satisfy the requisites of due process. In this regard, it bears noting that

the bill contains separation of functions provisions analogous to those in the Administrative Procedure Act, 5 U.S.C. §554(d). While not specifically required by due process, such a provision serves the larger aim of fostering impartiality in adjudicative decisionmaking, which is mandated by due process.

Having stated my conclusions first, allow me to summarize the reasoning which has lead me to them.

As to the jury trial issue, it is well established that the Seventh Amendment preserves the right of trial by jury in civil cases as it "existed under the English common law when the amendment was adopted" in 1791. Baltimore & Carolina Line v. Redman, 295 U.S. 654, 657 (1913); see also Atlas Roofing Co. Inc. v. OSHRC, 430 U.S. 444, 449-461 (1977); NLRB v. Jones & Laughlin Steel Corp., 301 U.S. 1 (1937); Parsons v. Bedford, 3 Pet. (28 U.S.) 433, 446-48 (1830). The term "common law" was used in contrast to suits in which equitable rights and remedies alone were acknowledged at the time of the Amendment's framing. See Parsons v. Bedford, supra. The term does not apply to cases arising under the admiralty or maritime jurisdiction, which are tried without a jury, or to cases involving statutory proceedings unknown to the common law. See Glidden Co. v. Zdanok, 370 U.S. 530, 572 (1962); Reconstruction Finance Corp. v. Bankers Trust Co., 318 U.S. 163 (1943); NLRB v. Jones & Laughlin Steel Corp., 301 U.S. 1, 48 (1937).

In the present instance, one might conceivably argue that an action based on an alleged false claim to the United States is in the nature of a contract or tort action, for it might be said to rest on a contractual undertaking or a claim of fraud or misrepresentation, and thus might be assimilated to actions that were known at common law. But this would appear to be an unduly strained contention. It disregards the long line of cases upholding Congress' power to fashion administrative remedies for violations of statutory duties, as here.

Notably, in Atlas Roofing, supra, the Supreme Court held that the Seventh Amendment does not prevent Congress from assigning to the Occupational Safety and Health Review Commission the task of adjudicating workplace safety violations and imposing civil monetary penalties for them. The Court limited its holding to cases involving statutorily created "public rights":

> Our prior cases support administrative factfinding in only those situations involving 'public rights,' e.g., where the Government is involved in its sovereign capacity under an otherwise valid statute creating enforceable public rights. Wholly private tort, contract, and property cases, as well as a vast range of other cases, are not at all implicated. (430 U.S. at 458) (emphasis added)

Surely, if this bill were to become public law, a violation of its provisions would not amount to a "wholly private" case. Rather, it would be grounded ultimately on the statute's definition of a wrong and its provision for civil monetary penalties.

For the sake of argument, we should consider whether there is a material distinction between this bill and the law at issue in Atlas Roofing. One argument might be that the latter created new statutory obligations, whereas, according to the report of the Senate Committee on Governmental Affairs, S.1134 "would not create a new category of offenses" but would "capture only that conduct already prohibited by federal criminal and civil statutes . . . ." S. Rep. No. 212, 99th Cong., 1st Sess. 10 (1985)

(emphasis in original). This argument would seek to draw determinative meaning from the statement in Atlas Roofing that "when Congress creates new statutory 'public rights,' it may assign their adjudication to an administrative agency with which a jury trial would be incompatible . . . ." 430 U.S. at 456 (emphasis added).

However, such an attempt to distinguish Atlas Roofing is unconvincing. First, S.1134 would add a chapter to Title 5, U.S. Code, which contains new language dealing with "false claims and statements" to the United States. Even if a new "category" of offenses may be said not to have been created, a new offense will have been fashioned. Second, in any event Atlas Roofing does not turn on the "newness" of the statutory duty so much as on the facts that the duty and the attendant remedies were statutorily created and not predicated on the common law. The latter characteristics chiefly distinguish an administrative adjudicatory scheme -- such as the one in S.1134 -- from suits triggering a jury trial requirement.

Furthermore, courts repeatedly have reaffirmed the Atlas Roofing principle in subsequent cases involving disparate situations. See, e.g., Keith Fulton & Sons v. New England Teamsters, 762 F.2d 1124, 1132 (1st Cir. 1984); Republic Industries, Inc. v. Teamsters Joint Council, 718 F.2d 628, 642 (4th Cir. 1983) ("Congress may constitutionally enact a statutory remedy, unknown at common law, vesting factfinding in an administrative agency or others without the need for a jury trial"); Mynon v. Hauser, 673 F.2d 994, 1004 (8th Cir. 1982); Williams v. Shipping Corp. of India, 653 F.2d 875 (4th Cir. 1981); Essary v. Chicago & N.W. Transp. Co., 618 F.2d 13 (7th Cir. 1980); McGowan v. Marshall, 604 F.2d 885 (5th Cir. 1979); Buckeye Industries, Inc. v. Secretary of Labor, 587 F.2d 231 (5th Cir. 1979); Rosenthal & Co. v. Bagley, 581 F.2d 1258, 1261 (7th Cir. 1978). Accordingly, there is no reason to doubt Atlas Roofing's continuing vitality in the present circumstances.

With regard to the question about the Sixth Amendment, as sketched above, the short answer is that S.1134 is a civil monetary penalty statute, not a statute calling for a criminal prosecution. As such, the Seventh, not the Sixth, Amendment applies. It also bears noting that the Supreme Court has recognized that civil penalties can assume various forms, and such penalties do not easily lose their "civil" status by straying beyond some rigidly confined notion of such penalties. See United States ex rel. Marcus v. Hess, 317 U.S. 537 (1943); Helvering v. Mitchell, 303 U.S. 391 (1938).

Finally, with regard to the due process issue, an initial distinction should be drawn between the bill's adjudicatory procedures -- which afford a considerable measure of procedural protection to those who allegedly have made false claims to the United States -- and the procedures' actual operation in specific factual settings. The latter, of course, could raise independent due process concerns. Indeed, litigants often urge a due process claim in particularized factual circumstances that may not have been precisely anticipated in terms of a statute's general procedural provisions. Such a concrete contest necessarily lies beyond the scope of these comments.

Focussing on the bill's procedures, it must be said that they establish a rather elaborate set of safeguards. To begin with, the bill requires that any hearing under it must be held "on the record." (§803(e)). Section 803 (f)(2) also specifies a number of procedural requirements for such a hearing. These include written notice to any person alleged to be liable under the bill regarding the time, place, and nature of the hearing;

the legal authority and jurisdiction under which the hearing is to be held; and the matters of fact and law to be asserted by the agency. Also, any such person is to have the opportunity to submit facts, arguments, and offers of settlement or adjustment, and in particular to present a case through oral or documentary evidence, to submit rebuttal evidence, and "to conduct such cross-examination as may be required for a full and true disclosure of the facts." (§803(f)(2)(E)). There is specific provision for the right to counsel. There also is a separation of functions provision that seeks to insulate the hearing examiner from the investigating and reviewing officials. (§803(f)(2)(C) & (D)). In addition, there is a requirement that the hearing examiner not "consult a person or party on a fact in issue, unless on notice and opportunity for all parties to the hearing to participate. . . . ." (§803(f)(2)(C)(i)). And there is a requirement that the hearing officers conduct the hearing "in an impartial manner." (§803(f)(2)(G)). The hearing examiner is to issue a written decision, including findings and determinations in the case (§803(g)). Furthermore, there are provisions for administrative and ultimately judicial review of the hearing examiner's decision. (§§803(h)(2) & 805).

Taken as a whole, these procedures are similar to those of the Administrative Procedure Act for agency adjudications. See 5 U.S.C. §§554 & 556. In general, the procedures seem fully adequate on their face for purposes of due process. See Withrow v. Larkin, 421 U.S. 35 (1975) (discussing the importance of a fair trial without bias by the decisionmaker); cf. Mathews v. Eldridge, 424 U.S. 319 (1976); Perry v. Sindermann, 408 U.S. 593 (1972); Board of Regents v. Roth, 408 U.S. 564 (1972); Goldberg v. Kelly, 397 U.S. 254 (1970). If any particular questions about specific procedural protections -- or, for that matter, another issue -- should arise, I of course would be glad to address them.

I hope that these remarks will be of assistance. Thank you for the opportunity to comment on S.1134.

Sincerely,

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TOS:ajs

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April 16, 1986

Senator William S. Cohen
Chairman
Senate Subcommittee on Oversight
of Government Management
Committee on Governmental Affairs
Senate Hart Office Building, Room 322
Washington, D.C. 20510

Re: S. 1134

Dear Senator Cohen:

The Committee on the Administrative Judiciary is pleased to respond to the concerns expressed over the constitutionality of the administrative remedy for civil fraud found in the proposed Program Fraud Civil Remedies Act.

The report by the Oversight Subcommittee on S. 1134 contains an accurate summary of the state of the law on the constitutionality of an administrative remedy for civil penalties. S. Rep. 99-212, 99th Cong., 1st Sess. 30-34 (1985). Further, an exhaustive review of the writings of the leading authorities in the field of administrative law such as Professors Davis, Gellhorn, Stewart and Schwartz as well as the decisions of the federal courts show support for the assertion that a combination of investigative, prosecutorial and adjudicative functions in a single regulatory agency violates constitutional due process is scant to nonexistent.

Because S. 1134 does not involve a question of enforcing private rights, there is no need to consider whether the enforcement mechanism trenches on the judicial power traditionally and constitutionally vested in the Article III courts. See Northern Pipeline v. Marathon Pipe Line Co., 458 U.S. 50 (1982). Nor is there any question as to the constitutional authority of Congress to create a civil administrative remedy for frauds against the Government. In the language of Atlas Roofing, 430 U.S. 450, S. 1134 is a plain and simple instance in which the "Government sues in its sovereign capacity to enforce public rights created by statutes within the power of Congress to enact."

Since Atlas, the courts have gone even further and held that Congress may constitutionally grant an administrative agency, the Commodities Futures Trading Commission, the power to investigate, prosecute and decide, without a jury trial, the liability of commodity brokers for fines and reparations for frauds committed against private parties, their customers.

The court reasoned that because the "reparations" right was created by a statute that entrusted its enforcement to an administrative agency the case did not involve purely private rights. Myron v. Hauser, 673 F. 2d 994 (8th Cir. 1982). As the Oversight Subcommittee report points out, history and the decisions of the Supreme Court support the proposition that the right to a jury trial turns not only on the nature of the issue to be resolved but also on the forum in which it is to be resolved. S. Rep., supra, 31. Since S. 1134 involves the enforcement of public rights the choice of forum is clearly up to Congress.

With respect to the claim that the combination of functions of investigator, prosecutor and judge in an administrative or executive branch agency raises serious questions about the fairness of the process accorded accused individuals or corporations, we believe the provisions of the APA incorporated in S. 1134 satisfies all the requirements of substantive and procedural due process.

It is, of course, well settled that if administrative adjudicators are not afforded adequate protection against bureaucratic, and therefore political, intrusions into their role, their objectivity and independence will be compromised. Both the APA (5 U.S.C. § 554(d)) and S. 1134 (§ 803(f)(2)(C)(ii)) accomplish this by providing that no hearing officer may "be responsible to or subject to the supervision or direction of any officer, employee or agent engaged in the performance of investigative or prosecuting functions of any agency." This provision is the heart of the separation of functions concept and makes the administrative adjudicatory process constitutionally viable. This provision offers the needed protection against institutional bias and interest which an agency has in enforcing its enabling statute and regulations. Adjudicators will be functionally insulated from ex parte influences and pressures of investigators, prosecutors and, of course, agency heads and their staffs. Further, they may not consult ex parte with "any person or party on any fact in issue" (5 U.S.C. § 554(d)) or with any "interested person" with respect to any issue "relevant to the merits of a proceeding", except as authorized by law. (5 U.S.C. § 557(d)).

As the Supreme Court noted in Butz v. Economou, 438 U.S. 478, 513 (1978), " . . . the process of agency adjudication is currently structured so as to assure that the hearing examiner exercises his independent judgment on the evidence before him, free from pressures by the parties or other officials within the agency."

An instructive view of the dual nature of the independence conferred by the APA on administrative law judges is set forth in an opinion of Attorney General Levi. 43 Op. Attn. Gen. 1 (1977). There General Levi pointed out that the "independence of status of administrative law judges" as distinguished from their "decisional independence" or "independence of action" in hearing and deciding particular cases is set forth in section 11 of the original APA, now codified in Title 5, §§ 1305, 3105, 3344, 4301(2)(E),

5372 and 7521. As to the latter, the Attorney General stated that in the APA Congress intended to confer "decisionmaking autonomy" upon hearing officers in order to attract "high quality officers" and, more importantly, to insure against any possible "unfairness involved in the commingling of adjudicatory and prosecutory functions. See Wong Yang Sung v. McGrath, 339 U.S. 33, 44 (1950)." Id. at 4.

The legislative history of § 556(c) of the APA shows the powers conferred on administrative law judges to ensure their "independent judgment" were "designed to assure that the presiding officer will perform a real function rather than serve merely as a notary or policeman. He would have and should independently exercise all the powers numbered in the subsection. The agency . . . itself should not in effect conduct hearings from behind the scenes where it cannot know the detailed happenings in the hearing room and does not hear or see the private parties." Id. at 5.

The Attorney General then noted that while the "separation of functions" provisions do not technically apply to agency heads, "that does not implicitly sanction intervention by the agency head before the administrative law judge has decided the case; rather it was meant to eliminate what would otherwise be the effect of excluding agency heads from reviewing decisions, or even from supervising presiding officers in formal proceedings with respect to purely administrative matters." Id., n. 4.

We all agree with the proposition laid down in 1610 in Bonham's Case that "no man shall be a judge in his own cause." The difficulty lies in discovering the kind of activity a man must engage in before the cause becomes his own. For example, in NLRB v. Donnelly Garment Co., 330 U.S. 219 (1947) and Pangburn v. CAB, 311 F. 2d 349 (1st Cir. 1962) the courts held that "prior involvement in a particular case" does not disqualify a judge or agency "from subsequently passing on adjudicatory facts." And in Withrow v. Larkin, 421 U.S. 35, 47 (1976); FTC v. Cement Institute, 333 U.S. 683, 700-703 (1948); and Hortonville School District v. Hortonville Ed. Assoc., 426 U.S. 482, 493 (1976), the Supreme Court held that mere familiarity with the facts of a case gained by a tribunal in the performance of its statutory role does not disqualify it as a decisionmaker.

Thinking about the problem of commingling of functions was rather crude in its early stages and is still often crude in the popular polemics. The reason for the unsoundness of any broadside condemnation is that the principle which opposes the combination of functions has to do with individuals, not with large and complex organizations. For an individual to serve as both advocate and judge in a case is obviously improper. But it is not improper even in a criminal case for a large institution, the state, to prosecute through one officer, the prosecuting attorney, and to decide through another, the judge. Even juries function as arms of the state whether acting as grand inquisitors or triers of fact.

The fact that the administrative remedy is subject to oversight by the Article III courts under the provision for judicial review ensures the constitutionality of S. 1134. For it has long been recognized that so long as the essential attributes of judicial power such as review of agency findings and enforcement of agency orders remains in the Article III courts there is no constitutional impediment to the power of Congress to vest initial adjudication of such rights in Article I courts and administrative agencies. Crowell v. Benson, 285 U.S. 22 (1932); Northern Pipeline Co., supra; Kalaris v. Donovan, 697 F. 2d 376, 386 (D.C. Cir. 1983).

In sum, this committee finds the challenges to the constitutionality of the administrative remedy for program fraud created by S. 1134 are lacking in merit.

Respectfully yours,

Joseph D. Kennedy
Chairman
Committee on Administrative Judiciary
D.C. Chapter, Federal Bar Association