NO. 16-0549

IN THE SUPREME COURT OF TEXAS

DR. BEHZAD NAZARI, D.D.S., ET AL.,
Petitioners,

v.

THE STATE OF TEXAS,
Respondent,

v.

XEROX CORPORATION ET AL.,
Respondents.

On Petition for Review from the Third Court of Appeals, Austin, Texas
Cause No. 03-15-00252-CV

BRIEF OF THE PHARMACEUTICAL RESEARCH AND MANUFACTURERS OF AMERICA AS AMICUS CURIAE IN SUPPORT OF PETITIONERS

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January 29, 2018

TABLE OF CONTENTS

Page

INDEX OF AUTHORITIES

Page(s)

CASES

STATUTES

OTHER AUTHORITIES

INTEREST OF AMICUS CURIAE

The Pharmaceutical Research and Manufacturers of America (PhRMA) is a voluntary, nonprofit association representing the Nation's leading research-based pharmaceutical companies.[1] PhRMA's members research and develop innovative medicines, treatments, and vaccines that save, prolong, and improve the quality of the lives of countless individuals around the world every day.

PhRMA members proudly provide these benefits to low-income Texans through the Texas Medicaid program. But the State of Texas has adopted a broad and dangerous interpretation of the Texas Medicaid Fraud Prevention Act (TMFPA), seeking to impose extraordinary financial liability in suits in which the State claims to be exempt from the ordinary rules of litigation. These suits expose companies doing business in the State of Texas to threats of crippling liability.

PhRMA is particularly concerned with the outcome of these suits because the State has relied on its broad reading of the statute to pursue recovery for alleged harm from numerous pharmaceutical companies, including PhRMA members. *See* Jack Meyer & Chris Wolff, *Fighting Medicaid Fraud in Texas*, Taxpayers Against Fraud Educ. Fund 7-9 (March 2013), https://www.taf.org/IMAGES/Texas-Report-3-18-13.pdf (listing recoveries). PhRMA acknowledges that the State—like private litigants—receives protection

[1] A list of PhRMA members is available at http://www.phrma.org/about/members.

from fraud, but when the State sues to recover its damages for alleged fraud, the State must follow the same rules that apply to other litigants and be subject to counterclaims for offset.

No counsel for a party in this case authored this brief in whole or in part. No person or entity—other than amicus, its members, or its counsel—made monetary contributions specifically for the preparation or submission of this brief.

ARGUMENT

I. When the State Sues as an Injured Plaintiff to Recover Damages, the State Waives Immunity to Counterclaims.

This Court holds that "where [a] governmental entity has joined into the litigation process by asserting its own affirmative claims for monetary relief," adverse parties may "assert, as an offset, claims germane to, connected with, and properly defensive to those asserted by the governmental entity." *Reata Constr. Corp. v. City of Dallas*, 197 S.W.3d 371, 376–77 (Tex. 2006). "[I]t would be fundamentally unfair to allow a governmental entity to assert affirmative claims against a party while claiming it had immunity as to the party's claims against it." *Id.* at 375-76.

The rule of *Reata* is grounded, in part, in the principle that "governments who file suit must follow the same rules as the governed." *Id.* at 384 (Brister, J., concurring) (citing *Fristoe v. Blum*, 45 S.W. 998, 999 (Tex. 1898)).

The State argues that its action to recover under Section 36.052(a)(1) of the TMFPA constitutes a suit to "deter and punish civil offenses," which is "rooted in [the] [S]tate's law-enforcement prerogatives." State Br. at 45. According to the State, the Nazari appellant's counterclaims thus "allege state action taken in a different capacity than the capacity in which the State sues here." State Br. at 45. But even if the State is correct that its "capacity" matters to its amenability to counterclaims for offset, the State is wrong about the capacity in which it has sued.

It is true that the State may act as a sovereign, regulating private conduct and imposing civil penalties for violations of its laws, even when the State itself has suffered no injury. For example, the Attorney General and Texas Optometry Board can recover civil penalties from a person that violates the Texas Optometry Act by controlling the professional judgment of an optometrist. *Wal-Mart Stores, Inc. v. Forte*, 497 S.W.3d 460, 462 (Tex. 2016) (discussing Tex. Occ. Code §§ 351.408, 351.603(b)). Similarly, the Attorney General's Consumer Protection Division can seek civil penalties for violations of the Deceptive Trade Practice Act. *See* Tex. Bus. & Com. Code § 17.47(c). When acting as a sovereign and enforcing its laws, the State need not show that it has suffered any injury. The State argues that when it sues in this capacity, it does not become subject to any counterclaims for offset under *Reata*.

But the State does not always file suit as a sovereign enforcing its laws. When the State alleges that it has itself suffered an injury and seeks compensation for its loss, the State must abide by the same rules that apply to other litigants. *Cf. Gabelli v. SEC*, 568 U.S. 442, 450 (2013) (contrasting circumstances when "Government was itself a victim . . . suing to recover its loss" with circumstances when the Government was "bringing an enforcement action for penalties"). This principle has deep roots in Texas law:

> [W]hen a State enters the Courts as a litigant, it must be held subject to the same rules that govern the other litigants[.] . . . When a state

> appears as a party to a suit, she voluntarily casts off the robes of her sovereignty, and stands before the bar of a court of her own creation in the same attitude as an individual litigant; and her rights are determined and fixed by the same principles of law and equity[.]

Wortham v. Walker, 128 S.W.2d 1138, 1145–46 (Tex. 1939) (quotations omitted). And it continues to be acknowledged by this Court: "[W]here the Legislature has given no indication to the contrary the State must abide by the same rules to which private litigants are beholden." *State v. Naylor*, 466 S.W.3d 783, 792 (Tex. 2015).

The State's claim to recover "the amount of any payment . . . as a result of [an] unlawful act" under Section 36.052(a)(1) fits squarely within this framework. Tex. Hum. Res. Code § 36.052(a)(1). The State claims that it has been injured—that it has paid amounts "as a result of" an unlawful act—and seeks an amount that will compensate it for these injuries. Even if the State is correct that its immunity to counterclaims depends upon the capacity in which it has sued, in seeking this recovery, the State has waived its sovereign immunity to counterclaims under *Reata*.

The State notes that a defendant may be liable under the TMFPA even if the State has suffered no injury at all: "[The TMFPA] expressly deems acts 'unlawful' and thus denounces them by their commission alone." State Br. at 45. But merely proving that an act was "unlawful" does not permit the State to recover under Section 36.052(a)(1), which permits the State to recover only by proving "the amount of any payment . . . as a result of the unlawful act."

The State's argument—that the ordinary rules of litigation do not apply to its claims to recover the amounts that it purportedly paid as a result of unlawful acts—has radical consequences. In this case and in *In re Xerox Corporation*, No. 16-0671 (filed Aug. 31, 2016), the State has asserted the same claims against and seeks to recover the same payments from multiple defendants. Nor, in the State's view, would it be limited to recovering the same payment twice if it could identify three (or more) defendants to sue.

The ordinary rules of litigation, with their roots in the common-law, should not be lightly disregarded. Texas disfavors interpretations of statutes that create liabilities unknown to the common law or deprive persons of common law defenses: "[S]hould a statute create a liability unknown to the common law, or deprive a person of a common law right, the statute will be strictly construed in the sense that it will not be extended beyond its plain meaning or applied to cases not clearly within its purview." *B.C. v. Steak N Shake Operations, Inc.*, 512 S.W.3d 276, 283 (Tex. 2017) (quoting *Smith v. Sewell*, 858 S.W.2d 350, 354 (Tex. 1993)).

The prohibition against double recovery has deep roots in Texas and English law. Blackstone notes, "[I]f the party injured accepts a sum of money, or other thing, as a satisfaction, this is a redress of that injury, and entirely takes away the action." 3 William Blackstone, Commentaries *16; *see also Bradshaw v. Baylor*

University, 84 S.W.2d 703, 705 (Tex. 1935) ("There being but one injury, there can, in justice, be but one satisfaction for that injury.").

Indeed, the State's theory affects far more than the amount of its recovery: it limits both what evidence a defendant can discover and what evidence a jury will hear. In effect, the State contends that the TMFPA permits it to isolate a defendant of its choice, permitting the jury to hear evidence only of that defendant's alleged wrongdoing while excluding evidence of any wrongdoing of others or of the State.

Thus, at a trial of this case, the State will seek to place the entire blame for alleged payments on the Dental Group. And in a trial of the related *Xerox* matter, the State will seek to place the entire blame for the same alleged payments on the Xerox defendants. Neither jury will be exposed to the State's inconsistent theories, and neither jury will hear the whole story.

This runs contrary to the purpose of recoupment claims against the government, as identified by the Supreme Court of the United States: "[Recoupment] has never been thought to allow one transaction to be offset against another, but only to permit a transaction which is made the subject of suit by plaintiff to be examined in all its aspects, and judgment to be rendered that does justice in view of the one transaction as a whole." *United States v. Dalm*, 494 U.S. 596, 611 (1990) (quoting *Rothensies v. Electric Storage Battery Co.*, 329 U.S. 296, 299 (1946)). If the State prevails in this appeal and the *Xerox* mandamus

proceeding, then no jury will have the opportunity to render a judgment "that does justice in view of the one transaction as a whole."

The stakes are high. As the State notes, Texas Medicaid is a billion-dollar program, making up a quarter of the State's budget. State Br. at 44. When the State wields the TMFPA against defendants that regularly participate in the Medicaid program, the amounts involved can exceed hundreds of millions of dollars. The potential liability creates extraordinary pressure to settle. Indeed, as of 2013, only one TMFPA case had ever been tried to judgment. *Fighting Medicaid Fraud* at 6. Given the potential exposure of defendants under the TMFPA, correctly measuring the State's recovery—pursuant to principles such as waiver, mitigation, offset, and proportionate responsibility—is particularly important.

The express exemption from Chapter 41 confirms that State's suits under the TMFPA should be subject to the ordinary rules of litigation, including permitting defendants to assert offsetting counterclaims. The Legislature expressly excluded claims under Chapter 36 of the Human Resources Code from Chapter 41 of the Civil Practice and Remedies Code, which applies only to an "action in which a claimant seeks damages relating to a cause of action." Tex. Civ. Prac. & Rem. Code § 41.002(a). Because the State "seeks damages relating to a cause of action" in Section 36.052(a)(1) and would be subject to Chapter 41, the Legislature stated

expressly that Chapter 41 "does not apply to . . . an action brought under Chapter 36, Human Resources Code." Tex. Civ. Prac. & Rem. Code § 41.002(d)(3). If the State were simply immune to the ordinary rules of litigation or did not seek damages, the express exemption from Chapter 41 would be unnecessary.

Significantly, the exemption from Chapter 41 was added in the same bill that modified the State's recovery under Section 36.052(a)(1). Before 2005, recovery under Section 36.052(a)(1) was described as "restitution." S.B. 563, 79th Leg., R.S. (Tex. 2005). The State could recover "restitution of the value of any payment . . . provided under the Medicaid program, directly or indirectly, as a result of the unlawful act[.]" *Id.* The 2005 amendment eliminated the word "restitution" and clarified that the State could recover losses that occurred through "payment[s] made to a third party." *Id.* In the same bill, the Legislature added the exemption from Chapter 41. *Id.*

The House Research Organization's bill analysis confirms that the exemption from Chapter 41 was necessary to prevent Chapter 41 from applying to recovery against "providers committing fraud against the state": "CSSB 563 would exempt acts of Medicaid fraud from the limitations on the award of exemplary damages in the Civil Practice and Remedies Code." House Research Org. Bill Analysis, S.B. 563, 79th Leg., R.S. (2005).

> Supporters Say: . . . The bill would exempt cases involving Medicaid fraud from the caps on exemplary damages in place since HB 4 by

> Nixon was enacted by the 78th Legislature in 2003. Those limits were designed to protect providers and others from excessively high damage awards but not providers committing fraud against the state.

Id. Similarly, Patrick J. O'Connell, while testifying as Chief of the Attorney General's Civil Medicaid Fraud Division to the House Committee on Public Health regarding Senate Bill 563, explained that the exemption from Chapter 41 was necessary for suits against providers accused of committing fraud against the State. Hearing of the House Committee on Public Health at 4:00:10 (April 27, 2005) (discussing the cap on exemplary damages), http://tlchouse.granicus.com/MediaPlayer.php?view_id=23&clip_id=6416.

If the State were correct that its suits under the TMFPA are always filed in its sovereign capacity and not for recovery of "damages," then this exemption from Chapter 41 would be unnecessary. The inference to be drawn from the express exemption is clear: when the State seeks recovery under Section 36.052(a)(1) against providers accused of committing fraud against the State, the State has filed an action seeking damages, which would be subject to Chapter 41 in the absence of the express exemption. The Legislature understood that the State's claims for damages under the TMFPA would be subject to the ordinary rules of litigation.

To the extent that the State is correct that the availability of counterclaims turns on the capacity in which the State has filed suit, State Br. at 20-21, 42-48, the

State has sued as an ordinary plaintiff seeking to recover compensation for its injuries and should be subject to counterclaims for offset under *Reata*.

II. Section 36.052(a)(1) Permits the State to Recover Damages for Its Losses.

The State's argument that it has sued as a sovereign rather than an injured plaintiff is premised, in part, on an incorrect measurement of recovery under Section 36.052(a)(1).

The State argues that the Section 36.052(a)(1) remedy "do[es] not measure any overpayment or unauthorized payment by the State." State Br. at 43.

But the State fails to grapple with the text of the statute. Section 36.052(a)(1) permits the State to recover "the amount of any payment . . . provided under the Medicaid program, directly or indirectly, **as a result** of the unlawful act, including any payment made to a third party." Tex. Hum. Res. Code § 36.052(a)(1) (emphasis added). It is a traditional background principle "that a phrase such as 'results from' imposes a requirement of but-for causation." *Burrage v. United States*, 134 S. Ct. 881, 889 (2014). And but-for causation requires evidence that without the act, "the injury would not have occurred." *Ryder Integrated Logistics, Inc. v. Fayette County*, 453 S.W.3d 922, 929 (Tex. 2015) (quoting *Del Lago Partners, Inc. v. Smith*, 307 S.W.3d 762, 774 (Tex. 2010)).

To recover any amount under Section 36.052(a)(1), the State must thus prove that in the absence of the unlawful act, payment would not have been made. By definition, this recovery measures "overpayment," *i.e.*, payment that was made because of an unlawful act that would not have been made in the absence of an unlawful act. And this overpayment constitutes loss to the Medicaid program from the unlawful act. This measure of recovery is a classic measure of damages.

The State also argues that it can collect the "*entire* amount paid as a result of the violation." State Br. at 37 (emphasis in original). The State relies heavily on a comparison to the federal Social Security Act, but there are key differences in the text of the statutes. The Social Security Act permits an assessment of "not more than three times the **total amount claimed** for each item or service." 42 U.S.C. § 1320a-7a(a) (emphasis added). This phrase permits recovery of the "total amount" of the "amount claimed."

The State's example on page 32 of its brief thus correctly applies the language of the federal statute:

> [I]f a service properly warranting a $2000 payment was falsely claimed as a service warranting a $5000 payment, one might argue that the "damages" or "loss" is $3000, as the difference between the payment made and the allowable payment. But the Social Security Act assessment for this prohibited act would be the full $5000—"the amount claimed" for the service.

State Br. at 32. As the State notes, "this Social Security Act assessment is not an overpayment measure" but is "based on the full amount claimed." State Br. at 32.

But the TMFPA does not permit the State to recover the "total amount claimed" by the defendant. It says nothing about the "amount claimed" and instead focuses on the "result"—the TMFPA permits the State to recover only the "amount of [the] payment" that was "a result of the unlawful act." Applied to the State's example above, if the unlawful act was falsely claiming that the service warranted a $5000 payment, then the "amount of [the] payment" that was "a result of the unlawful act" would be $3000. The "full amount claimed" by the defendant is thus irrelevant under the TMFPA. It is hardly surprising that differences in text lead to different results.

Testimony from the State regarding the 2005 amendment agrees with this reading of the TMFPA. When testifying before the House Committee on Public Health, Patrick J. O'Connell explained that if a provider is "sending us a request for reimbursement for a $100 procedure . . . but in fact it was only $70 . . . all we're going to get is treble the $30 that's different[.]" Hearing of the House Committee on Public Health at 4:00:40 (April 27, 2005), http://tlchouse.granicus.com/MediaPlayer.php?view_id=23&clip_id=6416.

The proper measurement of the "amount of any payment provided . . . as a result of an unlawful act" is particularly important to members of PhRMA. Medicaid recoups approximately 45% of its drug spending from rebates provided by manufacturers. Daniel R. Levinson, *Higher Rebates for Brand-name Drugs*

Results in Lower Costs for Medicaid Compared to Medicare Part D, OFFICE OF GENERAL INSPECTOR, 18 (2011), https://oig.hhs.gov/oei/reports/oei-03-10-00320.pdf. In measuring the amount of payment by the State for a drug, the amount of these rebates must be considered. The actual payment by the State is the initial payment less the rebate received from the manufacturer. This is intuitive—the amount an individual pays for a gallon of milk is not the five dollar bill handed to the clerk; the amount paid is five dollars less the change that the clerk gives back.

In litigation against one of PhRMA's members, the State has argued that rebates cannot be considered in measuring its recovery under Section 36.052(a)(1). That is, the State intends both to recoup the full amount it initially paid for the drugs and to retain the rebates paid by the manufacturer. The State thus seeks to recover more than the amount paid as a result of the alleged unlawful act.

The State's position on the measure of recovery raises grave constitutional concerns. If rebates are disregarded or if the State can recover amounts that it would have paid regardless of the unlawful act, then the State's recovery bears no rational relationship either to the harm suffered by the State or the degree of alleged wrongdoing by the defendant. Such an interpretation should be avoided: "We have accordingly instructed the federal courts to avoid constitutional difficulties by adopting a limiting interpretation if such a construction is fairly

possible." *Skilling v. United States*, 561 U.S. 358, 406 (2010) (internal quotation marks omitted). To avoid these constitutional concerns, this Court need only read the statute in accordance with its plain text: The State may recover only amounts paid because of an unlawful act, not amounts that would have been paid regardless of the unlawful act.

The State does not seriously grapple with the significance of the availability of prejudgment interest on its recovery under Section 36.052(a)(1). Section 36.052(a)(2) permits the State to recover "interest on the amount of the payment . . . described by Subdivision (1) at the prejudgment interest rate . . . for the period from the date the benefit was received or paid to the date that the state recovers the amount." Tex. Hum. Res. Code § 36.052(a)(2).

The State makes only a brief (and circular) response: "[B]ecause the remedy under subsection (a)(2) of § 36.052 is derivative of the subsection (a)(1) remedy, it too is a statutory penalty, not damages." State Br. at 44. But the State fails to address the broader point: the availability of prejudgment interest indicates that the remedy under Section 36.052(a)(1) is compensatory. Prejudgment interest compensates a plaintiff for the lost time-value of its money; it is "compensation allowed by law as additional damages for lost use of the money due as damages during the lapse of time between the accrual of the claim and the date of

judgment." *Cavnar v. Quality Control Parking, Inc.*, 696 S.W.2d 549, 552 (Tex. 1985).

The State contends that Section 36.052(a)(1) simply imposes an arbitrary penalty, unrelated to the State's loss. *See* State Br. at 44 ("[T]he remedy under subsection (a)(1) of TMFPA § 36.052 is a statutory penalty—an award imposed 'for violation of a statute's terms without reference to any actual damages suffered.'" (quoting *Statutory penalty*, Black's Law Dictionary (10th ed. 2014)). But if the State's characterization were correct, then the Legislature would have no reason to provide for prejudgment interest.

The availability of prejudgment interest in Section 36.052(a)(2) confirms that the Section 36.052(a)(1) remedy compensates the State for the loss it suffers through payments as a result of an unlawful act. Because the State has sued as an injured plaintiff seeking to recover its own damages, its claims are subject to the counterclaims for offset.

CONCLUSION & PRAYER FOR RELIEF

This Court should hold that when the State seeks recovery under Section 36.052(a)(1), it sues as an ordinary litigant and waives sovereign immunity to counterclaims for offset under *Reata*. This Court should further clarify that the amount of any payment provided as a result of the unlawful act measures the State's overpayment.

Dated: January 29, 2018

Respectfully submitted,

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