

SIXTH CIRCUIT'S REJECTION OF TAINT DAMAGES THEORY IN FALSE CLAIMS ACT CASE REINFORCES THAT VALUE-RECEIVED MAY SUBSTANTIALLY OFFSET DAMAGES

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Government Enforcement Alert

By: Mark A. Rush, Joseph J Porcello, Joseph J. Porcello, Allison L. Burdette

In False Claims Act ("FCA") cases, the Department of Justice and, where the government has declined to intervene, *qui tam* plaintiffs, routinely pursue aggressive damages theories. In its recent decision in *U.S. ex rel. Wall v. Circle C Construction, LLC*,^[1] the Sixth Circuit provided a stern reminder to the government and *qui tam* plaintiffs that aggressive FCA damages theories, untethered from the facts and which fail to account for value received by the government, are subject to rejection in favor of more disciplined damages calculations. In *Circle C*, the Sixth Circuit scrutinized a district court's \$762,894.54 damages award for a relatively small underpayment of above-market wages under the Davis-Bacon Act, rejected the government's "taint" theory of damages and reversed the district court's award, which was computed based on the full value of the defendant contractor's allegedly tainted electrical work, trebled. The Sixth Circuit remanded and directed the district court to enter an award for the government's actual damages — just \$14,748 — which were less than two percent of the damages initially awarded. The Court cautioned that FCA damages must always be "grounded in reality" and chided the government's creative accounting and "fairyland" damages theory, stating that the proper focus of the damages inquiry is the extent to which the government did or did not receive the benefit of its bargain.

Circle C stands for the proposition that the government and, by extension, *qui tam* plaintiffs, should not obtain windfall damages in FCA cases when the government has received all or most of the benefit of its bargain. Damages should instead be reduced or offset based on the fair market value received by the government.

THE DECISION

Circle C involved a contract it entered into to build warehouses on a U.S. Army base and its subcontractor's failure to pay several electricians the above-market Davis-Bacon wages specified in Circle C's contract with the Army. The parties agreed that the underpayment of the electricians, in the amount of \$9,916, rendered Circle C's weekly statements of Davis-Bacon compliance under the contract false, thus giving rise to Circle C's liability to the government under FCA. The dispute related to damages.

Before the district court (and, later, the Sixth Circuit), the government argued the wage underpayment rendered all of the electrical work on Circle C's warehouse project "valueless" because the work was "tainted" by the failure to pay the required Davis-Bacon electrician wages. Relying on this theory, the district court awarded the government \$762,894.54 in damages (the entire \$259,298.18 the government paid for the electrical work on the Army warehouses, trebled, minus \$15,000 previously paid in settlement by the subcontractor).

On February 4, 2016, the Sixth Circuit issued its opinion rejecting the government's "creative" damages accounting in its FCA claim. The Court declared that the district court's award was based on "fairyland" damages rather than actual damages. Actual damages "are the difference in value between what the government bargained for and what the government received." Since the government received the warehouses for which it had bargained, the government's actual damages were the amount of the wage underpayment. The "taint" was made right by the treble damages available under FCA. The Sixth Circuit distinguished the *Circle C* case from cases where the goods delivered to the government were actually valueless because the goods were dangerous to use (such as helicopters with defective transmissions) or morally tainted (such as uniforms manufactured by child laborers in Indonesia). In those cases, an award equal to the full value of the contract may be appropriate. In contrast, money damages could remedy the wage underpayment in the *Circle C* case "every day."^[2] The Sixth Circuit thus reversed the district court's award and remanded the case with the instruction to enter a judgement of \$14,748, the government's actual damages of \$9,916 tripled according to 31 U.S.C. § 3729(a)(1)(G), minus \$15,000 already paid by the subcontractor in settlement of the underpayment issue. The Sixth Circuit described the revised damages as appropriately reflecting reality.

KEY TAKEAWAYS

The Sixth Circuit's ruling in *Circle C* makes it clear that, when it comes to damages in FCA claims, some courts will closely scrutinize whether the government received the value it bargained for and will base damages awards on that analysis. In cases where the government has received all or most of the benefit of its bargain, the fair market value of the goods or services received may serve to substantially reduce or offset the government's actual damages. This decision may be of particular relevance in false certification FCA actions where the statement certifies compliance with voluminous regulations and where a minor technical violation occurred. A prime example is FCA actions against healthcare providers that seek government payments based on accurate bills for competently provided and medically necessary services but nonetheless fail to comply with one or more technical regulatory requirements. Under such circumstances, *Circle C* may support a substantial offset of claimed damages where the government has received the full value of the services for which it contracted.

The Sixth Circuit's ruling also provides a reminder to FCA defendants of the importance of early case evaluation, with a strategic focus on their damages theory and a realistic assessment of their potential exposure. Although it may be counterintuitive, depending on the nature of the case, FCA defendants, working with their outside counsel, may be best served to focus more closely on damages than liability at the outset to understand what is really at stake.

Notes:

[1] *U.S. ex rel. Wall v. Circle C Constr., LLC*, 813 F.3d 616 (6th Cir. 2016).

[2] *Id.* A concurrence to the Sixth Circuit's opinion sought to clarify that it is not danger or immorality that render goods valueless, thereby making the damages award of the entire contract value appropriate. Instead, the basis of damages rests on "the extent to which the value of the injury to the public interest is calculable in terms of market value." As such, the Sixth Circuit's revised damages award was appropriate because the market value of the wage underpayment could be "precisely ascertained." *Id.* at 619 (Rogers, J., concurring).

KEY CONTACTS



MARK A. RUSH
PARTNER
PITTSBURGH, WASHINGTON DC
+1.412.355.8333
MARK.RUSH@KLGATES.COM

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