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Calculating Damages Under The False Claims Act: Basic Considerations to Review

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The greatest issue in False Claims Act investigations and litigation has long been recognized as the imposition of damages, and how you get there matters. See McDermott, *Qui Tam: An AUSA's Perspective*, 11 False Cl. Act and Qui Tam Q. Rev. 9 (October, 1997). The False Claims Act, 31 U.S.C. § 3729, is a civil statute that is remedial in nature but punitive in design due to treble damages and mandatory minimum penalty provisions. For some industries, like health care, where there is a high volume of low dollar claims or submissions, and evolving theories of liability, the potential for damages can be of constitutional import. Further, under the FCA, mandatory penalties may be imposed even where the government has suffered no damages.

The FCA provides a cause of action against anyone who submits or causes to be submitted a false claim to the government. Persons who violate the Act are liable for treble damages, or three times the actual damages, "which the Government sustains because of the act" giving rise to liability. Defendants found liable are also required to pay a mandatory penalty for each false claim (the current penalty range is between \$5,500 and \$11,000).

In the context of a qui tam, where a private individual initiates a False Claims Act action on behalf of the government, the relator is entitled to a share of the government's recoveries. 31 U.S.C. § 3730. Where the government intervenes, the relator is entitled to at least 15 percent and no more than 25 percent depending on the extent to which the person contributed to the prosecution. Where the government does not intervene and the relator moves forward independently, the relator is entitled to at least 25 percent and no more than 30 percent of the recoveries. Defendants found to have violated the Act are also liable for costs incurred by the relator or government in bringing the action.

The range of conduct that may constitute a violation of the FCA is broad, particularly since the Fraud Enforcement and Recovery Act of 2009 (FERA) significantly expanded the definition of "obligation" and eliminated the presentment requirement, such that a defendant may be liable where the money or property at issue "was to be spent or used on the Government's behalf or to advance a Government program or interest."

Given the scope of conduct that can give rise to FCA liability, it is not surprising that there is no single rule for calculating damages under the Act. The damages must be determined based on the facts of the particular case at issue and identifying and valuing damages can be a murky task. While there is no hard and fast rule, the fundamental guiding principle in calculating damages is to make the government whole for any damages incurred "because of" a violation of the Act. See *United States ex rel. Marcus v. Hess*, 317 U.S. 537, 551-52 (1943); *United States ex rel. Harrison v. Westinghouse Savannah River Co.*, 352 F.3d 908, 922-23 (4th Cir. 2003); *United States ex rel. Longhi v. Lithium Power Technologies*, 530 F. Supp. 2d 888, 890-91 (S.D. Tex 2008). See also S. Rep. No. 614, 96th Cong., 2d Sess. at 4.

The checklist below is designed to aid practitioners in thinking about how to approach FCA damages by identifying significant considerations. The checklist should not (and cannot, in light of the complexity of the question of damages under the FCA) supplant a careful review of the facts of a particular case in light of relevant governing precedent in the jurisdiction where the case is litigated.

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Calculating Base Damages

- Injury: Determine what damages to the government resulted “because of” the defendant's acts.

Comment: The burden is on the government or the relator to prove that the damages sought were caused by the fraud. The defendant will want to be able to distance the alleged damages from the fraudulent acts to the extent possible (such that the damages cannot be said to have been caused by the defendant's acts) in order to minimize its potential financial liability.

- Select an appropriate model for calculating damages based on the facts of your case and the damages identified. Below, we provide examples of categories of conduct that may give rise FCA liability with the corresponding measure of damages one may expect in those types of cases, including case examples. Again, the measure of damages will depend on the particular facts of your case. The chart below is by way of illustration and cannot be considered a hard and fast guide.

Fraudulent Conduct	Typical Measure of Damages and Illustrative Case Law
Delivery of defective/non-conforming goods or services	<p><i>Difference between value of what was received and the value of what should have been delivered (value of goods had there been no fraud).</i> <i>United States v. Borenstein</i>, 423 U.S. 303 (1976) (damages arising out of misrepresentation of quality of electron tubes supplied to the government measured by the difference between the market value of the tubes received and the market value of the tubes of the specified quality). <i>United States v. American Packing Corp</i>, 125 F. Supp. 788 (D. NJ 1954) (damages arising from defendant supplier providing lower quality meat than that specified by contract measured by the difference between the lowest market price for grades of meat of specified quality and the highest market price for the types of meat actually furnished). <i>United States v. Science Applications Intern. Corp.</i>, 626 F. 3d 1257 (D.C. Cir. 2010) (where market value of non-conforming goods or services cannot be ascertained – e.g., where expert advice is provided pursuant to a contract, but there is a conflict of interest, which is prohibited by the contract – damages may be calculated based on the amount the government actually paid, less the value of the goods or services the government received or used).</p> <p><i>Unused portion of goods provided.</i> <i>Faulk v. United States</i>, 198 F.2d 169, 172 (5th Cir. 1952) (upholding quantity of unconsumed milk as the correct measure of damages where application of the usual measure - difference between the value of the commodity delivered and that contracted to be delivered – would have allowed defendant, who had supplied condensed milk instead of fresh milk pursuant to a contract, to profit from the fraud). <i>Henry v. United States</i> (where defendant provided soap not meeting specifications, damages were based on the amount the government paid for the soap, less the value of the goods used).</p>
Failure to provide goods or services bargained for	<p><i>Amount paid for the goods or services not delivered.</i> <i>United States v. American Precision Products Corp.</i>, 115 F. Supp. 823 (D.N.J.1953) (where progress payments were made for work not yet completed, measure of damages was the difference between what the government advanced in reliance on false claims, and what the government would have advanced had the false items not been included on the claims)</p>
Misrepresentations of cost resulting in overcharges	<p><i>Amount charged to government as a result of misrepresentations.</i> <i>United States v. Ehrlich</i>, 643 F.2d 634 (9th Cir. 1981) (reasoning that where excess payments resulted from the falsification of construction costs, “[t]he damages calculation begins...with a determination of the</p>

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	amount by which [defendant] falsely overstated those costs.”)
Bid-rigging/Collusion	<i>Difference between what the government paid and what it would have paid in a competitive environment.</i> <i>Brown v. United States</i> , 207 Ct. Cl. 768, (1975) (damages arising out of collusive bidding for government housing renovation project measured by difference between subcontractors margin of profit and typical margin of profit for industry)
False Certification	<i>Measured by the amount of money paid out by reason of the false claim over and above what it would have paid if claims had been truthful.</i> <i>United States v. Rogan</i> , 459 F. Supp. 2d 692 (N.D. Ill. 2006) (concluding that damages were equal to the value of all claims submitted for services performed by physicians with whom hospital had a prohibited financial relationship under Stark and had violated kickback statute, because had the government known of the prohibited financial relationships and kickbacks, it would have paid nothing for the claims)
Government loans obtained by fraud	<i>Measured by the damages that the government would not have incurred “but for” the fraudulent loan.</i> <i>United States v. Ekelman & Associates, Inc.</i> , 532 F.2d 545 (6th Cir. 1976) (affirming district court holding that “the amount of actual damages sustained by the government was the amount paid upon default to the mortgage holder by the government plus reasonable expenses and maintenance and repair costs incurred by the government in preserving the mortgaged property less credits due the defendants, such as funds realized upon ultimate disposition of the property, rental income derived from the property, and any amount recovered from the veteran-mortgagor by the government”). <i>United States v. Woodbury</i> , 359 F.2d 370 (9th Cir. 1966) (affirming district court ruling that government incurred no damages where the government got what it paid for, but noting that “expense[s] in the form of time and money spent...in straightening out the mess...and in protecting its interests thereafter,” may have been recoverable as damages had the government made an attempt to prove any such damages).
Government grants obtained by fraud	<i>Measured by the full amount of grants awarded to defendants based on false statements.</i> <i>U.S. ex rel. Feldman v. van Gorp</i> , 697 F.3d 78 (2d Cir. 2012) (concluding that where government receives nothing of measurable value because benefit goes to a third party, and government has “entirely” lost the opportunity to award the grant money to someone who would have used it for its intended purposes, the measure of damages is equal to full amount of the grants awarded to defendants because of false statements)
Reverse false claim/Retention of overpayment	<i>Measured by the amount of the overpayment not returned.</i> <i>United States v. Borseau</i> , 531 F.3d 1159 (9th Cir. 2008), <i>cert. denied</i> 129. S. Ct. 1524 (2009) (in context of false claims arising out of misrepresentations made on Medicare cost reports, court stated that “Damages for a reverse false claim consist of the difference between what the defendant should have paid the government and what the defendant actually paid the government.”)

Comment: Although the burden is on the government (or relator) to prove damages, it does not have to do so with mathematical precision. Where market value is not available or the measure of harm is otherwise difficult or impossible to quantify, the court may allow the government (or relator) to establish damages using some kind of proxy. For example, where a negotiation process is tainted by false statements relating to costs of performance, a court may look to the difference in the cost that was disclosed and the actual cost to calculate damages. See *United States ex rel. Taxpayers Against Fraud v. Singer Co.*, 889 F.2d 1327, 1333 (4th Cir. 1989) (“The obvious premise upon which the presumption operates is that fraudulent inflation of cost proposals fundamentally distorts the negotiation process for a

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sole source contract and that the eventual contract price likely would have been even lower than the company's 'best estimate' had the contractor instead provided the government with that uninflated estimate at the start of negotiations." Defendant's profits, the dollar value of any kickbacks paid, and the Federal Sentencing Guidelines are examples of proxies that may be relevant to establishing damages.

- Determine whether consequential damages are available in the relevant jurisdiction and under what circumstances.

Comment: In jurisdictions where the governing case law provides that consequential damages are generally not available under the FCA, how damages are characterized matters. Put differently, in jurisdictions where consequential damages are not available, a court may still find seemingly consequential damages available if it finds that the fraudulent act was a proximate cause of the harm. See, e.g., *United States v. Ekelman & Associates*, 532 F.2d 545 (6th Cir. 1976) (damages arising out of loans obtained based on fraudulent statements included the expenses incurred by the government in maintaining property upon default, notwithstanding defendants arguments that such damages were consequential, because the responsibility of maintaining the property was forced on the government because of the fraud); *United States ex rel. Roby v. Boeing Co.*, 79 F. Supp. 2d 877 (S.D. Ohio 1999) ("If this Court determines at trial that the only damages presented by the government and Relator are of a consequential nature, then those damages would not be available to the Government and Relator under a FCA theory. However, if the Government and Relator present sufficient evidence that damages sought are of a direct, proximate, and foreseeable nature, then those damages may be available to the Government and Relator under a FCA theory of recovery."). The government and relators will have an incentive to link the damages as directly as possible to the fraudulent act; defendants, on the other hand, will want to persuade the court that the alleged damages are not the proximate result of the fraudulent act, emphasizing any intervening causes to divorce the damages from the underlying conduct. In addition, where consequential damages are unavailable under the FCA, they may still be available under an alternative theory. *United States v. Aerodex*, 469 F.2d (5th Cir. 1972) (holding that although consequential damages are not available under FCA, but that defendant could be liable for consequential damages for breach of express warrant).

- Determine whether penalties may apply and how many.

Comment: Statutory penalties may be awarded, even in the absence of economic injury. *U.S. ex rel. Davis v. Dist of Columbia*, 679 F.3d 832 (D.C. Cir. 2012). Assess whether the imposition of mandatory penalties may be unconstitutionally excessive. *U.S. ex rel. Bunk v. Birkart Globalistics GmbH & Co.*, No 1:02cv1168, 2012 U.S. Dist. LEXIS 18445 (E.D. Va. Feb. 14, 2012) (in no damages case, penalties for 9,136 invoices amounting to \$50 million fine held unconstitutional).

- Determine whether prejudgment interest may be available.

Comment: With the exception of the 8th Circuit, prejudgment interest is generally unavailable under the FCA; the reasoning is that treble damages are designed to capture these ancillary costs. See *United States v. McLeod*, 721 F.2d 282 (9th Cir. 1983); *United States v. Cooperative Grain and Supply Co.*, 476 F.2d 47 (8th Cir.1973).

- Determine whether investigative costs may be available.

Comment: There is a division of authority as to whether investigative costs are available under the FCA.

- Consider credits or counterclaims that may reduce the amount of damages owed by the defendant. To the extent that payments have already been made to the government in connection with the fraud, those payments may be credited to the government's damages *after* they are trebled (or doubled). See *United States v. Bornstein*, 423 U.S. 303 (1976) (reasoning that if credits were applied before doubling damages,

defendants could avoid the double damages by paying the single damages prior to settlement).

Comment: Payment of restitution in a parallel criminal case cannot be used to offset damages in a FCA case. See 18 U.S.C. § 3663(a).

Treble or Double?

Treble damages are mandatory and the court is without discretion, *unless* the court finds that:

- the person committing the violation furnished government officials responsible for investigating false claims violations with all information known to such person about the violation within 30 days after the date on which the defendant first obtained the information;
- such person fully cooperated with any government investigation of such violation; *and*
- at the time such person furnished the United States with the information, no criminal prosecution, civil action, or administrative action had commenced under Title 31 with respect to the violation, and the person did not have actual knowledge of an investigation into the violation;

in which case, the court may double, instead of treble, the damages. 31 U.S.C. § 3729.

Comment: Although the jury determines damages under the FCA when there is a factual dispute, courts have held that the jury is not to be instructed that the damages will be trebled or that penalties are available for each claim, as it may distort the jury's decision-making process in deciding base damages. See *U.S. ex rel. Laymon v. Bombardier Transp. (Holdings) USA, Inc.* 656 F. Supp. 2d 540 (W.D. Pa 2009); *U.S. ex rel Schaefer v. Conti Medical Concepts, Inc.*, 2009 W.L. 5104149 (W.D. Ky. 2009).

Limitations on Recovery

- Determine whether the government has already recouped the damages. The government generally may not duplicate recovery of damages. See *United States ex rel. Miller v. Bill Barbert International Construction, Inc.*, 505 F. Supp 2d 20 (D.D.C. 2010); *United States v. Rogan*, 459 F. Supp. 2d 692 (N.D. Ill 2006).
- Take into account Constitutional considerations.

Comment: An argument that damages and penalties are excessive under the Excessive Fines Clause of the Eighth Amendment *may* be available if penalties are grossly disproportionate to the wrong. See *United States v. Rogan*, 517 F.3d 449 (7th Cir. 2008); *United States v. Mackby*, 339 F.2d 1013 (9th Cir. 2003).

- Note that penalties under the FCA are not considered criminal punishment for purposes of the Double Jeopardy clause. See *Hudson v. United States*, 522 U.S. 93 (1997).

Tax Implications

- Evaluate the potential tax implications for your client.

Comment: In general, punitive civil penalties are not deductible. Section 162(f) of the Internal Revenue Code provides that “no deduction shall be allowed [as an ordinary and necessary business expense] for any fine or penalty paid to the government for the violation of law.” Compensatory damages (e.g., single damages), however, are not considered a punitive fine or penalty and may be deductible. Treas. Reg. § 1.162-32(b)(2). Whether multiple damages are compensatory or punitive depends on the intent of the parties and what purpose the payment was meant to serve (as multiple damages can serve both

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compensatory and punitive ends). Where damages are awarded by a court at the conclusion of litigation, the characterization of the damages is typically clear. However, False Claims Act settlements, by policy, are silent as to the nature of the payment. Where the settlement agreement is silent or ambiguous, the court will look to extrinsic evidence to discern the parties' mutual intent and the burden is on the taxpayer to prove such mutual intent. While the easiest way to establish that damages are deductible would be to include a provision in the settlement characterizing the damages, it is the government's policy to remain neutral with respect to the characterization of the settlement sum for tax purposes. Defendants' counsel should be mindful of how tax characterization may be leveraged during negotiations.

Note that characterization of settlement sums is relevant to relators as well. For example, pursuant to the Jobs Creation Act of 2004, attorneys fees and related costs are excluded from a relator's taxable income. Pub. L. No. 108-357, § 703, 118 Stat. 1418 (2004). Awards are otherwise considered taxable income.

Additional Resources

For additional information related to the tax implications of FCA settlements, see False Claims Act Settlements with Department of Justice, I.R.S. Industry Specialization Program Coordinated Issue, 2008 WL 4106103 (September 5, 2008); I.R.S. Gen. Couns. Mem. 2007-0015 (July 12, 2007); I.R.S. Tech. Adv. Mem. 200502041 (January 14, 2005).

For a detailed discussion of the federal False Claims Act, see BNA's Health Law & Business Series, Portfolio No. 2650, "False Claims Act: Health Care Applications and Defenses."