

ALERT

The Sixth Circuit Deals a \$657 Million Reminder That the Government Bears the Burden of Proving Damages

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After over a decade of litigation about an alleged 30 year-old fraud, the U.S. Department of Justice was given a stern reminder that the Government bears the burden of proving damages when it sues a contractor for False Claims Act damages, restitution, and price adjustments in connection with pricing governed by the Truthful Cost or Pricing Data Act (formerly TINA). The Court of Appeals for the Sixth Circuit (Sixth Circuit) reversed a \$657 million damages award against United Technologies Corp. (United Technologies) because the Government failed to prove that the contractor's alleged false certified cost and pricing data caused any actual loss.

In 1983, United Technologies bid on a contract to manufacture jet engines for the Air Force. In 1998, years after the contract concluded, the Government brought a price adjustment claim against United Technologies at the Armed Services Board of Contract Appeals (ASBCA) for violating TINA, and, in 1999, a False Claims Act and common law restitution claim in a federal district court in Ohio. The ASBCA dismissed the TINA claim because no actual damages were proven. ASBCA No. 53349 (Jan. 19, 2005), *aff'd*, 463 F.3d 1261 (Fed. Cir. 2006).

In the False Claims Act lawsuit, the district court found that United Technologies knowingly overstated its initial cost projections and falsely certified that its final proposal reflected its best estimates and/or actual costs. United Technologies was thus found to have violated the False Claim Act by knowingly certifying defective cost and pricing data. The district court awarded the Government \$7 million under the False Claims Act's civil penalty provision but

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declined to find that the Government had sustained any actual damages. The Sixth Circuit subsequently reversed and remanded the claim for the district court to review its damages calculation. On remand, the district court awarded the Government \$657 million, the subject of this appeal.

In general, along with a civil penalty for each false claim or false statement, the False Claims Act provides for trebled damages equal to the Government's actual loss. But, according to the Sixth Circuit panel, "[w]hen the Government gets what it paid for despite a contractor's misstatements, it has suffered no 'actual damages.'" In this week's decision, the Sixth Circuit concluded that the Government did not adequately prove that United Technologies' conduct caused actual damages.

The Sixth Circuit concluded that the Government's damage calculations were flawed because the calculations: (1) failed to determine the "fair market value" of the contract as a whole and thus whether the Government actually overpaid; (2) failed to consider the role of competition in the pricing; and, (3) failed to consider whether United Technologies' price reductions in later years offset the initially overstated costs. The Government's improper calculations focused on United Technologies' original cost and pricing data for every contract line item, instead of performing a "comparable sales" analysis against other aircraft engine prices to establish fair market value, which the Sixth Circuit determined was the "preferred method," even in the limited and heavily regulated jet engine market. In reaching its conclusion that the Government's damage calculations were flawed, the Sixth Circuit found, like the ASBCA before it, that the Government could not succeed on a presumption that each dollar of overstated costs equaled a dollar of damages. Where, as here, the contract was competitively priced, the circumstances supported that competition controlled prices, rather than the cost and pricing data.

The Sixth Circuit ultimately remanded the case back to the district court to determine damages, but expressed significant hesitation about the prospect of continued litigation: "after seventeen years of litigation about a fraud that occurred thirty-two years ago . . . there is something to be said for leaving it at that."

This decision is a reminder that the Government bears the burden of proving its actual damages when seeking False Claims Act damages, TINA price adjustments, or restitution. For contractors, the decision is a reminder of the significant incentive to challenge damages calculations as vigorously as underlying liability. Although preparing arguments about damages can be costly and time consuming, the magnitude of the positive reversal of United Technologies' fortunes proves that it can be worth every penny. The decision is also a caution to carefully vet your damages expert, however-as the Government was admonished here, an auditor is not necessarily a pricing expert.