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ALERT

Sixth Circuit Rejects "Fairyland" False Claims Act Damages for Underpayment of Davis-Bacon Wages

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In an emphatic opinion issued earlier this month, the Sixth Circuit Court of Appeals drastically reduced a damages award under the False Claims Act (FCA) against a contractor that underpaid wages required under the Davis-Bacon Act (the Act) but delivered the work contemplated under the contract. The court's decision that the FCA damages must be based on the amount of unpaid wages (which was less than $10,000) and not the entire value of the services (more than a quarter-million dollars) is welcome news for companies that do business with the Government. The FCA permits the Government to receive treble damages—triple the amount of the Government's "actual" damages, or the difference in value between what it paid for and what it received—and so how courts calculate the Government's actual damages can dramatically affect the scope of potential liability. In this respect, the Sixth Circuit's insistence on "damages grounded in reality" and not "fairyland" sharply contrasts with the increasingly popular theory that any false claim "taints" the entire contract, nullifying any value to the Government and permitting damages of triple the Government's payment for the relevant services.

This whistleblower case was brought on behalf of the Government by an employee of a subcontractor on a project to build warehouses on an Army base. The contract required Circle C Construction and its subcontractor to pay electricians above-market wages under the Davis–Bacon Act, 40 U.S.C. § 3142, and to submit weekly compliance statements representing that the companies had paid the required wages. In fact, the subcontractor underpaid its electricians by $9,916,

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making Circle C's compliance statements false certifications under the FCA, 31 U.S.C. § 3729.

As discussed in a Wiley Rein article and interview with Wiley Rein Government Contracts partner Eric Leonard published on *Law360* in October 2012, the Sixth Circuit previously affirmed the district court's finding of liability but reversed the damages award because it concluded that the court's calculation was speculative and based partly on purchase orders that were not addressed in the whistleblower's complaint. After remand, the lower court in August 2014 awarded damages totaling $777,894.54, which it calculated by tripling the entire amount paid for the subcontractor's services—on the theory that the underpaid wages "tainted" the services and rendered them worthless—before subtracting the subcontractor's $15,000 settlement payment.

The Sixth Circuit emphatically rejected this calculation and substantially reduced the damages award to $14,748. The court dismissed the notion that the Government received no value from the electrical work, noting that "in all of these warehouses, the government turns on the lights every day." The court reasoned that "the government bargained for two things: the buildings, and payment of Davis-Bacon wages," and that it "got the buildings but not quite all of the wages," and thus the Government's "actual" damages were the shortfall in wages of $9,916. The court also rejected the argument that damages should be based on the entire value of the services because the Government *would have* withheld payments had it known of the underpaid wages, noting that the Act does not permit such a total withholding, and therefore the Government's damages theory was "fairyland rather than actual."

The Sixth Circuit's decision should come as a relief to government contractors. The Department of Justice and whistleblower attorneys often argue, with increasing success, that FCA damages should be based on the entire contract value with no deduction for value to the Government. This method of determining damages—in conjunction with expansive and increasingly prevalent theories of what constitutes a false claim—presents massive potential liability for contractual or regulatory violations despite the contractor's full performance and absent truly fraudulent conduct. Separately, the Government and whistleblowers often argue that even if damages must account for value to the Government, the deduction should come *after* trebling, a method known as "gross trebling" that can substantially affect the damages amount in cases where the Government received value under the contract. The Sixth Circuit's decision may help stem this tide and restore commonsense principles to calculating FCA damages. Indeed, last April, the Sixth Circuit overturned a $657 million damages award after concluding that the award failed to soundly calculate the Government's actual loss.

Overall, this case emphasizes that companies assessing their FCA liability should account for any value to the Government. This value can come not only from products and services provided under the contract, but also the Government's sale of any property related to the claims, credits to the Government from self-reported overpayments, or restitution to the Government in related proceedings. This case is also a reminder of the importance of vigorously challenging damages calculations—a process that, while costly, can be worth every penny in cases where the Government has advanced dubious damages theories that inflate its actual loss.