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Valuing Services Provided: FCA Damages in the Wake of United States v. Anchor Mortgage Corp.



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Introduction

In *United States v. Anchor Mortgage Corp.*, [1] the U.S. Court of Appeals for the Seventh Circuit endorsed net trebling over gross trebling as a measure of calculating False Claims Act damages. Although not all circuits have confronted it, the majority of circuits to consider the issue have endorsed this approach.[2]

Drawing on this and other recent decisions, this article makes the case for why net trebling is the more sensible approach to FCA damages calculation and why courts should assign some value to the services the government received even if the services failed to comply with a particular regulation, rather than accede to the notion that the government would have paid nothing for services tainted by a regulatory violation.

This article then explores whether this reasoning could extend to FCA cases involving allegations that the provider submitted claims for payment for services provided in violation of the Stark Law and/or the Anti-Kickback Statute ("AKS").

I. Damages Under the False Claims Act

Penalties and damages under the FCA can be enormous. The FCA imposes two types of liability—a statutory penalty and the potential for treble damages. First, the statutory penalty imposes a $5,500 to $11,000 civil fine per violation on any defendant who submits a false claim or makes a false statement for payment of a false

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[1] United States v. Anchor Mortgage Corp., Nos. 10-3122, 10-3342 & 10-3423, 2013 WL 1150213 (7th Cir. Mar. 21, 2013).

[2] Other circuits endorsing net trebling include the Second, Sixth, D.C., and Federal Circuits. *See, e.g.*, United States *ex rel.* Feldman v. Gorp, 697 F.3d 78, 87–88 (2d Cir. 2012); United States v. United Technologies Corp., 626 F.3d 313, 321–22 (6th Cir. 2010); United States v. Anchor Mortgage Corp., Nos. 10-3122, 10-3342 & 10-3423, 2013 WL 1150213, at *3 (7th Cir. Mar. 21, 2013); United States v. Sci. Applications Int'l Corp., 626 F.3d 1257, 1279 (D.C. Cir. 2010); Commercial Contractors, Inc. v. United States, 154 F.3d 1357, 1372 (Fed. Cir. 1998). The Ninth Circuit is on the gross trebling side, relying on United States v. Bornstein, 423 U.S. 303 (1976). *See, e.g.*, United States v. Eghbal, 548 F.3d 1281, 1285 (9th Cir. 2008). Although the Fifth Circuit has not squarely addressed the issue, it appears that there would be precedent to support a gross trebling approach. *See, e.g.*, Faulk v. United States, 198 F.2d 169, 172 (5th Cir. 1952) (in conspiracy prosecution where defendant wrongfully substituted reconstituted milk for fresh milk, jury not instructed to consider market value of reconstituted milk in measuring damages) (case cited in *Bornstein*).

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claim.[3] Second, the defendant can be liable for up to ''3 times the amount of damages which the Government sustains because of the act of [the defendant].''[4]

This treble damages provision is particularly important to the government, not only because it provides an opportunity for lucrative recoveries but because treble damages affect the dynamic of litigation. When facing both treble damages and penalties, parties have a strong incentive to settle claims rather than defend them in court. Treble damages penalties may vary depending on what trebling method the government advances.

Two approaches have emerged—known as ''gross trebling'' and ''net trebling.'' Although the FCA is silent on the appropriate trebling method, the gross trebling approach combines all amounts that the United States paid as a result of the alleged false claim, trebles that total, and subtracts any offsetting amounts that had been realized by the government.[5]

That approach is endorsed by the Department of Justice and favored by whistleblowers because the resulting damages amount is greater.

On the other hand, the net trebling approach combines all amounts that the United States paid as a result of the alleged false claim, subtracts any offsetting amounts that had been realized by the government, and then trebles that total. This approach is more akin to the actual losses incurred by the government.

II. Why Gross Trebling Is Inconsistent With FCA Damages

The FCA's damages multiplier has both compensatory and punitive roles.[6] However, despite punitive attributes, gross trebling is excessive and inconsistent with the meaning of the FCA.

Under the gross trebling approach, neither the government nor the defendant is ultimately in a just position. Trebling prior to subtracting offsetting amounts realized by the government leads to windfall recoveries and decreased likelihood that defendants will mitigate damages (since any offsetting amounts conferred to the government are marginalized by not being factored in until post-trebling). Gross trebling provides a recovery to the government that significantly exceeds any amount needed to make the government whole.

Using a net trebling or gross trebling approach can have enormous impact on the evolution and outcome of FCA cases. Recent decisions, discussed below, show that courts are increasingly keen on the actual impact of a defendant's false or fraudulent claims, and will not impose grossly exaggerated damages while ignoring the value of the goods and services provided by the defendant to the government, even if the provision of such goods fails to comport with an applicable statute or regulation.

Because the government will likely continue to argue for gross trebling in jurisdictions without firmly ensconced net trebling jurisprudence, it is important to underscore the various net trebling decisions when litigating FCA damages calculation.

A. *United States v. Anchor Mortgage Corp.*

The Seventh Circuit squarely decided the trebling issue in *United States v. Anchor Mortgage Corp.*[7] After a bench trial, the lower court found the defendants, Anchor Mortgage Corp. and its chief executive officer, liable under the FCA for lying in connection with applying for federal guarantees of home mortgage loans and paying kickbacks for client referrals.[8]

A main issue before the Seventh Circuit was the proper approach to trebling of damages and whether a net or gross trebling method was the more appropriate interpretation of § 3729(a)(1). The district court's approach, endorsed by the United States in the case, called for gross trebling.

This approach combined all amounts that the United States paid to lenders under the guarantees, trebled that total, subtracted any offsetting amounts realized by the government from sales of collateral securing the loans, and then added the statutory penalty of $5,500 for each offending loan.[9]

The Seventh Circuit rejected the gross trebling approach in favor of a net trebling approach.[10] In doing so, the court emphasized that the FCA, though silent on the appropriate trebling method, does not signal a departure from the norm, which is net trebling.[11] For example, the Clayton Act[12] (another federal statute) provides for treble damages as a remedy for various antitrust violations, which are calculated using net trebling.[13]

Moreover, the court found that quantifying damages using net (as opposed to gross) loss is the norm in civil litigation.[14] For example, according to the Uniform Commercial Code, when a seller tenders nonconforming goods, damages are calculated as the difference between the contract price and the value of the goods received.[15] The gross trebling equivalent would

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[3] Penalty amounts are adjusted by the Federal Civil Penalties Inflation Adjustment Act of 1990 (28 U.S.C. § 2461 note). Statutory penalties may be imposed without the government proving damages caused by the false claim.

[4] 31 U.S.C. § 3729(a). Damages are reduced from treble to double if the defendant voluntarily discloses a violation as described in § 3729(a)(2) of the FCA.

[5] As discussed above, the FCA provides that damages awarded be ''3 times the amount of damages which the Government sustains'' but does not provide any additional guidance on the proper meaning of ''damages.''

[6] *See, e.g.*, Vermont Agency of Nat. Resources v. U.S. *ex rel.* Stevens, 529 U.S. 765, 784–85 (2000) (''the FCA imposes damages that are essentially punitive in nature . . . .'').

[7] United States v. Anchor Mortgage Corp., Nos. 10-3122, 10-3342 & 10-3423, 2013 WL 1150213 (7th Cir. Mar. 21, 2013).

[8] *Id.* at *1.

[9] *Id.* at *2.

[10] The net trebling calculation here begins the same way as gross trebling—by combining all amounts that the United States paid to lenders under the guarantees—but then subtracting the value of any collateral from the loss before trebling. The resulting monetary difference between the two approaches can be significant. Using one loan as an example, the Seventh Circuit calculated gross treble damages to be $332,229.15 and net treble damages to be $195,829.15 (both including the $5,500 civil penalty). *Id.*

[11] *Id.* at *3.

[12] *See* 15 U.S.C. § 15. As part of the damages calculation in Clayton Act cases, the court subtracts the competitive market price from the defendant's monopoly price (*i.e.*, the monopoly overcharge) and trebles that difference.

[13] *See Anchor Mortgage Corp.*, 2013 WL 1150213, at *3.

[14] *Id.*

[15] *See, e.g.*, U.C.C. § 2-714 (2010).

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entail trebling the contract price without regard to the value of goods received.

Interestingly, the government contended that gross trebling was appropriate under the Supreme Court's decision in *United States v. Bornstein*.[16] *Bornstein* held that double damages (now treble damages) are properly calculated from actual damages suffered by the government and that the multiplier exercise should occur ''before any subtractions are made for compensatory payments previously received by the Government from any source.''[17]

The government in *Anchor Mortgage* contended that the *Bornstein* holding compelled the Seventh Circuit to use gross trebling. However, the Seventh Circuit found that a footnote to the above statement ''unambiguously uses the contract measure of loss, supporting a net trebling approach.''[18]

B. *United States v. Science Applications International Corp.*

In *United States v. Science Applications International Corp.* (''SAIC''), a government contractor agreed to provide the Nuclear Regulatory Commission (''NRC'') with expert advice and certified that it had no organizational conflicts of interest.[19] The United States alleged that SAIC violated the FCA by seeking government payments from the NRC while knowingly violating contractual provisions governing potential conflicts of interest.[20]

The DOJ brought suit against SAIC alleging one breach of contract claim and two civil FCA claims (the district court jury found SAIC liable on all claims). Damages on the breach of contract claim totaled $78 and damages on the FCA claims totaled $1,973,839.61—the full amount of all government payments made to SAIC under the relevant contracts. This amount was then trebled and combined with the $577,500 in civil penalties to reach a grand total of $6,499,096.83.

The D.C. Circuit affirmed the breach of contract judgment but vacated and remanded the FCA damages issues to the district court—reproving the district court's jury instruction. The district court instructed the jury as follows:

> Your calculations of damages should be limited to determining what the Nuclear Regulatory Commission paid to [SAIC] over and above what the NRC would have paid had it known of SAIC's organizational conflicts of interest. Your calculation of damages should not attempt to account for the value of services, if any, that SAIC conferred upon the Nuclear Regulatory Commission.[21]

The D.C. Circuit applied a benefit-of-the-bargain framework, rejecting the lower court's approach of automatically computing damages as the total amount of payments made by the government.[22] Under the benefit-of-the-bargain framework, the fact finder awards an amount of damages that ''puts the government in the same position as it would have been if the defendant's claims had not been false.''[23]

Accordingly, the D.C. Circuit held that the damages should have been measured as the difference between the value of SAIC's services—compromised by the appearance of bias in the undisclosed conflict of interest—and the value of conflict-free services that were promised.[24] Additionally, the D.C. Circuit found that the jury should have been instructed to account for the value of services SAIC provided to the government.[25]

C. *U.S. ex rel. Davis v. District of Columbia*

Less than two years after *SAIC*, the D.C. Circuit highlighted and expanded *SAIC*'s damages holding in *United States ex rel. Davis v. District of Columbia*.[26] In *Davis*, the relator's firm prepared the Medicaid reimbursement claims for the District of Columbia Public Schools (''DCPS'') for fiscal years 1995, 1996, and 1997.[27] While Davis's firm was preparing the fiscal year 1998 form, DCPS hired a new firm to prepare the claims, replacing Davis's firm.[28]

Davis's firm retained key supporting documentation for the fiscal year 1998 form, and the new firm submitted DCPS's fiscal year 1998 Medicaid reimbursement claim without the required documentation. Davis alleged that submitting the fiscal year 1998 form without the required documentation violated the FCA and that the United States would not have paid DCPS anything had it known that the reimbursement documentation was absent.[29]

Relying on benefit-of-the-bargain framework articulated in *SAIC*, the D.C. Circuit held that the government sustained no damages because the purpose of the documentation requirement is to ensure services were actually provided, and there was no dispute in the case that the services were in fact provided.[30] There was no allegation that the performance received by the government was worth anything less than what was paid for the services.[31]

Finally, the court noted that although treble damages were unavailable, statutory penalties would be appro-

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[16] United States v. Bornstein, 423 U.S. 303 (1976).

[17] *Id.* at 316.

[18] *Anchor Mortgage Corp.*, 2013 WL 1150213, at *4. The *Bornstein* footnote reads, ''The Government's actual damages are equal to the difference between the market value of the tubes it received and retained and the market value that the tubes would have had if they had been of the specified quality.'' 423 U.S. at 316 n.13.

[19] United States v. Sci. Applications Int'l Corp., 626 F.3d 1257 (D.C. Cir. 2010).

[20] *Id.* at 1260.

[21] *Id.* at 1278.

[22] *Id.* at 1278–79.

[23] *Id.* at 1278 (internal citation omitted).

[24] *Id.* at 1279.

[25] This is not to say that the government will never be able to recover the full value of payments made to the defendant. Under the benefit-of-the-bargain framework, the government will sometimes be able to recover the full value of such payments, but only where the government proves that it received no value from the product or service delivered. *See* United States v. Sci. Applications Int'l Corp., 626 F.3d 1279 (D.C. Cir. 2010).

[26] U.S. *ex rel.* Davis v. District of Columbia, 679 F.3d 832 (D.C. Cir. 2012).

[27] *Id.* at 835.

[28] *Id.*

[29] *Id.* at 839. Like *SAIC*, the government in *Davis* sought damages equal to the full amount of payments made to the contractor.

[30] *See id.* at 840.

[31] The court included an illustrative analogy to support the lack of damages: ''A server's failure to bring a receipt after dinner causes no harm when you know you've been properly charged. The same is true here: The government got what it paid for and there are no damages.'' *Id.*

priate against DCPS if a violation was proved on remand (and that Davis may be eligible to share in that recovery, penalties without damages, if he proves his claims).[32]

III. FCA Damages Implications on Stark Law and Anti-Kickback Statute

Although recent federal cases have made considerable progress in sorting out the damages analysis under the FCA, it remains to be seen whether the same reasoning could extend to FCA cases involving allegations that the provider submitted claims for payment for services provided in violation of the Stark Law and AKS.

Traditionally, the government has argued that damages must be based on the entire amount of the payment for all services provided in violation of Stark and/or AKS.[33] Indeed, courts have routinely adopted the government's position that damages in FCA cases based on Stark or AKS violations equal the entire amount of all government payments for services provided in violation of Stark and/or the AKS.[34]

For example, in *United States v. Rogan*, the government sued the owner of a medical center under the FCA alleging that the defendant participated in a scheme to submit claims for payment to Medicare and Medicaid in violation of the Stark Law and the AKS.[35]

Following a bench trial, the court ruled in favor of the government, finding that compliance with Stark and the AKS was a condition of payment, rendering the underlying claims false.[36]

In calculating damages, the court made no findings regarding the value of the underlying services, or whether such services were medically necessary. Instead, the court simply calculated damages as the whole amount paid by the government for services rendered in violation of Stark and the AKS.[37]

However, as pointed out in *SAIC* and *Davis*, the lower court's reasoning in *Rogan* conflates causation with damages.[38] The total amount paid by Medicaid for the medical services in question totaled $16.5 million, which was trebled, resulting in a damages award of over $50 million.[39] Despite this massive damages award, there were no findings that the services were not actually provided, or were medically unnecessary, or were of poor quality. In other words, the government received $16.5 million worth of medical care that was reasonable and necessary, and for which it likely would have paid another provider had it discovered the underlying Stark and AKS violations at the time.[40]

The court gave no consideration to the government's actual loss as a basis for damages, instead allowing the government to reap a windfall. The Seventh Circuit affirmed the damages award, even while conceding that ''most of the patients for which claims were submitted received some medical care-perhaps all the care reflected in the claim forms.''[41]

As discussed above in *Davis* case, the D.C. Circuit instructed that the proper measure of damages was the difference between the value of the ''tainted'' services the government received and the value of the ''untainted'' services it had been promised.[42] The taint was the defendant's failure to maintain adequate supporting documentation for services provided to Medicaid beneficiaries as required by federal regulations.[43]

In determining the value of the tainted services, the *Davis* court examined the purpose of the underlying documentation requirement, concluding that the regulations were designed ''to ensure that the government pays only for services actually rendered.''[44] Because there was no dispute that the services were actually rendered, ''the maintenance of documents to prove that they were has no independent monetary value.''[45] Ultimately the taint did not reduce the value of the services the government received at all.

A related issue is how the court would quantify the taint of a Stark or AKS violation. The Stark Law is largely designed to prevent overutilization and the provision of medically unnecessary services.[46]

Imagine a case involving a ''technical'' Stark violation, such as failure to sign a physician lease renewal for a certain period of time during which the parties otherwise operated in accordance with the terms of the original, Stark-compliant lease. In such a case, assume that the undisputed evidence in the record shows that the services rendered during the period of time the lease renewal remained unsigned were all medically necessary.

The reasoning of the *Davis* court could easily apply. In *Davis*, the regulation that was violated was designed to verify that services were provided. Since there was no dispute services were provided, the regulatory violation caused no economic loss to the government. In this

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[32] U.S. *ex rel.* Davis v. District of Columbia, 679 F.3d 832, 840 (2012).

[33] This argument is based in part on the fact that the Stark statute and regulations require providers to refund all payments received for designated health services that were provided pursuant to a prohibited referral. *See* 42 U.S.C. § 1395nn(g)(2); 42 C.F.R. § 411.353(d).

[34] *See*, *e.g.*, United States v. Mackby, 261 F.3d 821 (9th Cir. 2001); U.S. *ex rel.* Pogue v. Am. Healthcorp., 914 F. Supp. 1507 (M.D. Tenn. 1996).

[35] United States v. Rogan, 459 F. Supp. 2d 692 (N.D. Ill. 2006), *aff'd*, 517 F.3d 449 (7th Cir. 2008).

[36] *Id.* at 717.

[37] The *Rogan* court explained as follows:

> The measure of damages the United States is entitled to recover under the FCA is the amount of money the Government paid out by reason of the false claims over and above what it would have paid out if the claims had not been false or fraudulent. . . . [i]n the instant case, the United States would have paid Edgewater nothing for hospital claims related to patients referred to Edgewater by physicians with a prohibited financial relationship with the hospital. *Id.* at 726 (internal citations omitted).

[38] *See Davis*, 679 F.3d at 839.

[39] *Id.* at 727.

[40] At least one court has tried to justify the apparent windfall to the government in this context by explaining that if it were otherwise, the government would be ''in the position of funding illegal kickbacks after the fact.'' U.S. *ex rel.* Bidani v. Lewis, 264 F. Supp. 2d 612, 616 (N.D. Ill. 2003). In this respect, calculating damages in Stark/AKS-based FCA cases as the entire amount paid for all services provided in violation of Stark and/or the AKS ends up functioning as a restitution or disgorgement model for damages, designed to punish the defendant rather than make the plaintiff whole.

[41] United States v. Rogan, 517 F.3d 449, 453 (7th Cir. 2008).

[42] *Davis*, 679 F.3d at 840.

[43] *Id.* at 834.

[44] *Id.* at 840.

[45] *Id.*

[46] Am. Lithotripsy Soc'y v. Thompson, 215 F. Supp. 2d 23, 26 (D.D.C. 2002).

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hypothetical case, the Stark Law was designed to prevent medically unnecessary services from being billed to federal healthcare programs.

Since there is no dispute the services in question were medically necessary, the Stark Law violation caused no economic loss to the government. Similar to the *Davis* case and its benefit-of-the-bargain approach, the court could justifiably calculate damages as zero.

That does not mean that all FCA cases involving Stark and/or AKS violations should result in a finding of zero damages. Presumably, the evidence in some cases would show overutilization and lack of medical necessity.

Further, the taint of a more serious AKS violation would presumably reduce the value of the services the government received more than the taint of a relatively minor Stark violation. But courts should analyze value in calculating FCA damages, even if the underlying violation is serious enough to render the services of no value, rather than basing damages on the entire amount of the government payment.

IV. Conclusion

Between the net and gross trebling approaches to FCA damages calculation, net trebling is the more sensible. It makes the government whole without excessively penalizing the defendant and providing a government windfall.

Given the enormity of the potential damages in FCA cases, it should be incumbent on courts to engage in a more thorough analysis of the government's actual economic loss, instead of advancing a theory which summarily aggregates all government payments.

A proper accounting of benefits conferred on the government by the defendant rectifies the government's actual loss. This approach should also apply to FCA cases involving allegations that a provider submitted claims for payment for services performed in violation of the Stark Law and/or the AKS.