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IN THE

Supreme Court of Virginia

RECORD NO. 161799

MCR FEDERAL, LLC,

Appellant,

v.

JB&A, INC.,

Appellee.

BRIEF OF APPELLEE

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STATEMENT OF THE CASE

This case involves the sale of a government contracting business (the "Intelligence Business"). On May 31, 2011, MCR Federal, LLC ("MCR") induced JB&A Inc. ("JB&A") to sell the Intelligence Business by representing that MCR was not under investigation. At the time of this representation, MCR (1) knew that it had violated federal ethics laws; (2) was aware that the Air Force was investigating these violations; and (3) was actively concealing its ethical misconduct and the investigation from JB&A. The Air Force ultimately launched a criminal investigation of MCR, forced MCR's president to resign, and twice suspended MCR from obtaining any contracts from the federal government.

If MCR had told JB&A the truth, JB&A would have not closed the sale. Instead, relying upon MCR's false representations, JB&A consummated the transaction. Under the purchase contract JB&A was to receive $19.5 million of the purchase price as earn-out payments in the two-year period after closing if the Intelligence Business met certain performance benchmarks once it became part of MCR. As a result of MCR's ethical misconduct and suspensions — and MCR's false statements about them — JB&A and its shareholders never received any of the $19.5 million in payments.

JB&A sued MCR in the Circuit Court for Fairfax County for breach of contract and fraud. MCR filed a counterclaim for fraud. After a 21-day bench trial

and extensive post-trial briefing and argument, the Circuit Court found that MCR had committed constructive fraud and breached the terms of its contract to purchase the Intelligence Business. The court also ruled that MCR's counterclaim was baseless. The trial court issued meticulous fact-findings, including over 70 pages of specific credibility determinations covering each of the witnesses.

The court awarded JB&A $11,995,002 in damages, representing the difference between the value of the Intelligence Business at closing less the amount that MCR paid for it. The trial court also awarded JB&A approximately $3.7 million in prejudgment interest on its breach-of-contract claim under Delaware law. And it awarded JB&A $1.9 million in attorney's fees based on its finding that MCR had engaged in a deceitful and callous — "almost sinister"— pattern of misconduct by filing a baseless counterclaim and having its witnesses provide false testimony at trial.

MCR appeals. It does not, however, challenge the trial court's holdings that it breached its contract with JB&A as a result of its misrepresentations; that it is liable to JB&A for the damages caused by that breach; that JB&A is entitled to prejudgment interest under Delaware law on its contract damages; that MCR's counterclaim was baseless; or that MCR engaged in a pattern of callous, deliberate and deceitful acts.

Rather, MCR appeals the trial court's rulings that (i) MCR was liable for fraud as a result of its misrepresentations (Assignment of Error 1); (ii) MCR's misrepresentations caused JB&A damages in the amount of $11,995,002 (Assignments of Error 2 and 3); and (iii) JB&A was entitled to an award of attorney's fees based on MCR's callous, deliberate and deceitful acts (Assignments of Error 4 and 5).

COUNTERSTATEMENT OF FACTS

MCR joins the legions of appellants who address unfavorable results by shading the evidence in their own favor on appeal. Its Statement of Facts presents the evidence in the light most favorable to the party who lost below.

1. In Late 2010, JB&A Decided to Sell the Intelligence Business

JB&A was a government contractor, primarily performing work for U.S. intelligence agencies. Founded in 1988, JB&A developed a reputation for high integrity and quality work. This allowed the Intelligence Business to grow from 2 to 190 employees, and enabled it to increase its revenues consistently every year. Appendix (A) 299:13-22, A164, 190. By 2010, it earned approximately $60 million in annual revenues. A299, 1301-03. An employee stock ownership plan, or "ESOP," owns about 67% of JB&A's stock. A201, 1279-1328. In 2009, JB&A hired an outside consultant to analyze its ability to meet its long-term obligation to repurchase stock from the ESOP when its employees retire. Trial Record (TR)

2183; A1859-70. The consultant found that JB&A was managing its repurchase obligation appropriately, and that, if JB&A stayed its course, it would save up enough cash to fund the ESOP repurchase obligation. *Id.*

The consultant also told JB&A that the current market for the sale of its Intelligence Business was attractive, and that it could expect to receive approximately $60 million on a sale. A749, 221. Based on this robust assessment of the market, JB&A's Board of Directors decided to pursue a sale. A747-49. Future ESOP repurchase obligations played no factor in this decision. TR1526-27, A747-48. As the trial court found, "[t]here was no compelling event in 2010 which made this sale a necessity." A2313; *cf.* Br. 2-4 (claiming that "JB&A need[ed] to sell itself" to fund ESOP buyback).

2. <u>To Preclude Other Buyers from Making Offers, MCR Moved Quickly and Signed a Letter of Intent with JB&A on February 11, 2011</u>

JB&A retained an investment banking firm, the McLean Group ("McLean") to help find a buyer. McLean immediately identified more than sixty potential buyers. A2045, 1946-48. MCR moved quickly to acquire JB&A. In February 2011—after JB&A had been on the market for only a few months—the parties signed a letter of intent ("LOI"), which prohibited JB&A from soliciting bids from other buyers while they negotiated a purchase agreement with MCR. Specifically, paragraph 11 of the LOI stated that JB&A could not:

> …directly or indirectly, through any representative or otherwise, solicit or entertain offers from, negotiate with or in any manner encourage, discuss, accept or consider any proposal of any other person relating to the acquisition of [JB&A], its assets, equity or business, in whole or in part, whether through direct purchase, merger, consolidation or other business combination.

A1681, 1676-82. *Cf.* Br. 29 (claiming that there is no evidentiary support for a claim that the letter of intent precluded JB&A from discussing a sale with other buyers).

3. <u>On May 5, 2011, JB&A Signed a Purchase Agreement to Sell the Intelligence Business to MCR for $62.2 Million</u>

On May 5, 2011, JB&A and MCR signed an asset purchase agreement (the "APA") governed by Delaware law. A1172-1278; APA §8.8; A1236. MCR agreed to pay approximately $62.2 million for the Intelligence Business, paying $42.7 million at closing and paying up $19.5 million in "earn-out payments" over the following two years if the Intelligence Business hit certain revenue and gross-margin targets in 2011 and 2012. *Id.*; APA § 1.8; A1186-87.

Under the APA, MCR had to make certain representations to assure JB&A that MCR's conduct would not prevent JB&A from receiving the full $62.2 million purchase price. Under § 3.3 of the APA, MCR represented that there existed:

> no private or government action, suit, proceeding, claim, . . . investigation, litigation, or inquiry pending or, to the knowledge of [MCR] threatened before, with or by any Governmental Entity or other Person against [MCR]. ., nor were there any circumstances that could reasonably lead to an investigation, inquiry, etc… that [c]ould cause a Buyer Material Adverse Effect. A1214.

The APA was an executory contract. It contained certain conditions precedent to be satisfied by each party before the other had the duty to perform. APA § 5.3; A1228. One of those conditions precedent was that MCR provide a certificate (the "Bring-Down Certificate") to JB&A certifying that all representations made by MCR under the APA on May 5, 2011, would be true and correct at the time of the closing date.[1] APA § 5.3; A1228. MCR was under no duty to provide the Bring-Down Certificate or close the sale – *i.e.*, MCR had no liability to JB&A if it failed to provide the Certificate or close the sale**.** The failure to provide the Certificate would simply excuse JB&A's obligation to close the sale by terminating the APA. In the event of such a termination, Section 6.2 of the APA provided, in relevant part, that the APA "shall forthwith become void and there will be no Liability under this Agreement [APA] on the part of any party…". APA § 6.2; A1229.

4. <u>Before the May 31 Closing, MCR Violated Federal Ethics Laws and the Federal Government Launched an Investigation</u>

While JB&A and MCR were preparing to close the sale, MCR was

[1] Among the conditions precedent under the APA was that "[t]he representations and warranties of [MCR] in this Agreement that are qualified as to materiality shall be true and correct in all respects on and as of the Agreement Date and on and as of the Closing Date as though such representations and warranties were made on and as of such date…." APA, § 5.3(c). Section 5.3(e) further stated as another condition precedent that "[MCR] shall have delivered to [JB&A] a certificate of an officer of [MCR] to the effect that the **conditions precedent** set forth in Sections… and 5.3(c) have been satisfied." (emphasis added). A1228.

simultaneously preparing a final price proposal on a multi-million dollar Air Force contract. On May 19, 2011, an Air Force contracting officer sent an email to certain MCR employees that inadvertently attached the pricing information of MCR's sole competitor for the contract. A1329. Within minutes, the Air Force officer realized her mistake and directed MCR to destroy the pricing information.[2] A1330. MCR ignored that directive. Four MCR employees either reviewed or discussed the competitor's pricing information, and one employee retained a copy. A1336, 1375-77, A690, 693, 1361.

The next day — and eleven days before closing — the Air Force launched an investigation under the Procurement Integrity Act ("Act or PIA") into MCR's handling of its competitor's pricing information. It requested affidavits from all MCR employees who had received the information. A1339, 1397-98, A668-70, 1343, 1361-66, 1374. The Act imposes strict ethical restrictions on obtaining or using a competitor's pricing information. 41 U.S.C. §§ 2101-2107. Companies that violate these restrictions are subject to a range of sanctions, including criminal prosecution, civil fines, disbarment and suspension. 41 U.S.C. § 2105; FAR § 3.104.8.

Upon receipt of the request for affidavits, MCR hired Venable, an experienced government contracting law firm, to assist with the investigation.

[2] MCR inaccurately suggests that MCR initiated the recall and containment measures. This is incorrect. *Compare* Br. at 10 with A1329-30.

A1349, 1353, A648-51. Understanding the negative implications of the Air Force investigation, MCR's management demanded total secrecy, instructing that "[n]o one is to mention that we have Venable involved, please." A1353. Venable advised MCR that anyone who had been exposed to the competitor pricing information had to be removed from working on the Air Force bid proposal. A1353, 1386.

MCR ignored Venable's advice. Instead, MCR directed these "tainted" employees, armed with the competitor's prices, to continue work on the bid proposal. What is more, MCR affirmatively "cover[ed] up" their participation. A2308, 2321, 2582-83, 2355, 2357, 2302, 2320.

On May 26, 2011, MCR submitted a bid that was 33% lower than its previous proposal and substantially lower than its competitor's bid. A392-93, A575; TR 646.

5. MCR Induced JB&A to Close on May 31, 2011 by Concealing the Air Force Investigation and Falsely Representing that MCR Was Not Under Investigation

Consistent with MCR's plan to maintain total secrecy, MCR hid the Air Force investigation from JB&A. As the trial court found:

> MCR was given the opportunity by JB&A to do their due diligence. They [MCR] were given all the information to do that. Access to all the information. MCR, on the other hand, never gave JB&A a similar opportunity. They hid the facts from JB&A, didn't give JB&A an opportunity to see the facts, let alone make an

appropriate inquiry and engage in their own due diligence about the errant email situation. A2352-53.

On the morning of May 31, 2011, the Air Force told MCR that it was still investigating whether MCR had violated the PIA. A544-47, 600-04.

Later that same day, MCR executed the Bring-Down Certificate, falsely representing to JB&A that MCR was not subject to any investigations. A2347-48.

Relying on this representation, JB&A closed the sale of the Intelligence Business to MCR. A661-668, 768-69, A232. If MCR had told the truth, JB&A would not have closed and instead would have explored sale opportunities with other buyers. A252-54; A2299-2301, 2314-15.

JB&A received about $42.7 million at closing. Payment of the remaining $19.5 million of earn-out payments depended upon how the Intelligence Business performed in 2011 and 2012. MCR was confident that it would perform quite well. In June 2011, MCR's CFO booked a liability of $17.5 million on its financial statements as an estimate of the amount of the earn-out payments that MCR expected to pay JB&A. A854-857 (MCR CFO O'Brien); A1628, para. 2.

6. On August 23, 2011, the Air Force Suspended MCR for Ethical Misconduct and Began a Criminal Investigation

Two months later, the Air Force suspended MCR from government contracting based on a finding that MCR's handling of its competitor's pricing information violated the Act. A1436-48, Plaintiff's Exhibit (PX) 71. This

suspension barred MCR—and by extension, the Intelligence Business—from accepting *any* new government contracts or assignments. The government also advised MCR of an active federal criminal investigation into its misconduct. *Id*.; TR3001, TR987. The four tainted MCR employees also were suspended. A1439-44. MCR's CEO at the time likely would have been suspended as well if MCR had properly disclosed his involvement in the scheme. TR1346, A1019, 2328.

The Air Force terminated MCR's suspension on September 26, 2011, after MCR admitted that it was guilty of ethical misconduct. Specifically, MCR admitted "its improper conduct, the improper conduct of its employees, and its deficient procedures" in handling the matter that led to the suspension, and conceded that the Air Force had "a legally sufficient case to suspend MCR." A1489-90, 1505.

7. <u>On October 26, 2011, MCR Is Suspended a Second Time for Engaging in a Cover-up</u>

Just a month later, the government suspended MCR *again* when the Air Force discovered that MCR had covered up its misconduct during the original investigation. A1507-14. The cover-up included making false statements in the MCR employee affidavits filed with the Air Force. *Id*.

During its effort to get the second suspension lifted, MCR told the Air Force about the significant negative financial impact the suspensions had on MCR and the Intelligence Business. A1461-76; *see also* A679-681, 1003. In a November

13, 2011 letter to the Air Force, MCR wrote that the Intelligence Business was being "crippled" by the suspensions. A1852-58. MCR also told the Air Force that the suspensions were causing the Intelligence Business to miss the financial targets necessary for JB&A and its ESOP participants to receive their earn-out payments. A1854, 1856-58. MCR said that, because of the suspensions, "JB&A's employees would lose a significant portion of the equity they hold in an Employee Share Ownership Plan, which for many makes up the majority of their retirement savings." A1854.

MCR's second suspension was lifted on November 16, 2011 only after MCR admitted that it was guilty of the alleged misconduct and agreed to remove its CEO. A1520-1600, 734-35, 609-10; *cf.* Br. 10 (claiming that Air Force reimposed suspension "based on an apparent error in reading MCR's affidavits.")

8. <u>MCR's Suspensions Caused Intelligence Business to Miss Financial Targets Necessary for JB&A to Receive Earn-out Payments</u>

MCR's expert admitted that a government suspension has the impact of detonating an "atom bomb" on a government contracting business. A1101. And MCR's suspensions here were no exception. The first suspension "broke" the Intelligence Business, and the second suspension "crushed" it. A243. The suspensions barred the Intelligence Business from bidding on any new contracts, accepting new work, or renewing existing contracts for almost two months during 2011. A1094-98, A685. They caused the Intelligence Business to lose more than

100 employees. A243, 765-66, 1110-13. By the end of 2012, the Intelligence Business had lost almost half of its revenues from 2010. A243.

Even so, the Intelligence Business just barely missed its financial targets for the 2011 payment from MCR. A2514:2-12, TR2035-36, TR4059. Contrary to what it told the Air Force, MCR denied that its suspensions caused the Intelligence Business to miss the financial targets and refused to make *any* of the earn-out payments. Thus, JB&A never received a penny of the $19.5 million of the agreed-upon $62.2 million purchase price for the Intelligence Business.

9. MCR and its Independent Experts Valued the Intelligence Business at $54,687,545 as of the Closing Date

In preparing its 2011 financial statements, MCR management was required to determine the value of the Intelligence Business as of the closing date. MCR valued the Intelligence Business at $54,687,645. A1674-75. In its 2011 audited financial statements, MCR management acknowledged that this figure represented the fair market value of the Intelligence Business as of the May 31, 2011 closing date. A1671-75, A888-91. (CFO O'Brien).

MCR arrived at this value with the assistance of McLean, which provides independent valuation services. A827, A1601-06, A2068-2136. MCR had used McLean in the past for these types of valuations and was pleased with the quality of their work. A825-27, 1055. MCR continues to use McLean for sophisticated valuation work. A826, 1055, 2518-19. And McLean was, of course, intimately

familiar with the Intelligence Business after having served as JB&A's investment banker in the sale to MCR. A749; TR1522-23; A212-214.

McLean prepared a valuation report ("Valuation Report") which valued the Intelligence Business at $54,587,545 on the date of closing. A2068-2136. The Valuation Report references MCR management more than a dozen times as the source of the financial projections and other information used in the valuation. A2072, 2073, 2079, 2082, 2083, 2084, 2096, 2100, 2108, 2118, 2126-27, 2013. ("[b]ased on discussions with management"); A2082 ("the forecast below was based on information provided by management"); A2084 ("close collaboration with management"). A2073.

The Valuation Report also provided a purchase price allocation — that is, an allocation of MCR's purchase price among the various assets that comprised the Intelligence Business. MCR used both the $54,587,545 valuation of the Intelligence Business from the Valuation Report, and the Report's purchase price allocation, in its 2011 Financial Statements.

Aronson, an independent certified public accounting firm, audited MCR's 2011 Financial Statements in accordance with generally accepted auditing principles, which required examining "evidence supporting the amounts and disclosures in the [MCR] financial statements, assessing accounting principles used and significant estimates made by management." A2255. As part of its audit,

Aronson examined the Valuation Report and determined that it was accurate and reasonable. Auditing the Valuation Report effectively required Aronson to understand the Report as well as if Aronson itself had performed the valuation. *See* A1069:12-22. Thus, Aronson confirmed the $54,687,545 value for the Intelligence Business as of the date of closing. A1674-75.

As part of its valuation process, McLean asked MCR to provide probabilities that, prior to the suspensions, the Intelligence Business would have achieved the financial targets necessary to receive the earn-out payments. A1601-06, 2068-2135. MCR concluded that it was **95%** likely that, prior to the suspensions, the Intelligence Business would achieve the revenue and gross margin targets necessary to receive the minimum earn-out payments in 2011 ($4,893,750) and 2012 ($7,703,125). A833-834; A2126, 859, 2131. Thus, if the Intelligence Business had met those minimum thresholds each year, MCR would have been required to pay JB&A a total of $12,596,875. A2068-2135, 2137-38, A880-84.

10. Trial Court Proceedings

A. MCR Held Liable for Breach of Contract and Constructive Fraud

In 2013, JBA filed breach of contract and fraud claims against MCR. There were 21 days of trial and extensive post-trial briefing and argument. *See* A2294-2360 (01/13/2016 court's findings on MCR's liability); A2401-2529 (04/27/2016 - damages); A2539-2572 (05/26/2016 - fees); A2573-2607 (06/10/2016 – fees);

A2628-2694 (09/21/2016 – motion for reconsideration). The trial court ruled that MCR breached the APA because, when it delivered the Bring-Down Certificate to JB&A at the May 31 closing, it falsely represented that it was not under investigation. A2360.

The trial court also held that MCR committed constructive fraud in making this false representation. A2358. The trial court narrowly avoided holding MCR liable for actual fraud, finding MCR's misrepresentations were "colossally negligent" and "colossally stupid." *Id*. The trial court also found that MCR not only made affirmative misrepresentations, but also concealed material information from JB&A by intentionally and deliberately hiding the Air Force investigation and request for affidavits from JB&A:

> MCR, this Court found, engaged in an ***intentional*** course of conduct to cover up their actions, to cover up that they mishandled the errant email as far as the Air Force was concerned, that they were being asked to submit affidavits … This was a callus [sic] and ***deliberate*** pattern of deceitful acts that took place over a period of time, really truly culminated on May 31st

A2582, 2674 (emphasis added); A2353: 3-7, 2674.

Despite these findings, the trial court decided not to hold MCR liable for actual fraud, understanding that such a ruling would have a devastating impact to MCR's business as a government contractor**.** TR 12/17/15 Closing Argument at 38. (trial court noting "there are lives and businesses at stake").

B. JB&A Awarded Compensatory Damages of $11,995,002 and Prejudgment Interest

The trial court found MCR caused damages of $11,995,002, the difference between the value of JB&A's Intelligence Business on May 31, 2011 ($54,687,545) and the amount that MCR actually paid for that business ($42,692,543). A2512-22, A2529, A2695-96, A2326-30, A2347-58, A237-38. The trial court noted that it could have computed damages using a $60 million value for the Intelligence Business based on the testimony of JB&A's founder. A2515: 5-13. ("It's credible, it's uncontradicted. It would put JB&A in the same position they would have been in but for the fraud.") *see also*, A749. But the Court used the "more conservative" figure of $54,687,545—based on *MCR's own valuation* of the Intelligence Business—noting it had been validated by two independent experts, McLean and Aronson. A2515. The trial court cited MCR's damages expert who testified that the Valuation Report methodology was "accurate and appropriate" and "sound." *Id.* A1071.

The court also relied on the testimony of MCR's CFO who admitted at trial that $54,687,545 was the fair market value of the Intelligence Business at closing:

> Q: So the summary of $54,681,000 [sic] represents the purchase price for essentially an arms-length transaction between a willing buyer and willing seller as of May 2011 date, right?
>
> A: Correct.

A876; *see also* A 864-75, 2517-18 (discussion by the court).

The amount of the court's damage award was also supported by JB&A's expert, who opined that the Valuation Report and Aronson provided a high degree of reliability. A933, 936-37, 941, 943. The court awarded JB&A $3.7 million in prejudgment interest on the breach of contract claim under Delaware law. A2595, 2695-99.

C. <u>The Court Awarded Attorney's Fees of $1,894,484</u>

The trial court awarded JB&A $1,894,484 in legal fees based on JB&A's fraud claim under *Prospect Development v. Bershader* 258 Va 75 (1999). The court relied on its finding that "MCR engaged in callous, deliberate and deceitful acts which constituted a continuing pattern of fraudulent conduct…." A2586-92, 2695-99. It found that MCR's deceitful conduct included: (i) ignoring its own attorney's advice to remove the tainted employees, thereby intentionally violating federal ethics laws; (ii) covering up its ethics violations and hiding facts from Air Force such as its CEO's involvement; (iii) providing inaccurate affidavits to the Air Force; (iv) making false representations to JB&A at closing; and (v) intentionally concealing the Air Force investigation from JB&A. The court described MCR's conduct as "almost sinister." A2324, 2320-38, 2343-44, 2353-59, 2303-11, 2674.

The court also condemned MCR's trial conduct—"having witnesses come into this court and give what clearly proved to be false and misleading testimony."

A2588:18-20. It concluded that a senior member of MCR management, who had submitted the false affidavits to the Air Force, was "lying on the stand." A2306:11-2307:20, A2321. The trial court also cited numerous, other specific instances where MCR officers gave false or misleading testimony at trial, including:

- MCR Vice-Chairman and former CEO Neil Albert was "not credible" on certain crucial facts and "not truthful" on others; his testimony reflected that "his truth is expedient… [h]is truth is whatever is needed to get the intended result." A2347:4, 2349:4-5, 2357:13-17.

- MCR Chairman Michael Galvin gave "rehearsed and contrived speeches" and "spoke out of both sides of his mouth" as he tried to deny admissions made in his letters to the Air Force, and attempted to "recant" other testimony. A2310:2-7, 2312:6; and

- MCR President Vincent Kiernan had "a selective memory, very spotty. He couldn't remember conversation that he had participated in, he couldn't remember documents he had written, he couldn't remember documents he had seen or sent, he couldn't remember his deposition testimony. And this is even though he's the designee. He's the designee and he doesn't review anything for his testimony." A2333-34.

ARGUMENT

I. THE TRIAL COURT PROPERLY FOUND THAT MCR FRAUDULENTLY INDUCED JB&A'S PERFORMANCE OF AN EXECUTORY CONTRACT (ASSIGNMENT OF ERROR 1)

STANDARD OF REVIEW

This Court will review the trial court's judgment for clear error and will not set it aside unless it is plainly wrong or there is no evidence to support it. *Gov't Emps. Ins. Co. v. United Servs. Auto. Ass'n*, 281 Va. 647, 655 (2011). It will consider the evidence and all reasonable inferences fairly drawn from it in the light most favorable to JB&A, the prevailing party below. *Id*. It reviews questions of law *de novo*. *Id.*

DISCUSSION

The trial court's decision to hold MCR liable for the fraudulent inducement of the performance of an executory contract is consistent with a line of this Court's cases spanning almost fifty years. This includes *Ware v. Scott*, 220 Va. 317, 321 (1979); *Horner v. Ahern*, 207 Va. 860, 867 (1967); *Devine v. Buki*, 289 Va. 162, 175 (2015); *Modern Oil Corp. v. Cannady*, No. 141839, 2015 WL 10990113, at *2 (Va. Dec. 30, 2015).

In *Ware,* the buyers entered into a contract with the sellers to purchase a house, at which time the sellers represented that the house had no water problems. 220 Va. at 318. Between signing and closing, a flood damaged the house. *Id.* at

319. The sellers never disclosed this damage; the buyers found out over a year later. *Id.* This Court held that the sellers' failure to disclose that their residence was damaged by flooding constituted fraudulent inducement. *Id.* at 320. It explained that "performance of an executory contract may be fraudulently induced. Such is the case when one party fraudulently leads the other to believe that a condition precedent to the latter's duty to perform has been fulfilled. . . ." *Id*. at 320. In support, the Court cited the Restatement (Second) of Torts, § 551 (1977):

> One party to a business transaction is under a duty to exercise reasonable care to disclose to the other before the transaction is consummated…. subsequently acquired information that he knows will make untrue or misleading a previous representation that when made was true or believed to be so.

Id. at n.2.

The same principles apply here. MCR failed in its common law duty to disclose subsequently-acquired information, the Air Force investigation, which rendered its previous representation to JB&A untrue. To make matters worse, MCR affirmatively represented in the Certificate that there was no investigation when MCR knew this was false, and would induce JB&A's performance under the APA.

MCR insists that, because it signed the APA with JB&A, it cannot be held liable for fraudulent inducement, citing *Richmond Metro Auth. v. McDevitt St. Bovis, Inc.,* 256 Va. 553 (1998) and *Dunn Constr. Co. v. Cloney,* 278 Va. 260

(2009). Br. 17-22. In both cases, this Court held that a plaintiff could not bring a fraud claim where the misrepresentations related to the defendant's performance of construction services under a contract.

The defendants in *Dunn* and *McDevitt* were builders. In each case, the builder had a "duty" under a contract to perform the construction services and could be held liable by the customer if it failed to perform the construction services properly. *Dunn* at 268; *McDevitt* at 559. And in each case, the alleged misrepresentation in each case occurred in connection with or already "related to" the builder's duty to perform those construction services. *Dunn* at 268; *McDevitt* at 559. Because the source of the duty to perform the services was the builder's contract, this Court held that there was no cause of action for fraud in either case. *Dunn* at 267; *McDevitt* at 557.

MCR's reliance on *Dunn* and *McDevitt* is misplaced. The APA was an executory contract. It contained certain conditions precedent to be satisfied by each party before the other party had the duty to close the transaction. Providing the Bring-Down Certificate was one of those conditions precedent to JB&A's performance. APA § 5.3; A1228. But MCR was under no duty to provide the Bring-Down Certificate or close the transaction. MCR had no liability to JB&A if it failed or was unable to provide the Certificate because intervening facts (*i.e.*, the

Air Force investigation) had rendered its prior representations untrue.[3] Rather, under the APA, the failure to provide the Certificate would simply excuse JB&A's obligation to close the sale with no liability to MCR. APA § 6.2. A1229; *see TravelCenters of Am. LLC v. Brog*, 2008 Del. Ch. LEXIS 183, *9-10 ("…the non-occurrence of a condition is not considered a breach unless the party promised that the condition would occur."). *See also Smith v. McGregor*, 237 Va. 66, 75-6 (1989) (where a contract's condition precedent is not satisfied, "the contract bec[omes] void relieving the parties of their obligations under it.").

MCR does not — and cannot — point to any provision in the APA which obligated it to provide the Bring-Down Certificate. Nor did MCR provide the Certificate in connection with or relating to the performance of some other duty required of MRC under the APA.[4] As the trial court concluded, the APA incorporated "conditions precedent to each party becoming obligated to close the sale transaction" and "those condition precedents required truthfulness." November 15, 2013 hearing record at 102. This common law duty to tell the truth and not conceal material facts is the source of JB&A's fraud claim. Restatement (Second) of Torts §§ 526; 551 (1977).

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[3] *See* Lou R. King & Eileen T. Nugent *Negotiated Acquisitions of Companies, Subsidiaries and Divisions* § 14.02 [6] at 14-16 (2016); J. Freund, *Anatomy of Merger Strategies and Techniques for Negotiating Acquisitions* 158-59 (1975).

[4] Even if such a provision existed, having previously represented it was not under investigation, MCR still had a common law duty to disclose the investigation to JB&A. Restatement (Second) of Torts § 556 (c) (1977).

In an effort to distinguish the *Ware* line of cases, MCR asserts that JBA's fraud claim was extinguished once MCR submitted the Bring-Down Certificate. MCR argues that MCR's "specific contractual warranty that MCR provided in the Bring-Down Certificate….displaces any cause of action for fraud." Br. 19. Under this "displacement theory," the trial court's finding that MCR's misrepresentation constituted a breach of contract apparently means that MCR's tort liability also was extinguished. According to MCR, the plaintiff's contract in *Ware* and *Devine*, unlike the APA, contained no warranty upon which the plaintiff could sue for breach of contract.

This theory finds no support in Virginia law. It is well-settled that a single act can support damage awards based on breach of contract and tort. *See e.g., Abi-Najm v. Concord Condo, LLC,* 280 Va. 350, 361 (2010). It is equally well-established that a plaintiff who is fraudulently induced into entering or performing a contract can sue for fraud, notwithstanding the contractual relationship with the defendant or the terms of the contract. *George Robberecht Seafood, Inc. v. Maitland Bros.*, 220 Va. 109, 112 (1979); *House v. Kirby* 233 Va. 197, 200-201 (1987) ("…. character of fraud is not changed from tort to contract merely because the parties are also engaged in a contractual relationship."); *Packard Norfolk v. Miller*, 198 Va. 557, 565, 95 E.E.2d 207, 213 (1956) ("warranty stands no higher than the contract which is vitiated by the fraud"); *Horner, supra*.

This Court's holding in *Horner* is particularly instructive. There, a purchaser entered a contract to buy a house. The contract required the seller to provide a termite certificate, and "relieved [the purchaser] of the conditions of this contract" if termite damage was found. *Horner*, 207 Va. at 862. The house suffered from extensive termite damage. Even so, after the date of the contract, but before closing, the seller provided a certificate reporting no such damage. When the buyers discovered the termite damage after closing, they brought an action for fraud. *Id.* at 863. The trial court sustained the defendants' demurrers. *Id*. at 861.

On appeal, this Court reversed. It held that the action sounded in tort, not contract *Id.* at 867. The *Horner* Court explained that "[i]f the plaintiffs' allegations be true, it was because of defendants' fraud that the knowledge of the termite damage was kept from the plaintiffs, thus preventing them from using the escape clause prior to settlement." *Id.* The Court also rejected the sellers' argument that the buyers could not sue for monetary damages because the contract had a provision which limited their remedy to rescission:

> It was, allegedly, because of the defendants' fraud that the plaintiffs had satisfied the conditions imposed upon them by the contract before they discovered the fraud. To say under these circumstances that the plaintiffs have no right to elect to bring an action for damages would, in effect, permit the defendants to set up their own fraud as a defense. This they cannot do.

207 Va. at 867.

MCR also tries to distinguish the *Ware* line by arguing that those cases involve "active concealment of material information," while MCR was guilty of no "intentional wrongdoing." Br. 20. As a factual matter, this is incorrect. The trial court found MCR guilty of both active concealment and intentional wrongdoing. As a legal matter, whether an act of fraud involves active concealment or intentional wrongdoing is irrelevant in determining a party's liability for fraudulent inducement. *Packard Norfolk v. Miller,* 198 Va. 557, 561 (1956).

Finally, having failed to distinguish its case from *Ware et al.* on factual or legal grounds, MCR requests that this Court's prior fraud rulings not be extended to "sophisticated corporations, each represented by experienced counsel." Br. at 21. In effect, MCR asks that the Court sanction fraud involving executory contracts in commercial transactions, creating a safe haven for such fraudulent business conduct. Also, MCR's request overlooks the fact that the real victims of MCR's fraud are JB&A's employees who, as MCR admitted to the Air Force, stand to lose a significant portion of their retirement savings.

MCR's request should be denied. This Court in *Ware et al.* recognized that contracts such as the APA are structured to allow both parties to walk away unharmed when unanticipated events or conditions occur, eliminating potential litigation. This is exactly what would have happened here if MCR had told the truth. Having failed to do so, MCR should be held accountable.

II. THE TRIAL COURT'S AWARD OF COMPENSATORY DAMAGES IS SUPPORTED BY ABUNDANT, RELIABLE EVIDENCE (ASSIGNMENT OF ERRORS 2 AND 3)

STANDARD OF REVIEW

Following a bench trial, the trial court's findings of fact are viewed in the light most favorable to the prevailing party and will not be disturbed unless "plainly wrong or without evidence to support it." *Preferred Sys. Sols., Inc. v. GP Consulting, LLC*, 284 Va. 382, 394 (2012) (citation omitted). This is the standard under Delaware law as well. *Bank of N.Y. Mellon Trust Co., N.A. v. Liberty Media Corp.*, 29 A.3d 225, 236 (Del. 2011)("Where there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous.").

DISCUSSION

The trial court found that, but for MCR's false representations in the Certificate, JB&A would not have closed the sale and transferred the Intelligence Business to MCR. A2300-01. Instead, JB&A would have sold the business to another buyer. A252-54, 2299-2309, 2314-15. The trial court found that MCR's misrepresentations caused JB&A damages of $11,995,002, the difference between the fair market value of the Intelligence Business at closing and the amount actually paid by MCR. A2512-2522, 2529, 2695-96, A2326-30, 2347-48, 2358, 2337-38. *See Prospect Dev. Co., Inc. v. Bershader*, 258 Va. 75, 91 (1999); *Duncan v. Theratx, Inc.*, 775 A.2d 1019, 1022 (Del. 2001).

MCR does not challenge the trial court's holding that its false representations caused JB&A to sell the Intelligence Business to MCR. Nor does MCR dispute that the trial court used an appropriate standard to measure JB&A's damages. Instead, MCR appeals the amount of JB&A's damages, primarily by challenging the trial court's factual finding that Intelligence Business had a value of $54,687,545 at closing.

Two of MCR's Assignments of Error (Assignments 2 and 3) arise from the trial court's factual finding regarding this $54,687,545 value, one based on "causation" and the other based on the amount of damages awarded. However, these two Assignments, and MCR's arguments in support thereof, are largely redundant. If the value of the Intelligence Business exceeded what MCR paid at closing, then MCR caused damages by making false representations that induced JB&A to close. *Bershader* at 91. A2512-22, 2529, 2695-96, 2337-38, 2347-58, A252-54. Thus, whether MCR caused damages, and the amount of such damages, depends primarily upon the value of the Intelligence Business at closing.

But the trial court's award of damages was based on MCR's own contemporaneous valuation, as validated by two independent experts at that time. The damage award was further supported by the testimony of MCR's employees and expert at trial, as well as the testimony of JB&A's employees and expert.

Given this evidence, and the trial's court's meticulous credibility rulings, MCR offers no grounds on which JB&A's damage award can be disturbed.

A. The Court Reasonably Relied on MCR's Own Valuation to Ascertain JB&A's Fair Market Value at the Time of the Closing

A person who has been defrauded in the sale of property is entitled to damages equal to the difference between the actual value of the property at the time the contract was made and what the fraud victim actually received in the transaction. *Bershader*, 258 Va. at 91; *Klaiber v. Free Mason Assocs., Inc.*, 266 Va. 478, 486 (2003) (measure of damages is the difference between the value of the item bargained for and the value of the item actually received); *Duncan* at 1022 (damages equal to difference between market price and deemed sale price). In *Bershader*, the Court cited with approval Section 549 of the Restatement (Second) of Torts.[5] 258 Va. at 91. The comments to that section state:

> In a sales or exchange transaction the loss for which the recipient of a fraudulent misrepresentation is entitled to recover is usually the difference between the price paid or the value of the thing given in exchange and the value of the thing acquired. **The value of the article is normally determined by the price at which it could be resold in an open market or by private sale…**

Comment C (emphasis added).

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[5] While Section 549 addresses damages for actual fraud, Section 552B of the Restatement (Second) of Torts adopts the same measure of damages for negligent misrepresentations (*i.e.*, constructive fraud). Section 552B incorporates by reference Comments a to f from Section 549 of the Restatement (Second) of Torts. § 552B cmt. a.

In its financial statements, MCR reported that the "fair value" of the Intelligence Business was $54,687,545. A1674-75. MCR management approved and verified these financial statements and the $54,687,545 value. A1671-73. This figure comes from the Valuation Report, which explains that "fair value" means "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." A2072.

The trial court reasonably used this figure as a measure of JB&A's damages because the valuation had a high degree of reliability. Two independent experts selected *by MCR* — a valuation firm and an accounting firm — validated the $54,687,545 figure prior to this litigation, when MCR did not have a motive to undervalue JB&A's business. A2517-20; 1674-75, 2137-74, 2068-2139, 2528-29. At trial, MCR's own damages expert testified that the methodology used in the Valuation Report was correct. A2522. And MCR's CFO testified unequivocally that $54,687,545 represented the purchase price for the Intelligence Business in an arms-length transaction as of the closing date. A876.

The trial court's approach is consistent with Virginia law which has "defined the fair market value of a property as its sale price when offered for sale by one who desires, but is not obliged, to sell it, and is bought by one who is under no necessity of having it." *Keswick Club, L.P. v. County of Albemarle,* 273 Va. 128, 136, (2007) (quoting *Tuckahoe Woman's Club v. City of Richmond,* 199 Va. 734,

737, (1958). *See also Seafood Assoc. v. Bd. of Assessment Rev.*, 539A. 2d 1045, 1048 (Del. 1985) (defining fair market value as "the price which would be agreed upon by a willing seller and a willing buyer, under ordinary circumstances, neither party being under any compulsion to buy or sell.").

Using $54,687,545 was therefore a reasonably certain measure of the fair market value of the Intelligence Business as of the closing date. But MCR paid JB&A only $42,692,543 for the Intelligence Business. JB&A would not have sold the Intelligence Business to MCR absent MCR's false representations and concealment of the Air Force investigation. JB&A thus suffered damages of $11,995,002 as a proximate result of MCR's fraud and breach of contract. The trial court was justified in awarding that amount of damages.

MCR now complains that the Valuation Report was based on financial projections from JB&A that were "highly speculative and unduly optimistic," "presenting an unduly rosy picture of JB&A's business prospects." Br. at 32-33. Not so. The financial information in the JB&A's projections is materially different from the financial information in Valuation Report – different revenue numbers, different time periods, different gross margins and different earnings. A2521-22, 2084, 2126-27, 1890. Moreover, the record makes clear that MCR provided the financial information incorporated in the Valuation Report. The Valuation Report itself cites MCR management as the source of information more than a dozen

times. *see e.g.,* A2073, 2082-84, 2127. MCR'S CFO confirmed at trial that MCR management was the source of the financial information for the Valuation Report. A850: 8-11. And the trial court itself found that there was "no basis for MCR's claim" that the Valuation Report was somehow based on projections provided by JB&A. A2521-22.

MCR now tries to dismiss its own pre-litigation valuation of the Intelligence Business as merely a "speculative accounting entry." Br. 36. In fact, MCR was highly motivated to make sure that its valuation of the Intelligence Business was accurate. The valuation was used in MCR's 2011 and 2012 annual financial statements, which were delivered to its investors, board of directors, and bank. At the end of Aronson's audit of the 2011 financial statements, two MCR officers and the chair of MCR's audit committee signed a letter attesting to their belief that MCR's purchase price allocation based on the Valuation Report was "reasonably recorded." A1671-73. Financial statements are used to prepare tax returns, which an MCR officer would have signed under penalty of perjury. And as a government contractor, MCR was also required to deliver the financial statements to its federal government customers as evidence of its financial ability to perform.

MCR also claims that JB&A's reliance on the $54,687,545 valuation is incorrect because the Valuation Report's calculations "projected the performance of JB&A's business *as part of MCR*." Br. 28 (emphasis in original). This argument

is mistaken for several reasons. *First*, the projected revenue and expense numbers of the Intelligence Business are shown in the Valuation Report on a stand-alone basis. A2084. *Second,* the Valuation Report specifically states that the projections on which the valuation was based do "not include buyer [MCR] specific synergies." A2082; c*f.* Br. 8 (claiming valuation based on "synergies and strategic value to MCR"). *Third,* McLean prepared the valuation in accordance with ASC 820-10-35-2, which defines "value" as the price that would be received to sell an asset in an orderly transaction between "market participants." A2072, n.3. For purposes of ASC 820-10-35-2, as then in effect, "market participants" are unrelated or independent of the reporting entity[6]. Thus, contrary to MCR's assertion, the $54,687,545 value represents what a willing buyer **other than MCR** would pay for the Intelligence Business.

MCR also argues that the ESOP valuation of JB&A stock as of December 31, 2010 demonstrates that the value of the Intelligence Business was less than $54,687,545. Br. 32. By definition, an ESOP valuation of JB&A's stock does not represent the price at which the Intelligence Business could be sold in an arms-length sale to a third-party purchaser. The ESOP valuation explicitly states that its "estimate of value may not reflect the value that the Company may receive if it

[6] ASC-820-10-35-2 is part of the Accounting Standards Codification ("ASC"), which is the source of authoritative generally accepted accounting ("GAAP") principles published by the Financial Accounting Standards Board.

were sold in the current market place to a strategic buyer under competitive circumstances." A1995**.** Even MCR's own expert testified that the ESOP valuation did not represent the arms-length value for the Intelligence Business. A1077-78.[7] Thus, the trial court permissibly determined that there was more reliable evidence than the ESOP valuation in determining JB&A's fraud damages. A2917-20, 2528-29.

MCR insists that the Valuation Report was "legally insufficient" to support a damages award because there were no potential buyers other than MCR, citing *SunTrust Bank v. Farrar*, 277 Va. 546 (2009). Br. 30. In *Farrar*, the beneficiaries of a trust sued a trustee for breach of fiduciary duty for failing to sell property with a coal mine twenty years earlier when the trustee had obtained an appraisal of $1.1 million for property. At the time of the appraisal, there was a "declining coal market" and the mine was producing little or no income. *Id.* at 552. Also, an actual sale of the property was "not feasible" because it was subject to a lease. *Id.* at 552. The appraiser at trial could not recall whether he took the lease into account in valuing the property. *Id*. The earliest evidence of a willing buyer for the property was five years later, when there was an offer of $75,000. Based on these facts, this Court overturned a damages award of $1.1 million because the valuation was based

[7] This certainly was JB&A's understanding. When questioned whether JB&A anticipated selling the company for the amount of the valuation, JB&A's President at the time explained "[i]t had no relationship to a potential sale price or sale value. That was not the purpose of the valuation." A816: 3-7; *see also* A221.

on "unsupported projections" and there was no evidence of "a willing buyer or a viable market for the property at the appraised price." *Id* at 555.

Here, by contrast, market conditions were favorable for a sale. A749, A221. Unlike the property in *Farrar*, there was no encumbrance that prevented a sale of the Intelligence Business. The financial projections on which the Valuation Report was based were not "unsupported projections". *Id* at 555. Rather, the Intelligence Business had a 23-year history of growth in revenues prior to the sale, generating millions of dollars of earnings each year. *Commercial Business Systems v. Bell South*, 249 Va. 39, 50 (1995) (past business records providing evidence for "intelligent and probable estimate of damages"). The valuation was supported by JB&A's past performance, MCR's rigorous due diligence of that performance, and MCR's detailed projections regarding future performance of the Intelligence Business.

As to MCR's argument about the absence of a willing buyer, MCR need only look in the mirror — MCR itself agreed to pay $62.2 million — a price that substantially exceeded the value for the Intelligence Business in the Valuation Report. JB&A and its investment banker identified more than sixty other potential buyers. A1946-49, 1991-2055. JB&A was on the market for only a few months[8]

[8] This can hardly be considered an "exhaustive" marketing period for the sale of a $60 million business. In many parts of Virginia, it takes longer than that to sell a house.

before it signed an exclusivity agreement with MCR which precluded JB&A from discussing a sale with any other buyers. A1676-82; TR356. If the MCR deal did not close, JB&A could have approached these or other potential buyers. A252-54. And having served as JB&A's investment banker, McLean knew all the details of JB&A's sale process when it arrived at its valuation.

If there was any doubt as to the validity of the methodology used to value the Valuation Report, it was eliminated by MCR's expert at trial. Not only did MCR's expert testify that the methodology used in the Valuation Report was "sound and "appropriate", she used the same methodology in her own attempt to value the Intelligence Business.[9] A1071, A2527, TR3887, TR3899, TR3896, TR4102.

B. Substantial Evidence on the Lost Earn-Out Payments Supports The Trial Court's Damage Award

Under the APA, JB&A would have received up to $19.5 million in earn-out payments if the Intelligence Business met certain financial targets in 2011 and 2012. The trial record contains ample evidence that, absent MCR's suspensions, the Intelligence Business would have hit those targets. This corroborates the trial court's damages finding.

[9] The trial court disregarded the MCR expert's calculation of JB&A's damages, however, because her assumptions were incredible, she made a "multimillion dollar error" in her computations, and "she admitted to having made several significant errors during her testimony." A 2522-24, 2586.

Before the suspensions, MCR booked a liability of $17.5 million on its financial statements as an estimate of the amount of the earn-out payments that it expected to pay JB&A. A854-57; A1628. In November 2011, MCR admitted to the Air Force that JB&A was on track to receive those earn-out payments. In early 2012, MCR management assigned a probability of **95%** that, prior to its suspension, JB&A would achieve financial targets necessary to receive the minimum earn-out payment in 2011 and 2012. A859, 877-79; A2126-33. John Knight, then MCR's Senior Vice-President in charge of the Intelligence Business in 2011 and 2012, testified that the Intelligence Business would have hit at least the first levels of the earn-outs for both years, and identified specific lost opportunities due to the suspensions, A2056, A758, 760, 773-93. The trial judge found this testimony credible. A2334, 2313.

The actual performance of the Intelligence Business in 2011, further corroborates that JB&A would have received the earn-out payments. As the trial court observed, despite the loss of existing contracts and new business because of the suspensions, the Intelligence Business barely missed the revenue threshold for a 2011 earn-out payment. A2514.

Based on the forgoing, the trial court could have awarded JB&A damages based on the likelihood the Intelligence Business would have met the earn-out targets. If the Intelligence Business met the minimum targets, JB&A would have

received $12.7 million in payments. But, because MCR's ethical misconduct destroyed the Intelligence Business, the court felt that it was a challenge to project the precise amount of expected earn-out payments. A2507-15. Because MCR's own valuation of the Intelligence Business had such a high degree of reliability, the trial court chose to use the difference between the value of the Intelligence Business and what MCR actually paid to measure JB&A's damages. Even so, evidence supporting a $12.7 million value for the lost earn-outs shows that the trial court's award of $11,995,002 in damages was eminently reasonable.

MCR incorrectly claims that JB&A abandoned its argument for damages based on the lost earn-out payments. Br. 25 (citing A2495, 2507). MCR's record citations concern JB&A's breach-of-contract claim under section 1.9 of the APA relating to MCR's duty to run the business properly after the sale—a claim the trial court found unnecessary to address. A2360, 2506-07. JB&A always maintained that at the time of the breach and fraud, there was substantial evidence that JB&A was reasonably likely to hit the earn-out target and should receive compensatory damages on that basis. The briefs filed on this specific issue of damages reflect this. JB&A Damages Br. 02/08/16; Reply Br. 2/23/16.

The record thus contains ample evidence to support the trial court's damages award: MCR's contemporaneous valuation, its validation by two independent experts, testimony from MCR's employees, JBA's expert and MCR's trial expert.

Even so, MCR protests that the damage award is too "speculative". Br. at 37. But, this Court has instructed that "one whose wrongful conduct has rendered difficult the ascertainment of the precise damages suffered by the plaintiff is not entitled to complain that they cannot be measured with the exactness and precision that would otherwise be possible." *Washington Golf & Country Club, Inc. v. Briggs and Brennan Developers, Inc.,* 198 Va. 586, 592 (1956); *see also Beard Research, Inc. v. Kates,* 8 A.3d 573, 613 (Del. Ch.), *aff'd sub nom. ASDI, Inc. v. Beard Research, Inc*., 11 A.3d 749 (Del. 2010) ("Public policy has led Delaware courts to show a general willingness to make a wrongdoer 'bear the risk of uncertainty of a damages calculation where the calculation *cannot* be mathematically proven.") This admonition certainly applies to MCR here.

Finally, MCR's concern that JB&A will receive some sort of "windfall" is misplaced. Br. at 44. The trial court noted that, for purposes of computing JB&A's damages, it could have valued the business at $60 million based on the testimony of JB&A's founder. A2515 ("It's credible, it's uncontradicted. It would put JB&A in the position that they would have been in but for the fraud."). But the trial court decided instead to use "more conservative" amount from MCR's own valuation. *Id; see also*, A749 (Knight). Even with the damages award, MCR will pay JB&A substantially less than the $62.2 million agreed-upon purchase price for the Intelligence Business. This multi-million shortfall will be borne by the retirement

accounts of the ESOP beneficiaries. If anyone is walking away from this litigation with a windfall, it is MCR.

III. THE TRIAL COURT DID NOT ABUSE ITS DISCRETION IN AWARDING ATTORNEY'S FEES (ASSIGNMENT OF ERROR 4)

STANDARD OF REVIEW

The trial court's award of attorney's fees is reviewed for an abuse of discretion. *Bershader*, 258 Va. at 92. The trial court's determination that the damages, prejudgment interest, and attorney's fees awards were not duplicative and that no election of remedies was required is reviewed *de novo*. *Wilkins v. Peninsula Motor Cars, Inc.*, 266 Va. 558, 560 (2003).

DISCUSSION

In a fraud suit, a court may award attorneys' fees to the defrauded party. *Bershader,* 258 Va. at 92. *Bershader* shows how this rules works. There, the defendants engaged in actual and constructive fraud in the sale of property to the plaintiffs. *Id*. at 85. This Court articulated two factors in awarding attorney's fees to the purchaser. First, the Court found that the defendants had engaged in a "pattern of misconduct" involving "callous deliberate deceitful acts" not only with the plaintiffs but with other purchasers of property. *Id.; see also Carlson v. Wells*, 281 Va. at 189, *citing Bershader,* 258 Va. at 92–93, (finding attorney's fees award appropriate where facts were sufficient to establish a "pattern of misconduct" and "specifically a pervasive, wanton dereliction of duties….").

Second, the *Bershader* Court found the defendants' scorched earth litigation tactics warranted the award of attorneys' fees, noting:

> It was a global, comprehensive, all inclusive-basically defend everything and deny everything. And I'm not by saying that faulting the attorneys. That was the position taken by the defendants themselves.... It did take an enormous amount of effort by the complainants to prove their case in this situation.

258 Va. 75 at 93.

These factors both are present here. MCR engaged in a "pattern of misconduct," including (i) ignoring its own attorney's advice and intentionally violating federal ethics laws; (ii) covering up its ethics violations by hiding facts from the Air Force and providing false affidavits; (iii) making false representations to JB&A at closing; and (iv) intentionally concealing the Air Force investigation from JB&A. MCR's pattern of misconduct was not only deliberate and deceitful; it was, as the court observed, "almost sinister." A2324:3.

MCR also repeatedly engaged in trial tactics designed to intimidate and discourage JB&A and the ESOP participants by making it prohibitively expensive to bring their claims. For example, MCR filed a meritless counterclaim against JB&A alleging that JB&A had committed fraud by providing false projections. MCR filed this claim—even though MCR's officers testified that they were not misled by JB&A and that they never relied on the projections. A2318, 19, 26, 29.

And multiple MCR witnesses contradicted or recanted their own testimony, or gave untruthful testimony at trial. A2310, 2312, 2333-34, 2347, 2349, 2357.

MCR does not and cannot dispute the trial court's holding that its actions constituted a "pattern of misconduct" involving "callous, deliberate deceitful acts" within the meaning of *Bershader*. Rather, MCR asks that this Court to sanction its deceitful conduct by narrowing its holding in *Bershader*. The request should be declined.

A. <u>The Trial Court had Authority under *Bershader* to Award Attorney's Fees</u>

MCR argues that a court may only award attorney's fees under *Bershader* when it sits as a court of equity. Even if one accepts MCR's argument (which JB&A does not), this condition is satisfied here because the trial court explicitly ruled that it was sitting is equity on JB&A's fraud claim and invoking its power of equitable relief to award JB&A attorney's fees. A2575-2588, 2653-59, 2676. MCR asserts that the trial court could not sit as a court of equity because JB&A sought only monetary damages on its fraud claim. It is well-established, however, that an award of monetary damages on a fraud can be a form of equitable relief. *Millboro Co. v. Augusta Corp.*, 140 Va. 409, 421 (1924) (monetary award in lieu of restoration of the property upon rescission of contract).

MCR also ignores that JB&A's complaint specifically sought attorney's fees in its prayer for relief. Amended Second Amended Complaint, Counts 3 and 4, and Prayer For Relief. If one accepts MCR's argument that the award of attorney's fees is a form of equitable relief, then JB&A invoked the trial court's equity jurisdiction by seeking them. The fact that the trial court also may have considered legal claims does not preclude it from ruling on JB&A's claim for equitable relief in the form of attorney's fees. Va. Sup. Ct. R. 3:1; Va. Sup. Ct. R. 1:4(k).

More importantly, neither *Bershader* nor any of this Court's subsequent decisions applying *Bershader* expressly condition the award of legal fees on a court's invocation of its power of equitable relief. *See e.g., Devine,* 289 Va. at 178; *Carlson* 281 Va. at 109. For this reason, state and federal courts alike have almost uniformly applied *Bershader* where the plaintiff sought only monetary relief on legal claims. *See, e.g., Melnor, Inc. v. SKR Res., Inc.,* No. CIV.A. 5:04CV00113, 2006 WL 1518848, at *1 (W.D. Va. May 24, 2006); *Doddy v. Zedd Auctioneers, Ltd.,* 77 Va. Cir. 272 (2008); *Glaser v. Hagen,* No. 114CV1726LMBIDD, 2016 WL 521454, at *3 (E.D. Va. Feb. 5, 2016).[10] The only outlier is a circuit court decision, *Oswald v. Holtzman*, 90 Va. Cir. 9 (2015).

[10]*See also Rambus, Inc. v. Infineon Techs. AG*, 155 F. Supp. 2d 668, 690 (E.D. Va. 2001), *rev'd in part, vacated in part,* 318 F.3d 1081 (Fed. Cir. 2003) (reversing a fraud award because defendant had not breached a duty owed to plaintiff); *Grp. Ins. Concepts, Inc. v. Visium Sols. Corp*., 61 Va. Cir. 110 (2003) ("[C]ase law suggests that attorney fees are allowed in a law case involving fraud.").

Bershader has been on the books for almost 20 years. The General Assembly has not seen fit to overrule it. MCR suggests no compelling policy reason to overrule this consensus reading.

Instead, MCR tells the Court that its behaviour represents "no special circumstances" justifying an award of attorney's fees. Br. at 41. MCR's "sinister" behaviour and deceitful conduct included baseless counterclaims and multiple witnesses providing false testimony at trial. This case has required JB&A to expend millions in legal fees, paid mostly with funds which had been earmarked for the retirement accounts of JBA's employees. The trial court's award did not make JB&A whole on its legal expenses. The award excludes, for example, fees incurred in the defense of MCR's meritless counterclaims. Feb. 8, 2016 Declaration by David Barger in Support of Fees, attached to JB&A's Brief on Damages and Fees, February 8, 2015. There is no "windfall" here. Br. at 41.

The trial court's award of attorney's fees was fair, and it fits squarely within this Court's criteria under *Bershader*. It should be affirmed.

B. <u>Legal Fees May Be Awarded on Constructive Fraud Claims</u>

MCR also attempts to avoid its liability for attorney's fees because it was held liable for constructive, not actual fraud. This is irrelevant, as Virginia courts have awarded attorney's fees in cases not involving actual fraud.

In *Carlson*, for example, this Court approved an award of attorney's fees based on the trial court's findings that the defendants had "callously disregarded their custodial obligations" and were guilty of a "pervasive, wanton dereliction of the duties "imposed on them as custodians." *Carlson* at 189-90. The defendants, a father and uncle, were not held liable for fraud, but were found liable for violating "a duty to the [children] to use reasonable care and skill" in handling certain custodial accounts. *Id.* at 182. This duty is not materially different than the duty imposed on MCR not to commit constructive fraud. *See also Tauber v. Com. ex rel. Kilgore*, 263 Va. 520, 547(2002) ("a longstanding course of self-dealing … would have supported an award of attorney's fees.").[11]

What is more, this Court can affirm the trial court's judgment for any reason appearing in the record. *Miller & Rhoads Bldg., LLC v. City of Richmond* 292 Va. 537, 542 (2016). Here, the record supports a finding that MCR committed actual fraud, rendering its line of argument here irrelevant.

Constructive fraud differs from actual fraud in that the misrepresentation of material fact is not made with the intent to mislead, but is made innocently or negligently. *Kitchen v. Throckmorton,* 223 Va. 164, 171 (1982). A defendant also can be held liable for actual fraud for "affirmative misrepresentations made

[11] Under Virginia law, a fiduciary who engages in self-dealing commits constructive fraud. *Richardson v. AMRESCO Residential Mortgage Corp*., 267 Va. 43, 49 (2004).

recklessly…." *Bank of Montreal v. Signet Bank*, 193 F.3d 818, 826 (4th Cir. 1999) (citations omitted); *Hitachi Credit Am. Corp.*, 166 F.3d 614, 628 (4th Cir. 1999) ("Virginia law also recognizes an action for fraud where misrepresentations are made without specific fraudulent intent but made with reckless abandon and disregard for truth.").

Here, the trial court stated that "[t]the key leaders in MCR absolutely should have known that the disclosure that they were giving was a lie and misleading" and found the manner in which they behaved "colossally negligent" and "colossally stupid." A2358. If anything, this understates the severity of MCR's conduct. The Air Force investigation began eleven days before the closing date. MCR knew that allowing its tainted employees — described as "radioactive" by the trial court — to participate in preparing the final bid put MCR at substantial risk for being found guilty for violating federal ethics laws. A 386, 552-53, 1056-57, 1353. MCR knew this before closing because MCR's own attorneys instructed it a week earlier to immediately remove the tainted employees.

On the very day of closing, the Air Force confirmed in a telephone call with MCR management that MCR was still under investigation. Yet, later that day, MCR delivered the Bring-Down Certificate certifying to JB&A that MCR was not under investigation. These facts easily support the conclusion that MCR acted in a

"reckless manner" when it delivered the Bring-Down Certificate. *See Bank of Montreal*, *supra.*

In addition, the trial court found that MCR "engaged in an intentional course of conduct to cover up their actions, to cover up that they mishandled the errant email as far as the Air Force was concerned, that they were being asked to submit affidavits … deceitful acts that took place over a period of time, really truly culminated on May 31st." A2582. *See also* A2353:3-7 (finding that MCR "hid facts from JB&A."); A2659 (finding callous, deceitful and deliberate acts); A2674 ("defendant made efforts to hide, misstate, obfuscate the financial impact on the plaintiff"). That too establishes actual fraud. "Concealment of a material fact by one who knows that the other party is acting upon the assumption that the fact does not exist constitutes actionable fraud." *Allen Realty Corp. v. Holbert*, 227 Va. 441, 450 (1984). [12]

Finally, MCR failed in its common law duty to disclose subsequently-acquired information — the Air Force investigation — that rendered its previous

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[12] *See also Spence v. Griffin,* 236 Va. 21, 28 (1988) ("[C]oncealment, whether accomplished by word or conduct, may be the equivalent of a false representation, because concealment always involves deliberate nondisclosure designed to prevent another from learning the truth"); *Clay v. Butler,* 132 Va. 464, 474 (1922) ("If a party conceals a fact that is material to the transaction, knowing that the other party is acting on the assumption that no such fact exists, the concealment is as much a fraud as if the existence of the fact were expressly denied, or the reverse of it expressly stated.").

representation to JB&A untrue. This constitutes yet another ground for finding actual fraud. Restatement (Second) of Torts, §551 (1977).

IV. THE TRIAL COURT'S VERDICT DOES NOT REQUIRE AN ELECTION OF REMEDIES (ASSIGNMENT OF ERROR 5)

STANDARD OF REVIEW

The trial court's determination that the damages, prejudgment interest, and attorney's fees awards were not duplicative and that no election of remedies was required is reviewed *de novo*. *Wilkins v. Peninsula Motor Cars, Inc.*, 266 Va. 558, 561 (2003).

DISCUSSION

The trial court ruled that JB&A was entitled to prejudgment interest on its breach of contract claim and attorneys' fees on the fraud claim. These additional components of recovery were not part of the $11,995,002 compensatory damage award and are thus not duplicative. JB&A was not required to elect between these remedies. *Wilkins,* 266 Va. at 562. *See, also, Abi-Najm v. Concord Condo., LLC,* 280 Va. 350, 361, 699 (2010) ("[I]t is well-established that a single act or occurrence can, in certain circumstances, support causes of action both for breach of contract and for breach of a duty arising in tort, thus permitting a plaintiff to recover both for the loss suffered as a result of the breach and traditional tort damages, including, where appropriate, punitive damages...").

The trial court here awarded attorney's fees to JB&A on its fraud claim through the exercise of its equitable powers and awarded prejudgment interest to JB&A based upon its breach of contract claim. MCR argues it is impermissible for the trial court to award equitable and legal remedies. This argument is undermined by Virginia's merger of law and equity effective on January 1, 2006. Parties can now put all claims sounding in common law and equity into a single action. *See* W. Hamilton Bryson, *The Merger of Common-Law and Equity Pleading in Virginia,* 41 U. Rich. L. Rev. 77 (2006); Va. Sup. Ct. R. 1:4(k) (Repl. Vol. 2009) ("A party may also state as many separate claims or defenses as he has regardless of consistency ...."); Va. Code Ann. § 8.01-281 (Repl. Vol. 2007) (permitting the pleading of "alternative facts and theories of recovery.").

MCR cites no post-2006 authority that would require JB&A to elect remedies in this case. In fact, the very treatise MCR cites in support of its arguments contradicts its position: the "'single form of action' system permits a trial judge to follow equitable doctrines for claims and defenses of that nature, and accord jury trial rights and monetary relief for claims at law, without requiring the parties to file multiple suits, transfer (sometimes improvidently) from side to side, or seek a stay of one court's actions to pursue the other exclusively." Kent Sinclair & Leigh B. Middleditch, Jr., *Virginia Civil Procedure* §1.15 at 52 (6th ed. 2014).

Even before the merger of law and equity, a court sitting in equity could apply legal remedies. In *Waskey v. Lewis*, 224 Va. 206, 213 (1982), this Court stated that "when a court of equity acquires jurisdiction of a cause, for any purpose, it will retain it and do complete justice between the parties, enforcing, if necessary, legal rights, and applying legal remedies to accomplish that end." *Id.* (emphasis added).[13] Thus, it was well within the court's authority to award equitable relief in the form of compensatory damages and attorneys' fees on JB&A's fraud claim and pre-judgment interest on the breach of contract claim.

CONCLUSION

The Court should affirm the trial court's judgment.

[13] *See also Fid. and Casualty v. Bank,* 213 Va. 531, 538 (1973) ("[I]n a chancery cause the court has broad power to proceed to a complete adjudication of all rights asserted by the parties in order to avoid a multiplicity of suits and to terminate litigation…"); *Advanced Marine Enter. v. PRC Inc.,* 256 Va. 106, 122, (1998) ("[O]nce a court of equity obtains jurisdiction in a case, the court has discretion to transfer the parties to a court of law for adjudication of their law claims or to conclude the litigation by giving complete relief in the chancery cause.").

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Respectfully submitted,

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CERTIFICATE

I certify that on this 16th day of June, 2017, pursuant to Rules 5:26 and 5:32, three paper copies of this Brief of Appellee were hand-filed with the Clerk of the Supreme Court of Virginia, and electronic copies of the Brief were filed via VACES. On the same day, copies were served by email on:

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