In The

Supreme Court of Virginia

RECORD NO. 161799

MCR FEDERAL, LLC,

Appellant,

v.

JB&A, INC.,

Appellee.

BRIEF OF APPELLANT

L. Steven Emmert (VSB No. 22334)
SYKES, BOURDON, AHERN & LEVY, P.C.
281 Independence Boulevard, 5th Floor
Virginia Beach, Virginia 23462
(757) 499-8971 (Telephone)
(757) 456-5445 (Facsimile)
emmert@virginia-appeals.com

Counsel for Appellant

Miguel Estrada (pro hac vice)
John Millian (pro hac vice)
Lucas C. Townsend (pro hac vice)
Laura Cole (VSB 83763)
Andrew Davis (pro hac vice)
GIBSON, DUNN & CRUTCHER LLP
1050 Connecticut Avenue, N.W.
Washington, D.C. 22036
(202) 995-8500 (Telephone)
(202) 467-0539 (Facsimile)
mestrada@gibsondunn.com
jmillian@gibsondunn.com
ltownsend@gibsondunn.com
lcole@gibsondunn.com
adavis@gibsondunn.com

Counsel for Appellant

THE LEX GROUP ♦ 1108 East Main Street ♦ Suite 1400 ♦ Richmond, VA 23219
(804) 644-4419 ♦ (800) 856-4419 ♦ Fax: (804) 644-3660 ♦ www.thelexgroup.com

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TABLE OF CONTENTS

Page

STATEMENT OF THE CASE 1

ASSIGNMENTS OF ERROR 2

FACTS 2

1. JB&A needs to sell itself 2

2. JB&A's "exhaustive marketing process" yields only one offer: MCR's 4

3. MCR allocates an accounting price to its new purchase 7

4. The Air Force erroneously discloses a bid 8

5. The contracting business misses earnings thresholds, and JB&A sues 11

6. JB&A's trial evidence 13

ARGUMENT 15

1. The trial court erroneously allowed JB&A to sue in tort for "constructive fraud" based on the alleged breach of a contractual warranty. (Assignment 1) 16

   Standard of Review 16

   Discussion 17

2. The trial court failed to require legally sufficient evidence that MCR caused JB&A an injury. (Assignment 2) 22

   Standard of Review 22

   Discussion 22

TABLE OF CONTENTS
(continued)

Page

3. The trial court erred in awarding damages based upon a "purchase price allocation" calculation that was inherently speculative. (Assignment 3) 31

Standard of Review 31

Discussion 32

4. The trial court erroneously awarded attorneys' fees as "equitable" relief on JB&A's constructive-fraud count. (Assignment 4) 38

Standard of Review 38

Discussion 38

5. The trial court erred in failing to require JB&A to elect between incompatible legal and equitable remedies. (Assignment 5) 42

Standard of Review 42

Discussion 42

CONCLUSION 44

CERTIFICATE 46

TABLE OF AUTHORITIES

Page(s)

Cases

Abi-Najm v. Concord Condo., LLC,
280 Va. 350 (2010) 19

Cohn v. Knowledge Connections, Inc.,
266 Va. 362 (2003) 22

Devine v. Buki,
289 Va. 162 (2015) 18, 19

Dunn Const. Co. v. Cloney,
278 Va. 260 (2009) 16, 17, 18, 19

Gov't Emps. Ins. Co. v. United Servs. Auto. Ass'n,
281 Va. 647 (2011) 22

Great-West Life & Annuity Ins. Co. v. Knudson,
534 U.S. 204 (2002).....39, 40

In re IBP, Inc. S'holders Litig.,
789 A.2d 14 (Del. Ch. 2001) 28

Interim Healthcare, Inc. v. Spherion Corp.,
884 A.2d 513 (Del. Super. Ct. 2005).....29

Isle of Wight Cty. v. Nogiec,
281 Va. 140 (2011) 24

Jennings v. Realty Developers, Inc.,
210 Va. 476 (1970) 42-43

LaPoint v. AmerisourceBergen Corp.,
2007 WL 2565709 (Del. Ch. Sept. 4, 2007), *aff'd*, 956 A.2d 642
(Del. 2008) 24

Love v. Kenneth Hammersely Motors Inc.,
263 Va. 45 (2002) 39

TABLE OF AUTHORITIES
(continued)

Page(s)

Modern Oil Corp. v. Cannady,
No. 141839, 2015 WL 10990113 (Va. Dec. 30, 2015) 20

Newman v. Freeman Homes, Inc.,
89 Va. Cir. 377, 2014 WL 10520419 (Va. Cir. Ct. 2014).....42

Oswald v. Holtzman,
90 Va. Cir. 9 (Va. Cir. Ct. 2015) 40

Piney Meeting House Invs., Inc. v. Hart,
284 Va. 187 (2012) 38

Porter v. Commonwealth,
276 Va. 203 (2008) 38

Prospect Development Co. v. Bershader,
258 Va. 75 (1999) 15, 23, 38, 39, 40, 41

Reserves Dev. LLC v. Crystal Props., LLC,
986 A.2d 362 (Del. 2009) 32

Richmond Metro. Auth. v. McDevitt Street Bovis, Inc.,
256 Va. 553 (1998) 16, 17, 18, 22

Sensenbrenner v. Rust, Orling & Neale, Architects, Inc.,
236 Va. 419 (1988) 17, 21

Sugarland Run Homeowners Ass'n v. Halfmann,
260 Va. 366 (2000) 22

SunTrust Bank v. Farrar,
277 Va. 546 (2009) 29, 31, 32, 34, 35, 36, 37

VLIW Tech., LLC v. Hewlett-Packard Co.,
840 A.2d 606 (Del. 2003) 22

Ware v. Scott,
220 Va. 317 (1979) 20

TABLE OF AUTHORITIES
(continued)

Page(s)

Wilkins v. Peninsula Motor Cars, Inc.,
266 Va. 558 (2003) 42

Yancey v. Fenwick,
4 H. & M. (14 Va.) 423 (1809) 42

Treatises

1 Restatement (Third) of Restitution and Unjust Enrichment 40

Kent Sinclair & Leigh B. Middleditch, Jr., *Virginia Civil Procedure*
(6th ed. 2014) 43

STATEMENT OF THE CASE

This appeal arises from a final judgment of the Fairfax Circuit Court in an action based on the sale of a business's assets. The seller, JB&A, Inc. ("JB&A"), sued the buyer, MCR Federal, LLC ("MCR"), alleging that MCR breached the parties' contract by reaffirming, in a "bring-down" certificate at the closing, certain factual warranties. The warranties were true when the contract was made, but JB&A contended that, because of intervening events, reaffirming them at the closing was false. The suit asserted that this breach of warranty also constituted fraud in the inducement, and sought the same compensatory damages for fraud that JB&A claimed for breach of contract.

After a bench trial, the court ruled in favor of JB&A, finding that MCR had breached the contract and simultaneously committed constructive fraud in the inducement, and awarded JB&A $12 million in compensatory damages on both the breach-of-contract and constructive-fraud claims. The court also awarded JB&A $3.7 million in prejudgment interest on its breach-of-contract claim, plus a purportedly "equitable" award of $1.9 million in attorneys' fees on the constructive-fraud theory. The court therefore mixed legal and equitable relief to award JB&A nearly $17.4 million. This Court awarded MCR an appeal on April 11, 2017.

ASSIGNMENTS OF ERROR

1. The trial court erred in allowing JB&A to sue in tort for actual or constructive fraud based on allegedly false contractual representations. (Preserved: A. 28-32; A. 34-43; A. 45-87, 96-112; A. 157; A. 2291-93; A. 2297-98, 2360)

2. The trial court erred in granting judgment for JB&A absent credible evidence that MCR's alleged breach caused JB&A any injury. (Preserved: A. 2362-89; A. 2392-2400; A. 2338, 2347-48; A. 2437, 2496)

3. The trial court erred in awarding $12 million in damages based on a "purchase price allocation" calculation that assigned a price for the acquired business *as part of MCR*, based on speculative revenue projections for the acquired business that the trial court found all parties had disavowed. (Preserved: A. 2362-89; A. 2392-2400; A. 2443-87)

4. The trial court erred in awarding attorneys' fees as additional "equitable" relief on the constructive-fraud count. (Preserved: A. 2532-38; A. 2575-89; A. 2609-15)

5. The trial court erred in failing to require JB&A to elect between an equitable remedy for its fraud count and a legal remedy for its contract count, instead awarding relief under both theories. (Preserved: A. 2533-36; A. 2566-72; A. 2609-15; A. 2617-21; A. 2629-46, 2685-92)

FACTS

This case arises from the 2011 sale of JB&A's government-contracts business to MCR for $42.7 million in cash, plus the potential for up to $19.5 million in additional, future "earnout" payments if JB&A's business met certain sales and profit projections. A. 1186-89. The business did not meet those targets, and MCR did not make the earnout payments to JB&A.

1. JB&A needs to sell itself. JB&A was a government contractor that provided services and staffing to the U.S. intelligence community. A. 1150-51. In 2010, JB&A faced an uncertain future. Years earlier, it had instituted an Employee

Stock Ownership Plan ("ESOP") that invested a portion of employees' income in JB&A stock and required the company to buy back the employees' stock upon their retirement or termination, regardless of JB&A's financial circumstances. A. 197-203, 261. With an aging workforce, JB&A faced a "looming" buyback obligation, A. 1989, estimated at $20 million through 2018, A. 1866. By comparison, JB&A internally estimated the fair market value of its entire business at $37.6 million as of year-end 2010. A. 1998. This ballooning ESOP liability led the company, in 2010 and 2011, to explore the sale of its business in order "to satisfy the ESOP obligation." A. 1980-85. At the same time, JB&A recognized that its government-contracts business faced significant hurdles, including likely government budget cuts and increasing in-sourcing by government agencies, which threatened to significantly reduce the demand for JB&A's services. *See* A. 293-97; A. 802-03; A. 1978-79.

Against this backdrop, JB&A retained an investment bank, the McLean Group ("McLean"), to sell JB&A's business. In October 2010, McLean prepared an offering document that included projections of future revenues prepared by JB&A's management. A. 1872. JB&A projected that its revenues would grow from approximately $59.8 million in 2010 to $66.1 million in 2011 and $69.6 million in 2012. A. 1876.

But business did not go well in the following months. In late 2010 and early 2011, for example, JB&A learned that a key contract would be terminated and another would be delayed. A. 298; A. 1906-07. In February and March 2011, JB&A's executives lamented internally that "[r]evenues are down from 2010, and over 10% below our 2011 projection. It's uncomfortable to look at . . . ." A. 1909; A. 1950. By April 15, JB&A concluded internally that achieving its revenue projections was "unlikely," A. 1988, and JB&A personnel testified that they told MCR this fact, *see* A. 290; A. 753-54; A. 912.

2. JB&A's "exhaustive marketing process" yields only one offer: MCR's. In the fall of 2010, McLean began marketing JB&A to potential acquirers. A. 2045. As McLean described the process,

> over 60 potential acquirers were contacted, including private equity firms, financial consulting firms, advisory firms, mid-tier federal contractors, and large-cap federal contractors. Over a dozen companies reviewed detailed information regarding the Company and approximately a half dozen management meetings were held.

Id. Despite these concerted efforts, however, the process yielded "lack luster" results. *Id.* By year-end, "no formal offers were received." *Id.*

After several months with no success, JB&A received its only written letter of intent from a potential acquirer—MCR. A. 1947. MCR is a Virginia corporation in the government-contracts business, specializing in program management and related services for government and commercial clients. MCR

indicated that it would offer $45 million in cash, plus $17 million in potential future earnout payments that McLean concluded represented the "[s]trategic [v]alue of JB&A to MCR," A. 1948-49, or "synergies" that MCR could realize in time, A. 2077, 2082.

By early March 2011, the only other expression of interest that McLean received was an "oral indication of value from a private equity firm," which valued JB&A at "$30 million to $35 million," A. 1948—well below MCR's cash offer and closer to JB&A's own self-valuation of $37.6 million, A. 1998. Having received no other offers, JB&A signed a letter of intent with MCR. A. 1676-82. McLean reported that it had "completed" its "exhaustive marketing process" and judged the cash component of MCR's offer—without considering the potential earnout payments—to be "in a range of the Fair Market Value of the business." A. 1948; *see also* A. 795-96.

In the course of conducting due diligence, MCR discovered that JB&A had overstated its reported EBITDA—an accounting measure of the company's profitability—by overstating its revenues. *See* A. 797-98; A. 1041; A. 1042-49. After agreeing to adjust the purchase price downward for this overstatement, JB&A and MCR signed an Asset Purchase Agreement on May 5, 2011. *See* A. 1172-1278. Under the Asset Purchase Agreement, MCR lowered its purchase price for JB&A's business to $42.7 million in cash at closing. A. 1186-87. MCR

also agreed to pay up to $19.5 million in earnout payments, but only if the business met agreed-upon financial targets in 2011 and/or 2012. A. 1186-89. In addition, MCR made several warranties, including (as relevant here) Section 3.3(a) in the Asset Purchase Agreement:

> There is no private or governmental . . . investigation . . . or inquiry pending or, to the knowledge of Buyer, threatened before, with or by any Governmental Entity or other Person against Buyer or any of its Affiliates that would cause a Buyer Material Adverse Effect. . . . To the knowledge of Buyer, no event has occurred or circumstances exist that could reasonably be expected to give rise to, or serve as a basis for, any such . . . investigation . . . or inquiry that would cause a Buyer Material Adverse Effect.

A. 1214. The Asset Purchase Agreement and its warranties are governed by Delaware law. A. 1236.

The transaction closed on May 31, 2011. At closing, MCR delivered a "bring-down" certificate certifying that MCR's representations and warranties in the Asset Purchase Agreement remained "true and correct in all respects" as of the closing date. A. 1372. MCR delivered this bring-down certificate "pursuant to Section 5.3(e) of the Asset Purchase Agreement," *id.*, which expressly required MCR to make that certification, *see* A. 1228.

With the sale completed, JB&A became—and remains—a "shell" company. A. 1108. Having transferred its employees and assets to MCR, JB&A existed solely to distribute the sale proceeds, including any potential future earnout

payments received from MCR, to the ESOP and to JB&A's other stockholders. *See* A. 1106, 1107, 1108.

3. MCR allocates an accounting price to its new purchase. Accounting rules applicable to MCR's 2011 financial reporting required MCR to compute a "purchase price" for the newly-acquired assets. A. 824, 838-41; A. 2071. MCR hired McLean to perform this analysis, and McLean documented its calculations in a 2012 report known as the "purchase price allocation" (the "Allocation"). A. 2068-2136. The Allocation stated that it was intended only "to provide effective audit evidence," and did "not include a valuation opinion of the acquired tangible assets." A. 2072-73. It also explicitly cautioned that it "should not be used for any other purpose." A. 2071. Despite these limitations, the trial court used the Allocation as the sole basis for awarding JB&A damages for both its breach-of-contract and constructive-fraud claims—a key issue in this appeal.

The Allocation estimated the total "purchase price" of JB&A's assets, for MCR's accounting purposes, as the sum of two components: approximately $42.7 million in total cash paid at closing; and $11,995,002, representing a probability-weighted "fair value" of the potential earnout payments as of the closing date. A. 2080. To calculate the earnout component, the Allocation discounted the potential earnout payments by assumed probabilities that the business would achieve the revenue targets needed to pay earnouts for 2011 and 2012. *See* A. 2080, 2125-33.

Those probabilities, in turn, were based primarily on the highly optimistic revenue projections that JB&A originally gave to potential acquirers in 2010—but which, according to JB&A's own claims and testimony at trial, it had later disavowed before the closing. *Compare* A. 1890 ($66,055,965 million in total revenue projected for 2011), *with* A. 2084 (same); *see also* A. 1072-76; A. 2100 (total forecasted revenues based on sales of "$44.2 million for the remaining 8 months of 2011" and "$69.6 million in 2012").

Using this probability-weighted approach, the Allocation estimated a total "purchase price" of $54,687,545. A. 2080. That "price" reflected the expected performance of JB&A's business "as a going concern" through "2011 and 2012," A. 2073, 2080—*after* MCR acquired it—including synergies and strategic value to MCR, A. 1949; A. 2077. (MCR never had a need to value JB&A as a standalone entity.) Because JB&A's business failed to meet its financial targets, MCR wrote down to zero the earnouts component of that price in its 2011 and subsequent financial statements. A. 2167-69.

4. <u>The Air Force erroneously discloses a bid</u>. While JB&A and MCR were preparing to close their transaction, MCR was competing with another company for an Air Force contract. On May 19, 2011, an Air Force contracting officer inadvertently sent MCR the competitor's original bid information as an email attachment. Before the attachment was opened, the email was forwarded internally

to several MCR employees. *See* A. 1329; A. 1330. Ultimately, four MCR employees were exposed to the competitor's bid information. A. 976.

MCR immediately took steps to delete the errant email and inform the Air Force of its error. *See* A. 1329; A. 1330. At the trial below, MCR's employees testified about the protective measures they took to isolate the effects of the email. The court ultimately found that those efforts either were ineffective or not credible, *see* A. 2299-2360, but did not find any intentional wrongdoing by MCR, *see* A. 2358.

Despite its error, the Air Force "wanted to keep the procurement moving." A. 539. As the Air Force's chief of contracts testified, "we knew that there [were] a couple people within MCR who had seen the information, but we still made the determination that we would move forward." A. 538. Indeed, shortly after the Air Force contracting officer realized her error, she sent MCR another email attaching the correct documents and "requesting your Final Proposal Revision." A. 1341.

On May 20, the contracting officer requested affidavits from MCR employees who had received the email. A. 1339. The Air Force's chief of contracts later testified that the purpose in requesting the affidavits was "to try to get the facts to ultimately determine the impact" from the errant email. A. 580. MCR likewise understood the request as an attempt to clarify the bid record given the Air Force's mistake. A. 704-05; A. 1027.

As requested, MCR submitted its bid on May 26. A. 2194-2252. That same day, the Air Force agreed that MCR should provide the requested affidavits on June 7—one week after the JB&A transaction closed. A. 1422.

On June 7, MCR gave the Air Force the requested affidavits. A. 1375-96. The Air Force requested "several clarifications" to the information that MCR had provided, A. 1397-98, and MCR provided supplemental affidavits on June 17, A. 1399-1414. MCR heard nothing more until August 23, when MCR and four employees unexpectedly received notice that the Air Force had suspended them from government contracting as a result of having participated in the bidding process after receiving the errant email. A. 1439-44. This was the first suspension in MCR's 35-year history.

On September 26, 2011, the Air Force lifted the suspension after MCR acknowledged in writing certain "improper conduct" and "deficient procedures" in connection with the bid submission. A. 1489. On October 28, 2011, the Air Force re-imposed the suspension based on an apparent error in reading MCR's affidavits. *See* A. 739; A. 1510-14. After further communications with MCR's management, the Air Force lifted the second suspension within three weeks. *See*, *e.g.*, A. 1008-10. All told, MCR was suspended from government contracting for 53 days and

the investigations ultimately were "concluded without administrative, judicial, or executive action taken against MCR." A. 2176.[1]

5. The contracting business misses earnings thresholds, and JB&A sues. The business that MCR acquired from JB&A failed to meet its financial targets in 2011 and 2012, and MCR made no earnout payments. In 2013, JB&A sued MCR and three of its executives for breach of warranty under the Asset Purchase Agreement and for actual and constructive fraud in closing the transaction. A. 18-22, at ¶¶ 79-108. As relevant here, JB&A's original complaint alleged that MCR breached its contractual warranties, and also committed "fraud" (through the individual defendants), by reaffirming those contractual warranties in the May 31 bring-down certificate without also disclosing the Air Force's inquiry. A. 18-23, at ¶¶ 80-84, 94-101, 103-09. JB&A asserted that the financial targets to trigger earnout payments, as set forth in the Asset Purchase Agreement, had not been achieved because of lost business "[a]s a result of MCR's violations." A. 17, at ¶ 75; *see* A. 15-17, at ¶¶ 64-76. JB&A further alleged that "[b]ut for MCR's suspensions, JB&A would have been entitled to Earn-out Payments" under the Asset Purchase Agreement, A. 17, at ¶ 76, and that JB&A would not have closed

[1] At trial, the Air Force official who recommended the suspensions, David Robbins, testified that the decision to suspend MCR was "very aggressive," A. 1007, and that in retrospect "we needed more inquiry" before suspending MCR based on a mere appearance of impropriety, A. 1013-14.

the transaction but for the alleged "false statements and omissions," A. 21-22, at ¶¶ 98, 106.

MCR demurred to the original complaint, arguing that the fraud counts were based on the contractual warranties and that JB&A could not maintain overlapping contract and tort claims under Virginia's single-source-of-duty rule. The trial court overruled the demurrer. A. 106-12. JB&A later amended its complaint twice, and the Second Amended Complaint became the operative pleading. *See* A. 115-41. In its Second Amended Complaint, JB&A continued to assert that MCR breached its contractual warranties by delivering the May 31 bring-down certificate without disclosing the Air Force inquiry, and also fraudulently induced JB&A to close the transaction. *See* A. 136, at ¶ 92-97; A. 137-40, at ¶¶ 106-16. JB&A also continued to allege that "[b]ut for MCR's suspensions, JB&A would have been entitled to Earn-out Payments" under the Asset Purchase Agreement, A. 135, at ¶ 87, and that JB&A would not have closed on May 31 but for the alleged misstatements and omissions, *id*. MCR reasserted its demurrer to JB&A's Second Amended Complaint on the ground that "a fraud claim may not lie where the source of the duty to make a representation lies in contractual terms." A. 157.[2]

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[2] Two of the three individual defendants were dismissed before trial; the third was dismissed after trial on the merits. MCR counterclaimed for fraud after discovery revealed that JB&A had provided inflated revenue projections to hide its deteriorating business. At trial, JB&A's witnesses testified that they had

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6. JB&A's trial evidence. Eighteen witnesses testified during the 21-day bench trial. The court found all of JB&A's witnesses credible, yet only one of MCR's witnesses credible. A. 2299-2360. The court also found MCR liable for breach of the Section 3.3(a) warranty and for constructive fraud in not divulging at the closing the errant email and the Air Force's requests for affidavits—which JB&A contended (and the court believed) was a material "investigation" or "inquiry" in violation of the bring-down warranty. The court found, however, that neither MCR nor its executives had committed actual fraud, A. 2358—a finding that JB&A has not appealed. While MCR strenuously disagrees with the court's adverse and lopsided credibility and liability findings, they are irrelevant to the legal errors identified below.

JB&A presented exactly the same theory of damages for both its breach-of-contract and fraud claims. Notwithstanding the allegations of its Second Amended Complaint, JB&A was unable to show that but for the suspensions the business would have achieved sufficient revenue to justify even a single dollar in earnout

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disavowed those inflated projections before the closing, and the court found no liability on the counterclaim because JB&A's statements were "merely projections" and there was "no reasonable reliance." A. 2359. MCR does not seek review of that ruling here. Nevertheless, it is relevant to the court's legal errors in awarding damages because JB&A's *only* evidence of damages was the Allocation, which incorporated the same rosy projections that JB&A's witnesses claimed they had disavowed. *See* Assignment 3, *infra*.

payments. JB&A's counsel presented no evidence of the lost-earnout theory and later conceded that he had "put [the theory] to the side." A. 2495. JB&A's damages expert also disavowed the lost-earnout theory, admitting at trial that it would be "speculative" to assume that MCR failed to make earnout payments as a result of business lost during the suspensions. A. 941, 947. The trial court agreed that any theory of "how the suspensions financially impacted the parties and how things would have been different but for" the suspensions "would have required the Court to speculate." A. 2505-07.

Instead, JB&A sought as damages the difference between the $42.7 million in cash that MCR paid for JB&A's business and what it asserted was the "value" of that business as of the closing date. JB&A posited that, had MCR disclosed the Air Force "investigation," JB&A would have not closed the transaction—remaining independent and somehow achieving a higher price than the $42.7 million paid by MCR. JB&A did not, however, introduce any evidence that any willing buyer would have paid more than MCR—or even any valuation of JB&A's standalone business. Instead, JB&A claimed that—following a hypothetical refusal to close the deal—an independent JB&A would have sold for more, and based that claim solely upon the $54.7 million "purchase price allocation" that MCR temporarily booked only for financial accounting purposes. A. 2517-18. Rather than attempting to prove that it *actually* would have achieved the earnout,

JB&A urged the trial court to grant as damages the amount MCR had allocated to the probability-weighted earnouts (and immediately written down to zero with the approval of MCR's outside independent auditors) for accounting purposes in 2012. Finding this measure "reliable," the court awarded $11,995,002 in compensatory damages on the breach-of-contract and constructive-fraud counts. A. 2520, 2528-29.

Over MCR's objection, the court also awarded $1.9 million in attorneys' fees as "equitable" relief on the constructive-fraud count. A. 2575-89; A. 2696. Attempting to justify this departure from the American rule, the court reasoned that the money damages on the constructive-fraud count were equitable in nature and could be supplemented with attorneys' fees under this Court's decision in *Prospect Development Co. v. Bershader*, 258 Va. 75 (1999).

Finally, the court awarded $3.7 million in prejudgment interest on the breach-of-contract count, over MCR's objection that JB&A must elect between receiving legal relief for breach of contract or equitable relief for fraudulently inducing the closing of that contract. A. 2595-96; A. 2696.

ARGUMENT

The trial court committed five independent errors of law, each of which requires reversal. It erred in allowing an alleged breach of contract to proceed as an action for fraud based on the same alleged conduct; correcting this error

requires vacating the constructive-fraud judgment. The court further erred in entering judgment for JB&A based on legally insufficient evidence of causation and damages, which are essential elements of both of JB&A's claims; correcting either of these errors requires reversing the trial court's judgment and entering judgment for MCR on both the breach-of-contract and constructive-fraud theories. The trial court also erred in awarding purportedly "equitable" attorneys' fees on JB&A's legal claim constructive fraud; correcting this error requires vacating the award of attorneys' fees. Finally, the court erred in mixing legal and equitable remedies to award JB&A the highest possible money judgment; correcting this error requires vacating either the "equitable" or the damages components of the money judgment.

1. The trial court erroneously allowed JB&A to sue in tort for "constructive fraud" based on the alleged breach of a contractual warranty. (Assignment 1)

Standard of Review

The source of a legal duty is a pure question of law reviewed *de novo*. *See generally Richmond Metro. Auth. v. McDevitt Street Bovis, Inc.*, 256 Va. 553, 558-59 (1998). Whether there is sufficient evidence of an independent act of fraud is determined viewing the evidence in the light most favorable to the prevailing party at trial. *Dunn Const. Co. v. Cloney*, 278 Va. 260, 266 (2009).

Discussion

JB&A's theory below was that MCR made a fraudulent statement in the bring-down certificate, not in the original contract. But MCR's duty to provide that certificate arose in the Asset Purchase Agreement. That made this a contract claim, not one for fraud.

"Tort law is not designed . . . to compensate parties for losses suffered as a result of a breach of duties assumed only by agreement." *Sensenbrenner v. Rust, Orling & Neale, Architects, Inc.*, 236 Va. 419, 425 (1988). As this Court has explained, "[i]n determining whether a cause of action sounds in contract or tort, the source of the duty violated must be ascertained." *Richmond Metro. Auth.*, 256 Va. at 558. Where a particular misrepresentation "related to a duty or an obligation that was specifically required by the [contract]," the defendant's actions "do not give rise to a cause of action for actual fraud." *Id.* at 559. Nor will a negligent breach of contract support a tort action. *Id.*

This Court's decision in *Dunn Construction Co. v. Cloney*, 278 Va. 260 (2009), illustrates this principle, and shows why JB&A's fraud claim fails. In *Dunn*, a homeowner contracted with a builder for the construction of a house "to be completed in a workmanlike manner according to standard practices." *Id.* at 263 (quotation marks omitted). After defects were discovered in the foundation, the builder performed repairs and sought payment. *Id.* The homeowner paid for

the work, but only after the builder provided an additional, written guarantee of the repairs and the foundation's integrity. *Id.* at 264. When the homeowner later learned that the builder had not completed the repairs as represented and that his work did not meet building codes, the homeowner sued for breach of contract and fraud. *Id.* Although a jury found liability on both counts and awarded punitive damages on the fraud count, *id.* at 265, this Court, following *Richmond Metropolitan Authority*, reversed the fraud judgment.

The Court explained that the builder had breached his contractual duty to construct the foundation "according to standard practices," and his "false representation that he had made adequate repairs thus related to a duty that arose under the contract." *Dunn*, 278 Va. at 268. The builder's written guarantee did not "constitut[e] a fraudulent inducement violative of a common law duty separate and apart from any duty arising under the contract," the Court held, because "the payment obtained was also due under the original terms of the contract"—even if the builder's subsequent misrepresentations "were unquestionably deliberate and false." *Id.*

As *Dunn* makes clear, this single-source-of-duty rule applies with full force even for executory contracts requiring future performance. In *Devine v. Buki*, 289 Va. 162 (2015), for example, this Court upheld a claim for fraudulent inducement against the seller of a house who concealed a material fact that, had it been

disclosed, would have excused the buyers from performing. The contract of sale expressly "made no representations or warranties as to the condition of the property," *id.* at 167, and therefore explicitly *disclaimed* any contractual duty of disclosure. In that circumstance, this Court held that the buyer could sue the seller for fraud in the inducement. *Id.* at 175. Here, in contrast, the parties negotiated for and agreed upon the specific *contractual* warranty that MCR provided in the bring-down certificate. A. 1228. That contractual duty displaces any cause of action for "fraud."

The trial court below misunderstood these authorities. Perceiving a "gray area" that "the Supreme Court has not specifically touched on," the trial court allowed JB&A's tort claim to proceed under a "fraud in the inducement" theory. A. 107, 111. But this Court in *Dunn* rejected an identical theory under indistinguishable circumstances. Just as the builder's misrepresentations that induced the homeowner to pay for contracted-for work did not sound in tort, MCR's allegedly false warranty that induced JB&A to close the transaction under the Asset Purchase Agreement likewise failed to state a claim for fraud.

The trial court was led astray by cases allowing claims for fraudulent inducement in *entering* into a contract, *see Abi-Najm v. Concord Condo., LLC*, 280 Va. 350, 363-64 (2010), or cases involving actual (not constructive) fraud where the parties apparently made no contractual warranties at the closing and thus were

subject only to common-law duties of disclosure, *see Ware v. Scott*, 220 Va. 317, 320 (1979). Here, however, the parties entered into the Asset Purchase Agreement *before* the allegedly false warranty was made in the bring-down certificate; and MCR unquestionably made that warranty pursuant to the contract, not because MCR had any common-law duty to do so. A. 1372. Moreover, the trial court had no basis to extend the *Ware* line of cases, which involve the active concealment of material information, to this case, which (even under the trial court's view) involves no intentional wrongdoing. *See Modern Oil Corp. v. Cannady*, No. 141839, 2015 WL 10990113, at *4-5 (Va. Dec. 30, 2015) (holding that "a misrepresentation [that] entices a contracting party to perform an executory contract" must involve "active concealment or any other affirmative action intending to deceive").

If there could be any doubt on this score, it is dispelled by the trial court's liability ruling, which confirms that MCR was subject only to a contractual duty. As the court explained, liability turned on whether MCR "should have divulged the information about the Air Force's investigation . . . to JB&A at the bring-down or within the bring-down, that is, *was this sort of information contemplated to be divulged in the* [bring-down]." A. 2297-98 (emphasis added). "[I]f the answer to that was yes," the court continued, "then false information was essentially given in the [bring-down], . . . *which would constitute a breach of the contract*. And the

failure to do so *would also constitute a material representation*" for purposes of establishing constructive fraud. A. 2298 (emphases added). Thus, the court found, the "false representation at the May 31 bring-down . . . *in and of itself* would constitute a breach of the contract." A. 2360 (emphasis added). There can be no doubt that the trial court imposed both contract and tort liability for the supposed breach of a contractual duty—in direct conflict with this Court's precedents.

This case illustrates the wisdom of this Court's admonition against the "'more or less inevitable efforts of lawyers to turn every breach of contract into a tort.'" *Sensenbrenner*, 236 Va. at 424 (citation omitted). MCR and JB&A are sophisticated corporations, each represented by experienced corporate counsel, that bargained for contractual duties—including those requiring disclosure based on good-faith interpretations of what constituted a "material adverse effect" on the overall business. There was no independent common-law tort duty that governed their business relationship, much less MCR's contractual bring-down certificate. Thus, there was no need to extend the narrow exception that allows homebuyers, in cases where there is no governing contractual warranty, to sue sellers for actual fraud in inducing executory contracts. This dispute only involved a good-faith difference in contract interpretation, not an intentional act to defraud. The trial court's novel decision, if left uncorrected, would frustrate bargained-for

expectations in Virginia and threaten to turn "every breach of contract into an actionable claim for fraud." *Richmond Metro. Auth.*, 256 Va. at 560.

2. The trial court failed to require legally sufficient evidence that MCR caused JB&A an injury. (Assignment 2)

Standard of Review

"[P]roximate causation is a question of fact to be resolved by a jury," but "when reasonable people cannot differ, the issue becomes a question of law for the court to decide." *Sugarland Run Homeowners Ass'n v. Halfmann*, 260 Va. 366, 372 (2000). On appeal from a judgment following a bench trial, questions of law are reviewed *de novo*, and questions of fact are reviewed for clear error with the record viewed in the light most favorable to the prevailing party. *Gov't Emps. Ins. Co. v. United Servs. Auto. Ass'n*, 281 Va. 647, 655 (2011).

Discussion

Causation of damages is an essential element of liability under both JB&A's breach-of-contract claim and its constructive-fraud claim. To establish liability under either claim, JB&A was required to prove that MCR's alleged breach actually caused JB&A quantifiable damages. *VLIW Tech., LLC v. Hewlett-Packard Co.*, 840 A.2d 606, 612 (Del. 2003) (requiring "resultant damage" from breach of contract); *Cohn v. Knowledge Connections, Inc.*, 266 Va. 362, 369 (2003) ("A person asserting a claim of constructive fraud must prove that the misrepresentation forming the basis of the claim caused damage to the one relying

on it.”). Whether JB&A proved that element by the requisite clear and convincing evidence (*Prospect Dev. Co. v. Bershader*, 258 Va. 75, 86 (1999)) and thus whether JB&A established liability for either claim—contract or constructive fraud—is a central issue in this appeal.

For both claims, JB&A’s causation theory was exactly the same: that but for MCR’s alleged breach, JB&A would not have closed the transaction and would have retained the “value of [its] business.” A. 2438-39, 2495, 2506; *see also* A. 2408-09. According to JB&A, that “value” exceeded the $42.7 million that MCR paid to JB&A at the closing. But the trial court failed to require legally sufficient proof of JB&A’s “value,” and JB&A failed to prove that MCR’s alleged breach proximately caused JB&A *any* damages. As a result, JB&A failed to prove an essential element of its contract and tort claims, and the trial court’s erroneous judgment handed JB&A an eight-figure windfall.

In seeking to prove the causation of damages, JB&A had two conceivable options for demonstrating the lost value of its business—neither of which it proved.

First, JB&A could seek to prove that the false warranty caused it to lose earnout payments it otherwise would have been due. This lost-earnout theory is well-recognized in business disputes of this type. This approach would have required JB&A to provide evidence of specific lost business opportunities that, but

for the alleged breach and the subsequent suspensions, would have allowed JB&A's business to achieve the financial targets needed to trigger the earnouts. *See*, *e.g.*, *LaPoint v. AmerisourceBergen Corp.*, 2007 WL 2565709, at *9-10 (Del. Ch. Sept. 4, 2007), *aff'd*, 956 A.2d 642 (Del. 2008); *Isle of Wight Cty. v. Nogiec*, 281 Va. 140, 150-51 (2011). Without such evidence, it would be entirely speculative to infer causation of damages based on the mere absence of earnout payments, since any number of intervening factors having nothing to do with a defendant's breach could have caused a business to miss its earnout targets.

In its Second Amended Complaint, JB&A suggested its intent to rely on a lost-earnout theory, but JB&A abandoned any such theory at trial. JB&A presented no "direct evidence" that it would have achieved its earnout targets but for specific lost business opportunities that would have materialized "had only" MCR not been suspended. *LaPoint*, 2007 WL 2565709, at *10. Indeed, JB&A's counsel later expressly conceded that he had "put [the theory] to the side." A. 2495. And with good reason: as JB&A's expert also repeatedly conceded, it would be "highly speculative" to surmise that JB&A did not achieve its earnout targets in 2011 and 2012 *because of* specific lost business opportunities attributable to the brief suspensions. *See*, *e.g.*, A. 947 (Agresto recognizing "the really highly speculative nature of doing this analysis" based on lost earnouts); *see also* A. 940-41 (Agresto admitting that he "felt that it would be much more difficult to do and

much more speculative" to base damages on lost earnouts "caused by the suspensions"). This was especially the case given that the potential earnouts had been based on rosy business projections it had prepared to put itself up for sale, and which, according to its claims at trial, JB&A had abandoned before the closing. *See*, *e.g.*, A. 799-801.

The trial court accepted JB&A's waiver of its lost-earnout theory, noting that JB&A had "discarded or sort of ignored" the lost-earnout theory and "didn't really pursue it." A. 2495, 2507. Moreover, the court expressly found that a lost-earnout theory, had it been presented at trial, "would have required the Court to speculate." A. 2507. Accordingly, the record refutes any conceivable argument that JB&A would have hit any of the earnout targets but for MCR's actions.

Second, having discarded its earnout theory, JB&A chose a different tack: It claimed that it sold its business to MCR for less than that business was actually worth. This depends on the assumption that the business would have sold for more than $42.7 million to another buyer.

But there *was* no other buyer. Despite an intensive marketing effort, JB&A never received another bid. A. 1948.

Nor could the value of JB&A as a going concern justify a price above $42.7 million. JB&A valued itself at $37.6 million, and the only other expression of interest in the company put its value in the range of "$30 million to $35 million."

A. 1948; A. 1984; A. 1998, 2045. And JB&A never even tried to prove that it would have reached the earnout targets if it had continued to operate alone. A. 1997, 1998.

Only to MCR—only as a component of MCR's corporate structure—was JB&A worth what MCR paid for it.

The trial court never required JB&A to establish, with legally sufficient evidence, that *but for* MCR's alleged breach, JB&A would not have closed and would have been better off by retaining its business. Instead, in purporting to find causation of damages on this record, the trial court relied on evidence that had nothing to do with the causation theory that JB&A actually pursued. The court found that "the catastrophic financial impact on MCR from the suspension" established "causation of damages" because that impact "would not have occurred but for JB&A's reliance upon the false representation." A. 2347-48. But that putative injury *to MCR* in no way resulted from JB&A's decision to close on May 31, or from MCR's alleged breach in delivering the bring-down certificate.

To see why, the Court need only consider the *but-for* scenario that JB&A's causation theory needed to prove—that if MCR had truthfully disclosed the Air Force "investigation," *JB&A would not have closed the transaction*. That theory required JB&A to prove how the closing caused it injury—*i.e.*, how JB&A, had it remained independent, would have realized higher value than the $42.7 million

that MCR paid. But the Court instead focused on what happened *to MCR* as a result of its pre-closing conduct. This is completely irrelevant; even if it was foreseeable that MCR's handling of the Air Force's errant email would lead to *its* suspension, JB&A's theory was that a true bring-down certificate would have caused it not to close, and thus that it never would have become part of MCR.

In purporting to find causation of damages, the court focused on the *actual* scenario in which MCR suffered injury from closing the transaction and being suspending from government contracting. But whatever injury the suspensions may have caused *to MCR* after the closing, the fact of that injury cannot show that but for MCR's alleged breach on May 31, JB&A would have been better off by remaining independent and achieving a higher price.

The court also relied on the Allocation as evidence of the fact of damages, but that too was legally insufficient to infer causation, for at least two reasons.

Most fundamentally, the Allocation by its express terms is not a "valuation opinion," and certainly does *not* value JB&A as an independent going concern. *See* A. 2071-72. MCR hired McLean to prepare the Allocation in 2012 in order to provide the necessary documentation for MCR's financial accounting of the acquisition of JB&A's assets. *See*, *e.g.*, A. 824-25, 895; A. 2071-72. The Allocation assumes that the fair value to MCR of the acquired assets equals the total anticipated purchase price—the cash price that MCR paid plus the

probability-weighted "price" of the earnouts. A. 2071-2074, 2080; *see also* A. 2082 ("It is assumed that the purchase price is at Fair Value."). The Allocation in turn estimates the purchase price at $54.7 million, based on a series of additional assumptions about JB&A's "Forecasted Revenue Growth," A. 2083, and the probability of JB&A achieving that growth, *see* A. 2128.

But even if otherwise sound, those assumptions and probabilities projected the performance of JB&A's business only *as part of MCR*.[3] Indeed, because the earnouts would be paid (or not paid) based on the performance of JB&A's business as part of MCR, their probability-weighted "price" could not be used to measure JB&A's value as a standalone business. That is, after all, why McLean cautioned that the Allocation is not a "valuation opinion" and "should not be used for any other purpose" than to supply a fair value of the acquired assets for MCR's U.S. GAAP obligations. A. 2071-72; *see also* A. 921 (JB&A's expert agreeing that he "would not offer [himself] to the Court as an expert on valuations"). JB&A needed to establish its value as a *standalone business* in order to prove that it would have

[3] *See*, *e.g.*, A. 1949 (depicting purchase price attributable to "Strategic Value of JB&A to MCR"); A. 2077 ("JB&A will be immediately integrated into the MCR Federal structure" and "MCR will provide the platform necessary to synergistically expand our support to our customers in the federal government."); A. 2500 (JB&A's counsel: "There was value in adding JB&A to MCR's business. We agree with that."); *accord In re IBP, Inc. S'holders Litig.*, 789 A.2d 14, 83 & n.202 (Del. Ch. 2001); A. 844; A. 1040; A. 1093.

been better off had it refused MCR's $42.7 million payment and not closed on May 31, 2011.

Moreover, even if the Allocation could be used to establish the fact of damages (and it cannot), it says nothing about who *caused* those damages. In *SunTrust Bank v. Farrar*, this Court held that an inflated property appraisal, without evidence of a willing buyer at that price, is legally insufficient to prove "that anything the [defendant] did or did not do caused any damage to the [plaintiffs]" by selling the property for less than the appraised price. 277 Va. 546, 555-56 (2009). So too here: the Allocation's fair value "price" for JB&A's business, absent evidence of another willing buyer at that price, cannot by itself establish that MCR caused any damages as a matter of law. The most it shows is that MCR paid a premium for JB&A's business—a premium that no other buyer was willing to pay. *See Interim Healthcare, Inc. v. Spherion Corp.*, 884 A.2d 513, 549-50 (Del. Super. Ct. 2005) (rejecting the "circular proposition" that company was "worth $134 million because that is what the plaintiffs paid for it").

In opposing review by this Court, JB&A offered several reasons why its failure of proof should be excused, but none is availing. There is simply no record to support a contention that MCR's January 2011 letter of intent "precluded JB&A from discussing a sale transaction with other buyers," and should excuse JB&A from identifying other willing buyers at MCR's purchase price. Brief in

Opposition 18. In fact, JB&A accepted MCR's letter of intent only *after* it knew there were no other offers. A. 2045. That is why JB&A's investment banker reported that "61 potential acquirers *were contacted*" and the "exhaustive marketing process *was completed*." A. 1948 (emphases added). MCR made the *only* written offer.

JB&A is also wrong that "[a]ny uncertainty or imprecision about which MCR complains was a self-inflicted wound, caused by its own fraud and deceit." Brief in Opposition 18. The issue here is JB&A's failure to prove the causation element of its claims for breach of contract and constructive fraud. A plaintiff, of course, cannot prove an essential element of its claims by assuming the defendant's ultimate liability. Nor, for that matter, does JB&A's failure of proof turn on the trial judge's observations on witness demeanor and credibility; all of the issues on which this Court has granted review are issues of law.

In light of the Allocation's legal insufficiency in proving causation of damages, it is striking that the trial court disregarded the only direct evidence of JB&A's value as a standalone business—the ESOP valuation. Six months before closing, JB&A's own investment bank valued the standalone company at $37.6 million using a discounted cash-flow analysis. A. 1997-98. To be sure, JB&A's "value increased because MCR, as a willing buyer, was willing to pay more for the business than as a standalone entity would command from a valuation standpoint."

A. 1078. That simply means MCR paid *a premium* to reflect strategic value to MCR. Since there is no evidence of another buyer willing to pay such a premium, the only other possible measure of damages is JB&A's value as a going concern: the $37.6 million ESOP valuation. And because JB&A received well more than that amount, it has not shown that MCR caused JB&A any damages.

Without legally sufficient proof of causation, any award of damages is a windfall—and that is exactly what JB&A received. Legally sufficient proof of causation is an essential safeguard against the arbitrary imposition of liability and the unjustified reputational injury that can accompany it. If not corrected, the trial court's erroneous judgment and arbitrary award of damages, untethered to any legal violation by MCR, would harm the business climate in Virginia and undermine confidence in the Commonwealth's legal system. The judgment below, based on a legally insufficient causation finding, should be reversed.

3. The trial court erred in awarding damages based upon a "purchase price allocation" calculation that was inherently speculative. (Assignment 3)

Standard of Review

A trial court's damages award following a bench trial will be reversed if it is "plainly wrong or without evidence to support it." *SunTrust*, 277 Va. at 554. Similarly, under Delaware law, a damages award for breach of contract is reviewed

for abuse of discretion, and underlying factual findings are reviewed for clear error. *Reserves Dev. LLC v. Crystal Props., LLC*, 986 A.2d 362, 367 (Del. 2009).

Discussion

"[D]amage calculations based on unsupported projections are improper." *SunTrust*, 277 Va. at 555. Here, as noted, the trial court awarded damages as the difference between the $54.7 million purchase price allocation and the $42.7 million in cash paid by MCR—a difference equal to the probability-weighted "price" of the earnouts. A. 2518, 2529. But that "price" was entirely unsupported and speculative for at least three independent reasons, each of which renders the damages award legally erroneous.

First, the Allocation estimated a "price" for the earnouts based upon highly speculative and unduly optimistic projections of JB&A's future revenues that all parties—and the trial court—have disavowed. In 2010, when JB&A engaged McLean to sell JB&A's business, McLean prepared a Confidential Business Memorandum containing an overly optimistic projection of JB&A's future revenues supplied by JB&A executives. A. 1876. JB&A later disavowed those projections when key business prospects failed to materialize. A. 1988 (JB&A noting that "we cannot proceed to closing without acknowledging our revised projections"); *see also* A. 799; A. 911-12. Yet in 2012, when MCR retained McLean to prepare the Allocation, McLean used those *same* inflated and

disavowed projections of future revenues as a basis for allocating the purchase price of JB&A. *See* A. 1871-1905.

MCR's counterclaim for fraudulent inducement alleged that JB&A hoodwinked MCR with these projections by presenting an unduly rosy picture of JB&A's business prospects in an effort to sell the company. The court rejected that counterclaim after trial, ruling that JB&A's projections were of little value, *see* A. 2341-42, 2352, 2359, and were not believed by MCR, *see* A. 2318-19, 2333. Indeed, the court found that the inflated projections were "merely projecting a hopeful outcome," A. 2352, and found credible two JB&A witnesses who disavowed the inflated projections at trial, *see* A. 2312-13, 2343-44; *see also* A. 753-54, 755-56 (Knight); A. 911 (Yount).

But these same discredited projections were the basis for the Allocation, and hence for the court's flawed damage award. *Compare* A. 1890, *with* A. 2084, 2100; *see also* A. 1072-76. The court used the Allocation as evidence of the "value" that JB&A would have retained but for the alleged breach; yet, incongruously, the court also ruled that the imaginary world in which JB&A actually received the earnouts was merely a "hopeful outcome" and speculative. Not only were those two rulings flatly inconsistent, but there was no evidence supporting JB&A's inflated projections.

Awarding damages based on the Allocation was flatly contrary to this Court's decision in *SunTrust*, which held that a property appraisal was insufficient as a measure of damages in the absence of competent evidence that a market existed for the property at the appraised price. 277 Va. at 554-55. The appraisal in *SunTrust* was the product of an "undisputed . . . expert appraiser and engineer." *Id.* at 550 n.4. Yet this Court held that the undisputedly reliable appraisal was not enough, and reversed the trial court's judgment were the plaintiff had not provided independent evidence of a "viable market" for the property at the appraised price. *Id.* at 555. As in *SunTrust*, the Allocation's speculative and "unsupported projections" could never serve as the basis of a valid damage award. *Id.*

Nor does it matter that MCR itself commissioned the Allocation in 2012. In *SunTrust*, the property appraisal was also commissioned by the defendant Trustee "to assist in the sale of the Coal Mine." Br. of Appellant, No. 080550, 2008 WL 6722321, at *8 (Va.). This Court explained that the "goal of an appraisal is to reflect the fair market value of the subject property." 277 Va. at 556. Yet even though the defendant prepared the appraisal *specifically* for the purpose of estimating the fair market value of the property, this Court held that the appraisal was not sufficient as a basis for awarding damages.

Here, in contrast, MCR did not commission the Allocation for the purpose of estimating the fair market value of JB&A's standalone intelligence business. On

its face, the Allocation estimates only the "Fair Value of the identified intangible assets for U.S. GAAP reporting purposes," and "should not be used for any other purpose." A. 2071. The Allocation thus is even less appropriate as a measure of damages than the legally insufficient appraisal in *SunTrust*.

Second, the Allocation could not serve as a basis for awarding damages because, as noted, the "price" of the earnouts depended upon the performance of JB&A's business as part of MCR—not as a standalone business. Indeed, the very reason the parties agreed on contingent earnouts instead of additional cash at closing is because they could not agree that the earnouts represented any part of JB&A's value at the time of closing, but merely the *potential* value of "opportunities that [JB&A] had identified for [MCR] to grow the business beyond what [MCR was] paying for." A. 1051. The earnouts therefore provided no support for the trial court's award of damages based on supposed lost "value" to JB&A.

The court's erroneous use of the "price" of the earnouts to award damages is even less defensible than the use of a real-estate appraisal to award damages that this Court in *SunTrust* held was "improper." 277 Va. at 555. The error was not that the Allocation's *methodology* was flawed; indeed, this Court never questioned the methodology that the expert appraiser employed in *SunTrust*. Rather, the fundamental error was that the Allocation failed to measure what JB&A needed to

prove under its theory of the case: the value of JB&A's standalone business at the time of the closing. At a bare minimum, JB&A was required to introduce evidence of a "willing buyer" at the Allocation's $54.7 million "price" before the court could use that figure as the basis for awarding damages. *Id.* But there was no evidence of another buyer at that price, and not even MCR was willing to pay that amount in cash to close the transaction.

The trial court misapprehended this fatal flaw in JB&A's damages theory by suggesting that the Allocation was "more conservative" than pie-in-the-sky testimony by JB&A's founder and chairman that he would not have sold the business for "less than $60 million to any other buyer." A. 2515. But even the court could not find that subjective testimony a sufficiently reliable measure of damages, A. 2517-18, especially since there was no evidence of a willing buyer at anywhere near that price. In any event, the existence of other erroneous measures of damages does not mean the Allocation is reliable by default; it means that JB&A has failed to prove its damages.

Third, MCR's own financial reporting confirms that the earnouts were treated as an entirely speculative accounting entry. *See* A. 1674-75; A. 2167. JB&A urged the court to award damages based on the Allocation because MCR "used it in their financial statements." A. 2411. In adopting JB&A's argument, the trial court found it significant that MCR "accepted" the Allocation "as accurate

and true." A. 2520. Not only was that finding irreconcilable with the court's determination that MCR did not believe the inflated projections that underpinned the Allocation, A. 2358-59, but it was also inconsistent with MCR's own financial reporting.

In MCR's 2011 and 2012 financial reporting, for example, the footnotes discussing the acquisition reported that anticipated income for the business acquired from JB&A "is subject to change." A. 1675; A. 2167. The footnotes further reported that "management believes that no earn out will be paid" and thus "the Company has adjusted its accrued earn out liability of $11,995,002 to zero." A. 1675; A. 2167. These statements, and the undisputed fact that MCR immediately wrote down the earnouts, belie any suggestion that the Allocation's "price" for the earnouts reflected MCR's view of the "true" or "accurate" value for the acquired assets, or somehow constituted an admission by MCR.

The Allocation—based on disavowed, jettisoned projections—was JB&A's only evidence of its damages. The trial court's unsupported damages award, if not reversed, would encourage Virginia courts to pile speculation upon speculation in awarding damages. This Court should reaffirm *SunTrust Bank*'s holding that damages awards based on unsupported, speculative projections are improper.

4. The trial court erroneously awarded attorneys' fees as "equitable" relief on JB&A's constructive-fraud count. (Assignment 4)

Standard of Review

This Court reviews for abuse of discretion a trial court's discretionary award of equitable relief. *Bershader*, 258 Va. at 92. "The abuse-of-discretion standard includes review to determine that the discretion was not guided by erroneous legal conclusions," and a trial court "by definition abuses its discretion when it makes an error of law." *Porter v. Commonwealth*, 276 Va. 203, 260 (2008) (quotations omitted).

Discussion

The American rule should be uncontroversial. *See Piney Meeting House Invs., Inc. v. Hart*, 284 Va. 187, 196 (2012) ("attorneys' fees are [ordinarily] not recoverable by a prevailing litigant in the absence of a specific contractual or statutory provision to the contrary"). It applies by default in all cases where this Court has not expressly recognized an exception. But the trial court misapplied a narrow exception recognized in *Prospect Development Co. v. Bershader* for courts sitting in equity to award equitable relief on an actual-fraud claim when necessary to prevent a "hollow" victory. 258 Va. at 93.

In *Bershader*, homeowners sued a developer in equity for actual fraud and obtained an easement by estoppel against the developer, who had falsely promised them he would not develop the adjacent lot. 258 Va. at 80, 87. In affirming the

equitable easement, this Court also approved the chancellor's award of attorneys' fees in order to prevent a "hollow" victory for the plaintiffs, who had incurred more than $151,000 in attorneys' fees to obtain their equitable relief. *Id.* at 92-93. In authorizing this narrow, equitable exception to the American rule, this Court reaffirmed that the "[t]he general rule in this Commonwealth is that in the absence of a statute or contract to the contrary, a court may *not* award attorney's fees to the prevailing party." *Id.* at 92 (emphasis added).

The trial court, in seeking to find a basis for awarding fees, repeatedly and incorrectly stated that the law is "in flux." A. 2421, 2529. The court ultimately believed that it "was sitting in equity on the fraud claim," and that its award of money damages for constructive fraud "was restitutionary in nature and its purpose was to restore to the plaintiffs the value of what was lost by virtue of the defendant's fraud." A. 2584.

But this is not a case in equity, and a court does not exercise that power simply by labeling its award of damages "equitable." Rather, by awarding only money damages, the trial court awarded *legal* relief. *See*, *e.g.*, *Love v. Kenneth Hammersely Motors Inc.*, 263 Va. 45, 48 (2002) ("When a party seeks solely monetary damages caused by another's tortious conduct, he must bring his action on the law side of the court . . . .") (quotation marks omitted); *accord Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 212-13 (2002) (award of money

is legal relief unless that award requires one party to turn over certain specific funds improperly obtained).

Significantly, JB&A *never* pleaded a claim for equitable relief, *see* A. 140 (Prayer for Relief), and with good reason. Where plaintiffs "seek only money damages," and "are not seeking rescission or any other equitable relief," the trial court "is not sitting as a court of equity, but rather as a court of law." *Oswald v. Holtzman*, 90 Va. Cir. 9, 12 (Va. Cir. Ct. 2015); *accord Knudson*, 534 U.S. at 212-13; 1 Restatement (Third) of Restitution and Unjust Enrichment § 4(d), at 32. And because "neither the Virginia General Assembly nor the Supreme Court of Virginia has created or recognized an exception to the American Rule allowing an award of attorneys' fees in this circumstance," the trial court was "constrained to deny the request for fees." *Oswald*, 90 Va. Cir. at 12.

The trial court expressly "disagree[d] with" *Oswald*. A. 2583. But the *Oswald* court considered this precise question and correctly concluded that nothing in *Bershader* supports the view "that attorneys' fees may be awarded whenever fraud is proven, regardless of whether the equitable powers of the court are invoked." 90 Va. Cir. at 11. That conclusion applies with special force here, where MCR was found liable for constructive fraud and not, as in *Bershader*, for actual fraud. JB&A has not cross-appealed the trial court's rejection of its actual-

fraud claim, thereby conceding its failure to prove intentional fraud. This Court has never authorized fee shifting in a constructive-fraud case.

Even if the trial court had discretion to award equitable attorneys' fees to supplement money damages for constructive fraud, it would have abused that discretion in awarding fees here. JB&A already received a windfall from the $12 million damages award—on top of the $42.7 million in cash it received for the sale of a business it valued internally at only $37.6 million. JB&A is a sophisticated corporate entity, advised and represented by highly experienced corporate lawyers and investment bankers, and consciously entered into a contract to sell its business that did not include a fee-shifting provision. Further, the trial court made clear that it "did not award attorneys' fees as sanctions" against MCR. A. 2646; *see also* A. 2659. In short, no special circumstances outside the ordinary expense of litigation justified applying *Bershader*'s narrow exception here.

The trial court's misapplication of *Bershader*, if left to stand, would create a gaping exception that would swallow the American rule. A court could simply declare any award of money damages "equitable" relief in order to award attorneys' fees in the court's discretion. The trial court's award of fees was a repudiation of the American rule, as well as an unwarranted expansion of *Bershader* to apply to judgments involving only constructive fraud. The award of attorneys' fees should be reversed.

5. The trial court erred in failing to require JB&A to elect between incompatible legal and equitable remedies. (Assignment 5)

Standard of Review

Whether a plaintiff is required to elect between legal and equitable remedies is a question of law reviewed de novo. *Wilkins v. Peninsula Motor Cars, Inc.*, 266 Va. 558, 560 (2003).

Discussion

Finally, the trial court added $3.7 million in prejudgment interest to the $12 million in damages on the breach-of-contract count. Rather than require JB&A to elect between a legal remedy for its breach-of-contract count and an "equitable" remedy for its constructive-fraud count, the court entered a judgment awarding *both*. That is, the court entered a single award of $12 million in compensatory damages for both the contract and fraud counts, plus $1.9 million in equitable attorneys' fees on the fraud remedy, plus $3.7 million in interest on the contract damages. This stacking of inconsistent legal and equitable awards runs counter to Virginia's law of remedies and should be reversed.

"Where there is an adequate remedy at law, *i.e.*, damages, the plaintiff may not seek an equitable remedy." *Newman v. Freeman Homes, Inc.*, 89 Va. Cir. 377, 2014 WL 10520419, at *3 (Va. Cir. Ct. 2014) (citing *Yancey v. Fenwick*, 4 H. & M. (14 Va.) 423 (1809)). A plaintiff awarded legal and equitable remedies generally must elect between them. *See Jennings v. Realty Developers, Inc.*, 210

Va. 476, 482 (1970). This requirement survives the merger of law and equity courts, which preserved "in all respects the distinctions between law and equity." Kent Sinclair & Leigh B. Middleditch, Jr., *Virginia Civil Procedure* § 1.15 at 53 (6th ed. 2014).

After awarding equitable attorneys' fees, the trial court expressly "d[id] not find that an award of prejudgment interest on the fraud claim is necessary to make the plaintiff whole or to provide complete equitable relief." A. 2594. Stated differently, the court found that the $13.9 million in damages and fees on the fraud count was adequate to make JB&A whole. Inasmuch as the court awarded even more in damages and interest—$15.7 million—on the breach-of-contract count, it was plainly inappropriate for the court to award a *further* $1.9 million in attorneys' fees. The court handed JB&A windfall upon windfall.

The trial court's cumulative awards were particularly inappropriate because they awarded relief on inconsistent theories of liability. JB&A sued on the Asset Purchase Agreement to obtain legal damages for breach of contract. As the litigation progressed, however, JB&A sought to repudiate that contract and obtain parallel "equitable" relief for fraudulent inducement in the closing of that contract. And while the trial court acknowledged that this inconsistency presented "a difficult question," A. 2684, the court dodged the question by characterizing the equitable relief as "restorative" and thus "not inherently in conflict with the legal

award on the breach of contract claim," A. 2688. But JB&A should have been required to elect between its inconsistent remedies—to embrace the contract or repudiate it—rather than reap the best of both worlds.

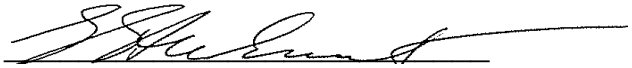
The trial court fundamentally misapprehended the law of remedies. A party who is made whole by an award of damages has no claim to equity. The trial court's stacking of legal and equitable remedies, if upheld, would incentivize courts to award arbitrary windfalls and would frustrate business expectations. This Court should reaffirm that courts generally may not award equitable relief on top of an adequate legal remedy, especially where (as here) those remedies flow from inconsistent theories of liability.

CONCLUSION

The legal issues in this appeal do not turn on the trial court's one-sided liability findings and credibility assessments. To be sure, MCR vigorously disagrees with the trial court's unnecessary and pejorative observations on the good-faith actions and truthful testimony of the company's dedicated employees who have an unblemished track record of ethical service. Even accepting those observations, however, would not justify JB&A's eight-figure damages award or the stacking of inconsistent equitable and legal relief. The trial court's repeated legal errors worked a gross injustice on MCR while handing JB&A a windfall.

MCR respectfully requests that this Court reverse the judgment and enter final judgment for MCR on both the breach-of-contract and constructive-fraud counts, because JB&A failed to prove the essential causation and damages elements of each. Alternatively, the Court should reverse the constructive-fraud count, or require JB&A to elect between its legal and equitable remedies. And, at a minimum, the Court should vacate the award of "equitable" attorneys' fees.

Dated: May 22, 2017



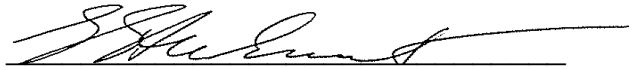
L. Steven Emmert (VSB No. 22334)
SYKES, BOURDON, AHERN & LEVY, P.C.
281 Independence Boulevard, 5th Floor
Virginia Beach, Virginia 23462
Telephone: (757) 499-8971
Facsimile: (757) 456-5445
emmert@virginia-appeals.com

Miguel A. Estrada (pro hac vice)
John C. Millian (pro hac vice)
Lucas C. Townsend (pro hac vice)
Laura R. Cole (VSB 83763)
Andrew B. Davis (pro hac vice)
GIBSON, DUNN & CRUTCHER LLP
1050 Connecticut Avenue, N.W.
Washington, D.C. 22036
Telephone: (202) 995-8500
Facsimile: (202) 467-0539
MEstrada@gibsondunn.com
JMillian@gibsondunn.com
LTownsend@gibsondunn.com
LCole@gibsondunn.com
ADavis@gibsondunn.com

CERTIFICATE

I hereby certify that on this 22nd day of May, 2017, pursuant to Rules 5:26 and 5:32(a)(3)(i), three paper copies of the Brief of Appellant and Appendix were hand-filed with the Clerk of the Supreme Court of Virginia and electronic copies of the Brief and Appendix were filed, via VACES. On this same day, an electronic copy of the Brief of Appellant was served, via email, and electronic copies on CD of the Brief and Appendix were served, via UPS Ground Transportation, upon:

David Barger, Esq.
Michael R. Sklaire, Esq.
GREENBERG TRAURIG, LLP
1750 Tysons Boulevard, Suite 1200
McLean, Virginia 22102
Telephone: (703) 749-1300
Facsimile: (703) 749-1301
bargerd@gtlaw.com
sklairem@gtlaw.com
Counsel for Appellee JB&A, Inc.



L. Steven Emmert