

SPECIAL TOPICS

Competitive Sourcing

Application of A-76 to In-House Performance after Contract Expires

Although the Office of Management and Budget (OMB) published its revised version of OMB Circular A-76 [Revised A-76]¹ over two years ago, there are still some unanswered questions concerning its application under certain circumstances. Specifically, one unresolved question is whether the Revised A-76 applies to in-house performance of a commercial activity² after the expiration of a contract resulting from an earlier standard competition³ or cost comparison.⁴

In *LABAT-Anderson, Inc. v. United States*,⁵ the plaintiff (LABAT) requested that the Court of Federal Claims (COFC) enjoin the government from allowing in-house employees to perform work LABAT had been performing under a contract. LABAT alleged⁶ the agency violated the Revised A-76,⁷ 32 C.F.R. Parts 169 and 169a, Exec. Order No. 12,615, and 10 U.S.C. § 2462 by permitting in-house employees to perform a commercial activity after the expiration of a contract resulting from a cost comparison under “Old” A-76.⁸ Because the COFC concluded that the agency did not violate these sources of law, it denied LABAT’s request for an injunction.⁹ Significantly, the COFC found that in this case, the agency was not required to follow the detailed Revised A-76 procedures in deciding who should perform a commercial activity after the contract expired.¹⁰

In May 2001, after conducting a cost comparison under the “Old” A-76, the Defense Logistics Agency (DLA) awarded a contract to LABAT for the performance of distribution services at a depot in Cherry Point, North Carolina.¹¹ On 30 September 2004, after some disagreement over contract pricing, the DLA formally notified LABAT that it would not exercise the option to extend the term of the contract.¹² The contract was scheduled to expire on 30 November 2004.¹³

Prior to performing this work in-house, the DLA conducted an informal cost study¹⁴ comparing the cost of government performance to the cost of LABAT’s performance.¹⁵ This informal cost study did not strictly comply with the

¹ U.S. OFF. OF MGMT. & BUDGET, CIRCULAR NO. A-76 (REVISED), PERFORMANCE OF COMMERCIAL ACTIVITIES (2003) [hereinafter REVISED A-76]. See also Office of Mgmt. & Budget, Revision to Office of Management and Budget Circular No. A-76, Performance of Commercial Activities, 68 Fed. Reg. 32,134 (May 29, 2003).

² *Id.* attach. A, ¶ B.2. A “commercial activity” is a “recurring service that could be performed by the private sector and is resourced, performed, and controlled by the agency through performance by government personnel, a contract, or a fee-for-service agreement.” *Id.*

³ *Id.* ¶ 4. Revised A-76 requires agencies to perform either streamlined or standard competitions to determine whether it is more economical for government personnel or a contractor to perform a commercial activity. The term the OMB now uses to describe the procedures under Revised A-76 that agencies must follow to study a commercial activity is “competitive sourcing.” *Id.*

⁴ RSH, *infra* note 8, app. 1. A “cost comparison” is a term that the previous version of OMB Circular A-76 used to describe “the process whereby the estimated cost of government performance of a commercial activity is formally compared . . . to the cost of performance by commercial . . . sources.” *Id.*

⁵ 65 Fed. Cl. 570 (2005).

⁶ *Id.* at 573.

⁷ REVISED A-76, *supra* note 1. Revised A-76 requires federal agencies to conduct competitions of commercial activities currently performed by government personnel to determine whether private sector performance or government performance would be less expensive. At the conclusion of a Revised A-76 competition, if the agency finds that contract performance is cheaper, then the agency awards a contract to a contractor. Conversely, if the agency finds that government performance is cheaper, then the agency issues a “letter of obligation” to the “official responsible for performance of the MEO.” *Id.* attach B, ¶ D6.

⁸ U.S. OFF. OF MGMT. & BUDGET, CIRCULAR NO. A-76, PERFORMANCE OF COMMERCIAL ACTIVITIES (1999) [hereinafter OLD A-76] and U.S. OFF. OF MGMT. & BUDGET, CIRCULAR NO. A-76, REVISED SUPPLEMENTAL HANDBOOK, PERFORMANCE OF COMMERCIAL ACTIVITIES (1996) [hereinafter RSH]. Revised A-76 replaced and superseded “OLD” A-76 for streamlined and standard competitions commenced after its effective date.

⁹ *LABAT*, 65 Fed. Cl. at 581-82.

¹⁰ *Id.* at 587-89.

¹¹ *Id.* at 572-73.

¹² *Id.*

¹³ *Id.*

¹⁴ *Id.* at 579-80. In conducting its informal cost study, the DLA used the software it would have used to perform a cost comparison under Revised A-76. The DLA’s informal cost study consisted of a comparison of the costs of personnel, supplies, material, and other costs. *Id.*

Revised A-76 procedures.¹⁶ The DLA concluded that performance in-house would be cheaper than performance by LABAT.¹⁷ The DLA then informed LABAT that it would perform the distribution service work with government employees until the DLA could resolicit and award a new contract.¹⁸

LABAT requested the COFC enjoin the DLA from utilizing its in-house employees to perform the distribution services that LABAT had been performing under contract.¹⁹ LABAT alleged that in-house performance of this work violated the sources of government procurement authority listed above.²⁰

The DLA moved to dismiss for lack of jurisdiction, arguing that LABAT did not have standing under the Tucker Act to file suit because the case did not involve a pending procurement.²¹ Although the COFC found that this case did not concern a solicitation or the award of a contract, the case concerned the “decision by the Government not to conduct a solicitation.”²² As such, the court found that it had jurisdiction over an “alleged violation of statute or regulation in connection with a procurement.”²³ Additionally, the COFC found LABAT was an interested party under the Tucker Act and had standing.²⁴ After concluding that it had jurisdiction under the Tucker Act,²⁵ the COFC reviewed the merits of LABAT’s request for an injunction.²⁶

The COFC commented that the Department of Defense (DOD) is required by statute to acquire services from commercial sources if these sources can provide them at a cost that is lower than government sources can provide.²⁷ Although the statute does not specify how to compare the cost of private versus public performance, it states that the DOD “shall ensure that all costs considered are realistic and fair.”²⁸

Apply the facts of this case, the court found that even though the DLA did not conduct a competition strictly in accordance with the Revised A-76 procedures, the DLA complied with the statutory requirement because the DLA’s informal cost study was “realistic and fair.”²⁹ In making its determination, the COFC determined that the DLA used the same computer software that it ordinarily uses to conduct competitions pursuant to the Revised A-76.³⁰ The COFC also found that

¹⁵ *Id.* at 579.

¹⁶ *Id.* at 580. For instance, Revised A-76 requires that the agency calculate the cost of overhead (personnel costs multiplied by twelve percent) in determining the total cost of agency performance. Nevertheless, the DLA did not add the cost of overhead into its calculations. *Id.*

¹⁷ *Id.* at 579. The DLA determined that the cost of performance by LABAT would be \$425,000 per month, while the cost of in-house performance would be \$365,475.50 per month. *Id.*

¹⁸ *Id.* at 573.

¹⁹ *Id.*

²⁰ *Id.* LABAT originally filed suit in the District Court for the District of Columbia but the case was transferred to the COFC because only the COFC has jurisdiction under the Tucker Act. *Id.* at 572.

²¹ *Id.* at 575.

²² *Id.* The Tucker Act, 28 U.S.C. § 1491(b)(1), states the COFC has jurisdiction:

[T]o render judgment on an action by an interested party objecting to a solicitation by a Federal agency for bids or proposals for a proposed contract or to a proposed award or the award of a contract or any alleged violation of statute or regulation in connection with a procurement or a proposed procurement.

See 28 U.S.C.S. § 1491(b)(1) (LEXIS 2005).

²³ *LABAT*, 65 Fed. Cl. at 581-582 (citing 28 U.S.C.S. § 1491(b)(1)).

²⁴ *Id.* at 575. The COFC referred to the Competition in Contracting Act (CICA), 31 U.S.C. § 3551(2)(A), for the definition of “interested party” (citing the Act’s definition as “[a]n actual or prospective bidder or offeror whose direct economic interest would be affected by the award of the contract or the failure to award the contract”). *Id.* The COFC found LABAT to be an interested party under the CICA because DLA’s decision not to exercise the option extending the term of its contract with LABAT affected LABAT’s direct economic interest. *Id.*

²⁵ *Id.* at 575-76.

²⁶ *Id.* at 575-77. Specifically, LABAT argued that the DLA violated Title 10 U.S.C. § 2462, Revised A-76, 32 C.F.R. Parts 169 and 169a, and Executive Order 12,615. *Id.* at 573.

²⁷ 10 U.S.C.S. § 2462 (LEXIS 2005).

²⁸ *Id.*

²⁹ *LABAT*, 65 Fed. Cl. at 570, 579.

³⁰ *Id.* at 580.

the DLA reasonably compared the personnel costs, material costs, and supply costs of both parties before determining that performance by in-house personnel would be cheaper than performance by LABAT.³¹

The COFC also commented that both federal regulatory provisions and the Revised A-76 procedures echo the statutory preference that agencies perform commercial activities with private sector employees if performance by private contractors is less costly than performance by government employees.³² In particular, procurement regulations require the government to compare the cost of government performance versus contractor performance to determine which alternative would be the better value for the government.³³ For instance, one provision states that agencies shall perform commercial activities with commercial sources if the “services can be procured more economically” with commercial sources than with government employees.³⁴ The stated purpose of this series of regulations is to update DOD policies regarding “commercial activities” as “required by E.O. 12615 and OMB Circular A-76.”³⁵ Additionally, DOD’s installation commanders are affirmatively required to conduct “cost comparisons” pursuant to OMB Circular A-76.³⁶

In applying the regulatory provisions and the Revised A-76 to this case, the court found the circular, as an executive policy, is relevant to the DOD only to the extent that the aforementioned federal regulations incorporate it.³⁷ The court stated that these federal regulations do not address a situation, as here, where the government has not completed a resolicitation prior to the expiration of a contract resulting from an earlier A-76 study.³⁸ As such, the court found that under the circumstances of this particular case, the federal regulations did not incorporate the Revised A-76 procedures. Thus, in its analysis of the DLA’s informal cost study, the court referred to the broad procedural rules located in Title 32, Parts 169 and 169a versus the more draconian rules of Revised A-76.³⁹ Consequently, the court stated that in this case, “we have found Circular A-76 inapplicable.”⁴⁰

Agency heads are also required by Executive Order 12,615 to perform commercial activities with private sector employees if such activities “could be performed more economically by private industry.”⁴¹ Although LABAT argued that the DLA violated this order, the court opined that the executive order does not provide the court with a “meaningful standard of review.”⁴² Additionally, the court stated that it viewed this executive order as akin to an internal “memorandum within the Executive Branch.”⁴³ Consequently, the COFC rejected this basis of LABAT’s argument.⁴⁴

In summary, after reviewing the bases of LABAT’s argument that the DLA improperly permitted in-house personnel to perform a commercial activity after the expiration of the contract between the DLA and LABAT, the COFC rejected it. In short, the court was satisfied that the DLA complied with the statutory and regulatory authority, even if it did not comply with Revised A-76. It is debatable that the COFC correctly applied the relevant procurement authorities to the facts of this case.⁴⁵ While 10 U.S.C. § 2462 places few requirements upon agencies conducting analyses of the cost of private versus government performance of commercial activities, the aforementioned federal regulations and the Revised A-76—taken together—impose strict requirements for conducting a competition. The COFC opined that the Revised A-76

³¹ *Id.*

³² 32 C.F.R. § 169 (1989) and 32 C.F.R. § 169a (1992).

³³ *Id.* § 169.4 (1989).

³⁴ *Id.*

³⁵ *Id.* § 169.1.

³⁶ *Id.* § 169.5.

³⁷ *LABAT*, 65 Fed. Cl. at 577.

³⁸ *Id.* at 579.

³⁹ *Id.* at 578-79.

⁴⁰ *Id.* at 580.

⁴¹ Exec. Order No. 12,615, 52 Fed. Reg. 44,853 (Nov. 23, 1987).

⁴² *LABAT*, 65 Fed. Cl. at 580.

⁴³ *Id.*

⁴⁴ *Id.*

⁴⁵ 10 U.S.C.S. § 2462 (LEXIS 2005); Revised A-76, *supra* note 1, and 32 C.F.R. § 169 and 32 C.F.R. § 169a.

procedures applied to the DOD only insofar as 32 C.F.R. parts 169 and 169a incorporate it.⁴⁶ The court further stated that these regulations did not address the situation, as here, where the agency opts to perform a commercial activity with in-house employees after allowing a contract to expire.⁴⁷ Thus, the court argues that because the regulations do not address the specific facts of this case, the requirements of Revised A-76 also do not apply.⁴⁸

Conversely, it is conceivable that 32 C.F.R. Parts 169 and 169a do incorporate the Revised A-76.⁴⁹ For example, 32 C.F.R. 169.1(b) states that it “updates DOD policies and assigns responsibilities for commercial activities (CAs) as required by . . . OMB Circular A-76.”⁵⁰ Further, 32 C.F.R. 169.5(c) states that “installation commanders shall have the authority and responsibility to . . . conduct a cost comparison of those commercial activities selected for conversion to contractor performance under OMB Circular A-76.”⁵¹ Additionally, another regulation in the same series mandates that the DOD conduct another cost comparison⁵² if the cost of a post-cost comparison contract “becomes unreasonable or performance becomes unsatisfactory.”⁵³ While the COFC found this provision inapplicable to this case,⁵⁴ the provision is, arguably, applicable.⁵⁵ The above regulations’ direct references to OMB Circular A-76 do not purport to require DOD to follow only portions of the Revised A-76. Therefore, it appears that the above regulations require DOD to fully utilize all of the detailed Revised A-76 procedures—not just some of the procedures.

In this case, the DLA allowed the LABAT contract to expire after a lengthy dispute over contract costs.⁵⁶ The DLA apparently believed that the LABAT contract costs were too high. If the contract costs were unreasonable, then 32 C.F.R. § 169a.10 would require the DLA to resolicit using Revised A-76 procedures.⁵⁷ Thus, contrary to the COFC’s assessment, it is possible to interpret the above regulations as requiring the DOD to follow all of the procedures set forth in the Revised A-76.

Even assuming that the DOD is required to comply with the Revised A-76 under the circumstances of *LABAT*, it is worth noting that the Revised A-76 does not directly reference performance of a commercial activity by in-house personnel under these circumstances. The Revised A-76 only references in-house performance of an activity formerly performed by a contractor in the case where the agency terminated the previous contract.⁵⁸

The impact of the *LABAT* court’s holding is unclear. Nevertheless, the court found that in a case where the agency allows temporary in-house performance of a commercial activity following the expiration of a contract resulting from an earlier A-76 competition, the detailed procedures of Revised A-76 do not apply.⁵⁹ Put briefly, the court found in-house performance of such a commercial activity permissible without first performing a formal competition pursuant to the Revised A-76.⁶⁰ Whether agencies will have wider discretion in deciding whether to follow the Revised A-76 procedures is a question for future editions of the *Year in Review*.

⁴⁶ *LABAT*, 65 Fed. Cl. at 578.

⁴⁷ *Id.* at 581-82.

⁴⁸ *Id.* at 578.

⁴⁹ 32 C.F.R. § 169 and 32 C.F.R. § 169a (1989).

⁵⁰ 32 C.F.R. § 169.1 (emphasis added).

⁵¹ 32 C.F.R. § 169.5.

⁵² 32 C.F.R. § 169a.10. This regulation was implemented while “Old” A-76 was in effect and as such, it uses the term “cost comparison,” an “Old” A-76 term, rather than “competition,” a Revised A-76 term. *Id.*

⁵³ *Id.* This provision seems particularly relevant to the facts of this case in that in this case, DLA, arguably, found LABAT’s contract costs unreasonable. As such, this provision requires the agency to conduct another “cost comparison” (now called a “competition”) pursuant to OMB Circular A-76 to determine whether it would be more cost effective for a contractor or in-house employees to perform the commercial activity.

⁵⁴ *LABAT*, 65 Fed. Cl. at 570, 579. The court found this provision inapplicable because in this case, prices were not unreasonable and performance was not unsatisfactory. *Id.*

⁵⁵ *Id.*

⁵⁶ *Id.* at 573.

⁵⁷ 32 C.F.R. 169a.10 (1992).

⁵⁸ *Id.* attach. B, ¶ E.6. In addition to government employees, this provision states that the agency may also use interim contracts or public reimbursable sources to temporarily perform a terminated contract. Nevertheless, these temporary remedies may not be used for more than one year after the date of contract termination. *Id.*

⁵⁹ *LABAT*, 65 Fed. Cl. at 581-82.

⁶⁰ *Id.*

Old A-76 is Gone But Not Forgotten

Although the Revised A-76 became effective over two years ago, the GAO is still reviewing protests of performance decisions based on the “Old” A-76. Two separate series of protests pursuant to the “Old” A-76 are discussed below.

In two related protests filed by Johnson Controls World Services, Inc. (JCWS), the protester first⁶¹ requested the GAO recommend award to JCWS and later⁶² requested reimbursement for its protest costs. In the first protest, JWCS requested the GAO recommend award to it because the Army’s MEO failed to include all of the costs required for in-house performance and further, because the Independent Review Officer’s (IRO) certification of the cost estimate was unreasonable.⁶³ After the Army withdrew the IRO’s certification, the GAO dismissed the protest as academic.⁶⁴ In the second protest, JCWS requested GAO’s recommendation that the Army reimburse it for protest costs because the Army unduly delayed taking corrective action in response to the earlier meritorious protest.⁶⁵ The GAO agreed and sustained the second protest recommending that the Army pay protest costs.⁶⁶

In June 2000, the Army announced its intent to conduct a cost comparison pursuant to the “Old” A-76 of the base operations support services at Walter Reed Medical Center.⁶⁷ In June 2003,⁶⁸ the Army issued a solicitation to potential offerors.⁶⁹ Before receiving proposals, the Army submitted its most-efficient organization (MEO)⁷⁰ and cost estimates to the Army’s IRO,⁷¹ the Army Audit Agency.⁷² In April 2004, the IRO first certified the accuracy of the Army’s cost estimate and the MEO.⁷³ In July 2004, the Army modified the Performance Work Statement (PWS) and in September 2004, the Army made corresponding changes to the MEO.⁷⁴ The Army submitted the revised MEO to the IRO and in September 2004, the IRO certified the MEO again.⁷⁵ On 29 September 2003, the Army compared the cost of performance of the base support services by the MEO to the cost of performance by JWCS and determined that performance by the MEO would be less expensive.⁷⁶ JWCS filed an administrative appeal and then protested to the GAO.⁷⁷ On 30 March 2005, JWCS filed its second protest arguing that the Army’s MEO failed to include all of the costs of government performance of the MEO and as such, the IRO’s certification was improper.⁷⁸

⁶¹ Johnson Controls World Servs., Inc., Comp. Gen. B-295529.2, B-295529.3, Jun. 27, 2005, 2005 CPD ¶ 124 [hereinafter *Johnson Controls I*].

⁶² Johnson Controls World Servs., Inc.—Costs, B-295529.4, 2005 U.S. Comp. Gen. LEXIS 152 (Aug. 19, 2005) [hereinafter *Johnson Controls II*].

⁶³ *Johnson Controls I*, 2005 CPD ¶ 124, at 2.

⁶⁴ *Id.* at 3.

⁶⁵ *Johnson Controls II*, 2005 U.S. Comp. Gen. LEXIS 152, at *6.

⁶⁶ *Id.* at *19.

⁶⁷ *Johnson Controls I*, 2005 CPD ¶ 124, at 2.

⁶⁸ *Id.* The Army received permission from DOD to proceed with the cost comparison under “Old” A-76 even though Revised A-76 was in effect at the time of the solicitation. *Id.*

⁶⁹ *Id.*

⁷⁰ RSH, *supra* note 8, app. 1. The most-efficient organization (MEO) is the “government’s in-house organization to perform a commercial activity.” The MEO is based on the PWS and is, in effect, the government’s “offer” which is compared against a private sector offeror during the cost comparison process. *Id.*

⁷¹ RSH, *supra* note 8, appendix 1. Under “Old” A-76, the IRO must certify in writing that the government’s cost estimate for government performance of the commercial activity under study is accurate. Also, the IRO must ensure that the government’s most-efficient organization (MEO) is capable of performing the work described in the PWS. *Id.*

⁷² *Johnson Controls I*, 2005 CPD ¶ 124, at 2.

⁷³ *Id.*

⁷⁴ *Id.*

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ *Id.*

⁷⁸ *Id.*

Specifically, JWCS contended that the Army's MEO was based on "unrealistically low staffing levels to perform this work."⁷⁹ In response to the first protest, the GAO held a hearing on the merits of the case.⁸⁰ After the hearing, the Army requested that the GAO dismiss the protest "as academic" because the Army's IRO planned to withdraw its certification of the MEO. The GAO granted that request and dismissed the protest.⁸¹

JWCS filed its second protest on 16 June 2005 requesting the GAO recommend that the Army reimburse it for the costs associated with this protest and its previous protest.⁸² The GAO granted this request after finding that the Army failed to "investigate the substantive grounds of this protest," to "produce documents when required, and "to take prompt corrective action in the face of a clearly meritorious protest."⁸³ The GAO reported that the Army admitted that it did not fully investigate the basis of JWCS' protest.⁸⁴ The GAO found that despite the requirement that the agency produce documents in response to a protest no later than five days prior to filing its report, the Army did not produce these documents until more than seventy days later—the day before the protest GAO hearing.⁸⁵ Further, the GAO found that the Army never made any sincere attempt to take corrective action in this case.⁸⁶ For the above reasons, the GAO recommended that the Army reimburse JWCS for the reasonable costs of pursuing its protest, to include attorneys' fees.⁸⁷

In a separate series of cases, last year's *Year in Review*⁸⁸ discussed *Career Quest, a Division of Syllan Careers, Inc.*, where the GAO sustained Career Quest's (CQ) protest following a cost comparison under the "Old" A-76.⁸⁹ Following the first protest, CQ filed another protest involving the same cost comparison referenced above.⁹⁰ The GAO denied the protest.⁹¹

As discussed in last year's *Year in Review*,⁹² the GAO sustained CQ's first protest following a cost comparison under the "Old" A-76.⁹³ In that protest, the GAO found that the General Services Administration (GSA) improperly evaluated the cost of the MEO and also failed to include an adequate staffing plan.⁹⁴ Although the GAO sustained the protest, it did not recommend award of the contract to CQ because there were two issues that could affect the final cost comparison decision.⁹⁵ The GAO recommended that the GSA evaluate the MEO's staffing levels in the technical performance plan and the cost estimate, and then conduct another cost comparison.⁹⁶ In response to GAO's recommendations, the GSA revised the MEO and the cost estimate; then it completed another cost comparison, again finding that agency performance would be less expensive.⁹⁷ The GSA announced that it would perform the function in-house.⁹⁸

⁷⁹ *Johnson Controls II*, 2005 U.S. Comp. Gen. LEXIS 152, at *14.

⁸⁰ *Id.* at *5.

⁸¹ *Id.*

⁸² *Id.* at *6.

⁸³ *Id.* at *18.

⁸⁴ *Id.* at *16.

⁸⁵ *Id.* at *17.

⁸⁶ *Id.*

⁸⁷ *Id.* at *19.

⁸⁸ See Major Kevin J. Huyser et al., *Contract and Fiscal Law Developments of 2004—Year in Review*, ARMY LAW., Jan. 2005, at 121-22 [hereinafter *2004 Year in Review*].

⁸⁹ Comp. Gen. B-293435.2, B-293435.3, Aug. 2, 2004, 2004 CPD ¶ 152 [hereinafter *Career Quest I*]. In this case, the General Services Administration (GSA) conducted a cost comparison under "Old" A-76 of the services at GSA's National Customer Support Center for Federal Supply Schedule users. GSA determined that performance by the MEO would be less expensive. *Id.*

⁹⁰ *Career Quest, a Division of Syllan Careers, Inc.*, Comp. Gen. B-293435.4, Mar. 31, 2005, 2005 CPD ¶ 91 [hereinafter *Career Quest II*].

⁹¹ *Id.* at 1.

⁹² See *2004 Year in Review*, *supra* note 88, at 121-22.

⁹³ *Career Quest I*, 2005 CPD ¶ 152, at 1.

⁹⁴ *Id.* at 1.

⁹⁵ *Id.* at 6-7. First, the MEO's cost estimate was based upon 34.5 FTEs while the MEO's technical performance plan (TPP) was based upon 38.5 FTEs. Second, while the MEO's TPP referred to the American National Standard Institute/American Society for Quality (ANSI/ASQ) standard for the purposes of meeting the PWS's quality control call monitoring requirement, the MEO staffing plan did not provide enough FTEs to comply with this standard. *Id.* at 2-3.

⁹⁶ *Id.*

⁹⁷ *Career Quest II*, 2005 U.S. Comp. Gen. LEXIS 65, at 3.

CQ filed a second protest on the merits protesting GSA's decision.⁹⁹ CQ argued that (1) the MEO should not have been permitted to revise the technical performance plan (TPP) and the cost estimate, (2) the MEO did not include adequate staffing to perform the quality control program required by the PWS, (3) the MEO did not include adequate staffing to perform the call center operations as required by the PWS, (4) the MEO understated the hours for certain personnel in the staffing plan, and (5) the contracting officer showed improper bias in favor of the MEO.¹⁰⁰

The GAO found each basis of the protest without merit. Regarding GSA's revision of its TPP and cost estimate, the GAO did not consider this basis because it was untimely. CQ submitted its protest more than ten days after it knew or should have known that the GSA might revise its MEO and cost estimate.¹⁰¹ On the issue of the adequacy of the MEO's staffing for both quality control and operation of the call center, the GAO stated it had "no basis to object"¹⁰² to the agency's conclusions on these matters.¹⁰³ Regarding whether the MEO understated the hours for certain personnel in the MEO, the GAO found that to be incorrect.¹⁰⁴ Finally, the GAO found that CQ did not meet the standard of presenting "credible evidence that clearly demonstrates bias."¹⁰⁵ Thus, the GAO found that CQ failed to demonstrate sufficient evidence on all grounds and denied the protest.¹⁰⁶

The GAO's New Set of Bid Protest Rules

Last year, the *Year in Review*¹⁰⁷ discussed the agency tender official's (ATO's) limited protest rights in competitions involving more than sixty-five full-time equivalent (FTE) employees.¹⁰⁸ On 14 April 2005, the GAO amended its protest regulations pursuant to the changes the National Defense Authorization Act for Fiscal Year (FY) 2005 (NDAA FY05) made to the Competition in Contracting Act (CICA).¹⁰⁹ Consequently, the GAO's protest regulations now recognize as an interested party the official responsible for submitting the agency tender in a Revised A-76 competition involving more than sixty-five FTEs.¹¹⁰ Additionally, although not mentioned in the NDAA FY05, the GAO's regulations gave certain additional parties intervenor status.¹¹¹ Specifically, if an interested party files a protest of a competition involving more than sixty-five FTEs, then the GAO's regulations permit a individual "representing a majority of the employees of the federal agency who are engaged in performance of the activity or function" subject to the competition and the individual who submitted the agency tender to intervene in the protest.¹¹²

⁹⁸ *Id.*

⁹⁹ *Id.* at 1.

¹⁰⁰ *Id.* at 3-7.

¹⁰¹ *Id.* at 3.

¹⁰² *Id.* at 4-5.

¹⁰³ *Id.*

¹⁰⁴ *Id.* at 6.

¹⁰⁵ *Id.* at 7.

¹⁰⁶ *Id.* at 8.

¹⁰⁷ See 2004 *Year in Review*, *supra* note 88, at 116-17.

¹⁰⁸ National Defense Authorization Act for FY 2005, Pub. L. No. 108-375, § 326, 118 Stat. 1848 (2004) [hereinafter NDAA FY05]. The NDAA FY05 amended the definition of "interested party" for protests under the Competition in Contracting Act (Pub. L. No. 98-369, Title VII, § 2701, 98 Stat. 1175) to include the "official responsible for submitting the Federal agency tender in a public-private competition" completed pursuant to Revised A-76 regarding an activity performed by more than 65 FTEs. 31 U.S.C.S. § 3551 (LEXIS 2005).

¹⁰⁹ Bid Protest Regulations, Government Contracts, 4 C.F.R. § 21 (2005) [hereinafter GAO Bid Protest Regs].

¹¹⁰ *Id.* Prior to this revision, the GAO Bid Protest Regs defined an interested party as an "actual or prospective bidder or offeror whose direct economic interest would be affected by the award of a contract or by the failure to award a contract." *Id.*

¹¹¹ *Id.* Prior to this revision, the GAO Bid Protest Regs defined an intervenor as an "awardee if the award has been made or, if not award has been made, all bidders or offerors who appear to have a substantial prospect of receiving an award if the protest is denied." The revision now includes additional parties as intervenors. *Id.*

¹¹² *Id.*

On 21 April 2005, Mr. David Walker, Comptroller General of the United States, testified to Congress¹¹³ concerning the results of the President's Management Agenda (PMA).¹¹⁴ Mr. Walker summarized some of the key aspects of the federal government's competitive sourcing program.¹¹⁵ He testified that in response to a requirement in the National Defense Authorization Act for Fiscal Year 2001, he convened the Commercial Activities Panel (CAP) in 2001 to study the A-76 process.¹¹⁶ After reviewing the CAP's recommendations, the OMB substantially revised the competitive sourcing process in May 2003 making the competition for federal commercial activities similar to FAR procedures and more evenly-applied to both the private and public sector.¹¹⁷ Mr. Walker also explained that while the Revised A-76 did not grant federal employees standing to file a GAO protest, Congress amended the CICA in 2004 thus granting federal employees standing to file a GAO protest in large A-76 competitions.¹¹⁸ Subsequently, the GAO modified its protest regulations implementing the change in the federal statute.¹¹⁹ Finally, Mr. Walker concluded by stating that that GAO continues to review the success and integrity of Revised A-76.¹²⁰

OMB's Latest Word on A-76

In May 2005, the OMB released a report on the results of competitive sourcing conducted by federal agencies in FY 2004¹²¹ pursuant to the PMA.¹²² The report stated that during FY 2004, federal agencies conducted two hundred seventeen competitions involving 12,573 FTE employees saving over \$1 billion dollars.¹²³

The report also identified some competitive sourcing trends for FY 2004.¹²⁴ The report stated that for the second consecutive year, federal agencies determined that performance of commercial activities by in-house personnel was more cost effective than private sector performance ninety-one percent of the time.¹²⁵ The report stated that eighty percent of the FTEs involved in competitions fell into one of five categories: (1) information technology, (2) maintenance and property management, (3) logistics, (4) human resources, personnel management, education and training, or (5) finance and accounting.¹²⁶ The average length of standard competitions was nine months while the average length of streamlined competitions was three months.¹²⁷ In FY 2004, the clear majority of the competitions (seventy-nine percent) were standard

¹¹³ U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-05-574T, 21, ASSESSING THE PRESIDENT'S MANAGEMENT AGENDA: WHAT GAO FOUND (Apr. 21, 2005) (Testimony Before the Subcommittee on Federal Financial Management, Government Information, and International Security Senate Committee (statement of Mr. David M. Walker, Comptroller of the United States)) [hereinafter WALKER TESTIMONY].

¹¹⁴ See U.S. OFF. OF MGMT. AND BUDGET, EXECUTIVE OFF. OF THE PRESIDENT, THE PRESIDENT'S MANAGEMENT AGENDA: FISCAL YEAR 2002, at 17 (2001), available at <http://www.whitehouse.gov/omb/budget/fy2002/mgmt.pdf> [hereinafter THE PRESIDENT'S MANAGEMENT AGENDA] (explaining that competitive sourcing is one of the key methods by which President Bush seeks to improve government performance).

¹¹⁵ WALKER TESTIMONY, *supra* note 113, at 21.

¹¹⁶ *Id.* The Commercial Activities Panel (CAP) was convened in response to a requirement in the National Defense Authorization Act for Fiscal Year 2002, Pub. L. No. 106-398, § 832, 114 Stat. 1654, 1654A-221 (2001). The CAP studied the policies and procedures of studying the costs of private versus public performance of commercial activities pursuant to "Old" A-76. See Gov't Accountability Office, Commercial Activities Panel, Improving the Sourcing Decision of the Government (2002).

¹¹⁷ WALKER TESTIMONY, *supra* note 113, at 21.

¹¹⁸ *Id.*

¹¹⁹ *Id.*

¹²⁰ *Id.* at 21-22.

¹²¹ U.S. OFF. OF MGMT. & BUDGET, REPORT ON COMPETITIVE SOURCING RESULTS FISCAL YEAR 2004 (May 2005), available at <http://www.whitehouse.gov/omb> [hereinafter OMB REPORT].

¹²² THE PRESIDENT'S MANAGEMENT AGENDA, *supra* note 114.

¹²³ OMB REPORT, *supra* note 121, at 1.

¹²⁴ *Id.* at 2.

¹²⁵ *Id.* at 8.

¹²⁶ *Id.* at 14.

¹²⁷ *Id.* at 5.

competitions while in FY 2003, the majority of the competitions (sixty-three percent) were streamlined.¹²⁸ Finally, agencies pursued larger competitions in FY 2004 (average of fifty-eight FTEs) than in FY 2003 (average of twenty-seven FTEs).¹²⁹

Reports on Competitive Sourcing in DOD

The aforementioned OMB Report¹³⁰ relied upon data submitted by the DOD in an earlier report (DOD Report).¹³¹ Both the 2005 OMB Report and the earlier DOD Report provide data specifically on competitive sourcing in the DOD.

According to the OMB Report, in FY 2004, the DOD completed seventy competitions involving 8,234 FTEs.¹³² Of these competitions, fifty-four were standard competitions, four were streamlined, and twelve were direct conversions.¹³³ The average number of FTEs involved in the DOD standard competitions was one hundred thirty-six, while in DOD streamlined competitions, the average number was thirty.¹³⁴ The most frequently competed commercial activity in DOD was “base/facilities support and management.”¹³⁵ Resembling the trend in other federal agencies, the performance decisions following DOD competitions favored in-house employees ninety percent of the time.¹³⁶ By the date of the OMB Report, the DOD had announced seventeen additional streamlined competitions affecting 266 FTEs; the report listed no additional standard competitions.¹³⁷

According to the DOD Report, during FY 2004, the DOD employed 408,715 FTEs performing commercial activities and 172,140 FTEs performing inherently governmental functions.¹³⁸ Concerning the FTEs performing commercial activities, the DOD listed the FTEs by OMB “Reason Codes.”¹³⁹ Of these, this report¹⁴⁰ listed 125,781 FTEs under “Reason Code A”¹⁴¹ and 173,154 FTEs under “Reason Code B.”¹⁴²

The DOD report also categorized work performed by military members—vice FTEs—as either commercial or inherently governmental.¹⁴³ During 2004, 841,820 military members were performing commercial activities, while 1,182,040 military members were performing inherently governmental functions.¹⁴⁴

In summary, to a great extent, competitive sourcing trends in the DOD mirror the trends in other government agencies. For instance, in FY 2004, both the DOD and other federal agencies determined that in-house performance was less

¹²⁸ *Id.* at 11.

¹²⁹ *Id.* at 12.

¹³⁰ *Id.*

¹³¹ U.S. DEP’T OF DEF. 2004 INVENTORY REPORT OF INHERENTLY GOVERNMENTAL AND COMMERCIAL ACTIVITIES (Aug. 2004), available at <http://share76.fedworx.org/inst/share76> [hereinafter DOD REPORT].

¹³² OMB REPORT, *supra* note 121, at 33. This total includes all competitions completed in FY 2004 regardless of when initiated.

¹³³ *Id.*

¹³⁴ *Id.*

¹³⁵ *Id.* at 36.

¹³⁶ *Id.* at 38.

¹³⁷ *Id.* at 34.

¹³⁸ DOD REPORT, *supra* note 131, at 6.

¹³⁹ *Id.* at 7. Revised A-76 requires federal agencies to assign one of six “Reason Codes” to commercial activities performed by government employees. See REVISED A-76, *supra* note 1, attach. A, ¶ C.1.

¹⁴⁰ *Id.*

¹⁴¹ REVISED A-76, *supra* note 1, attach. A, ¶ C.1. Reason Code A states the “commercial activity is not appropriate for private sector performance pursuant to a written determination by the CSO” (competitive sourcing official). *Id.*

¹⁴² *Id.* Reason Code B states the “commercial activity is suitable for a streamlined or standard competition.” *Id.*

¹⁴³ DOD REPORT, *supra* note 131, at 6.

¹⁴⁴ *Id.*

expensive than private sector performance about ninety percent of the time.¹⁴⁵ Additionally, in both the DOD and other federal agencies, the vast majority of competitions in FY 2004 were standard competitions.¹⁴⁶

DOD Delegates Duties for Subordinate Competitive Sourcing Officials

In last year's *Year in Review*,¹⁴⁷ the Contract and Fiscal Law Department discussed the DOD memorandum delegating Competitive Sourcing Official (CSO)¹⁴⁸ duties from the DOD CSO to military Component Competitive Sourcing Officials (CCSO).¹⁴⁹ In that memorandum, the DOD CSO appointed Component CSOs in each of the armed services delegating certain duties to the Component CSOs while retaining certain duties at the CSO level.¹⁵⁰

Under that DOD memorandum, in early 2005, both the Air Force¹⁵¹ and the Army¹⁵² CCSOs delegated some competitive sourcing duties to Delegated Competitive Sourcing Officials (DCSO). The Air Force and the Army have now delegated to DCSOs the authority to appoint competition officials for standard competitions, to approve changes to the solicitation closing date to facilitate the submission of the agency tender, and to make determinations regarding deficiencies in an agency tender.¹⁵³ The Air Force's policy is that an agency tender official must be at least an O-5 or GS-13 equivalent and organizationally independent of the activity being competed.¹⁵⁴ The Army has published more detailed guidance regarding the roles and responsibilities of competition officials in Army Regulation 5-20.¹⁵⁵

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Privatization

Housing Privatization Injunction Lifted

Last year's *Year in Review*¹⁵⁶ discussed *Hunt Building Company v. United States, (Hunt I)* where the COFC permanently enjoined the Air Force from awarding a military family housing privatization contract to Actus Lend Lease, LLC (Actus).¹⁵⁷ The COFC issued the injunction because the Air Force "failed to comply with its solicitation, changed material terms . . . and failed to treat offerors fairly and equally."¹⁵⁸ The COFC lifted the injunction on 24 November 2004

¹⁴⁵ OMB REPORT, *supra* note 121, at 38.

¹⁴⁶ *Id.* at 11 and 33.

¹⁴⁷ *See 2004 Year in Review, supra* note 88, at 120.

¹⁴⁸ REVISED A-76, *supra* note 1, ¶ 4.f. A Competitive Sourcing Official (CSO) is an official at the assistant-secretary level with the responsibility of overseeing the competitive sourcing program throughout a particular federal agency. *Id.*

¹⁴⁹ *See* Memorandum, Deputy Secretary of Defense, to Secretaries of the Military Departments et al., subject: Designation of the Department of Defense Competitive Sourcing Official (12 Sept. 2003). In the DOD, the CSO is the Deputy Under Secretary of Defense (Installations and Environment). *Id.* This memo is available at <http://emissary.acq.ods.mil/inst/share.nsf> by clicking on the following links: "Library," Documents by Organization." Office of the Secretary of Defense," and "SECDEF Designation of DOD CSO."

¹⁵⁰ *Id.*

¹⁵¹ Memorandum, Deputy Chief of Staff for Personnel, to all major command commanders et al., subject: Delegation of Competitive Sourcing Official (CSO) Responsibilities (14 Jan. 2005) [hereinafter Air Force Delegation Memo]. The memo is available at <https://www.safaq.hq.af.mil/contracting/affars/5337/library-5337-a76.html> by clicking on the following link: "Policy."

¹⁵² Memorandum, Assistant Secretary of the Army (Installations and Environment), to Assistant Chief of Staff for Installation Management, subject: Delegation of Responsibilities of the Army Component Competitive Sourcing Official (CCSO) and Delegated Competitive Sourcing Official (DCSO) (7 Mar. 2005) [hereinafter Army Delegation Memo].

¹⁵³ *Id.*

¹⁵⁴ *Id.*

¹⁵⁵ U.S. DEP'T OF ARMY, REG. 5-20, COMPETITIVE SOURCING PROGRAM para. 1-4 (20 April 2005). This regulation governs the implementation of Revised A-76 in the Army.

¹⁵⁶ *2004 Year in Review, supra* note 88, at 124-26.

¹⁵⁷ 61 Fed. Cl. 243 (2004) [hereinafter Hunt I]. This solicitation envisioned award of a contract conveying 1356 military houses and leasing approximately 238 acres of land located beneath or near those houses at Hickam Air Force Base, Hawaii. *Id.* at 248.

¹⁵⁸ *Id.* at 247.

(*Hunt II*) after reviewing a motion filed by both Actus and Hunt Building Company, Ltd. (Hunt) jointly requesting that it be lifted.¹⁵⁹

In *Hunt I*, the COFC found that the Air Force's unequal treatment of the two offerors in the competitive range, Actus and Hunt, warranted this severe remedy. First, the solicitation required the successful offeror to sign form legal documents at closing that would be "substantially identical"¹⁶⁰ to the documents attached to the solicitation. Nevertheless, after the Air Force selected Actus as the successful offeror, the Air Force permitted Actus to make significant changes to these documents. Second, the Air Force changed a material term of the solicitation to Actus' benefit but not to Hunt's benefit.¹⁶¹ Third, although the solicitation stated that award and closing would be based upon the offeror's "final revised proposal,"¹⁶² which the Air Force used for evaluation purposes, the Air Force permitted Actus to revise this final proposal.¹⁶³ Consequently, the COFC found that the Air Force contravened a fundamental principle of contract law that "evaluation and contract award must be made in accordance with the terms and conditions in the Solicitation."¹⁶⁴

Prior to the COFC's opinion in *Hunt II*, Actus, the successful offeror, appealed the injunction to the Federal Circuit.¹⁶⁵ While this appeal was still pending, Actus and Hunt entered into a settlement agreement permitting them to resolve their differences.¹⁶⁶ On 24 September 2004, the parties requested relief from the *Hunt I* injunction arguing that under the circumstances, injunctive relief was no longer necessary.¹⁶⁷ Specifically, the parties argued that the injunction was no longer appropriate in light of the fact that Hunt had decided that it no longer wanted to participate in this privatization procurement.¹⁶⁸ The COFC waited until the Federal Circuit remanded the case to the COFC before ruling on the parties' Federal Rule of Civil Procedure (FRCP) 60(b) motion.¹⁶⁹

The COFC granted the parties' joint motion under FRCP 60(b).¹⁷⁰ While the court did not vacate the earlier injunction, it granted relief from the injunction prospectively due to its "strong policy favoring settlement."¹⁷¹ Consequently, the Air Force was free to award the privatization contract to Actus.¹⁷²

It is significant that the COFC did not waver in its position that the Air Force's unequal treatment of the offerors in *Hunt I* clearly warranted the injunction preventing award of the housing privatization contract. The COFC permitted the Air Force to proceed to award the contract to Actus only because the parties to the case jointly requested that the court lift the injunction. Absent this joint request, the permanent injunction would have remained in effect until the Air Force corrected the serious errors in this procurement.

¹⁵⁹ *Hunt Building Co., Ltd. v. United States*, 63 Fed. Cl. 141 (2004) [hereinafter *Hunt II*]. The COFC issued its opinion in *Hunt I* on 8 July, 2004. *Id.* at 142.

¹⁶⁰ *Id.*

¹⁶¹ *Id.* The Air Force changed a term in the solicitation regarding the wording of form legal documents that the successful offeror would be required to sign at closing. *Id.*

¹⁶² *Id.*

¹⁶³ *Id.*

¹⁶⁴ *Id.* (citing *Lykes Bros. Steamship Co., Comp. Gen. B-236834.4*, July 23, 1990, 90-2 CPD 62).

¹⁶⁵ *Id.* at 142. Actus filed its appeal on 3 September 2004.

¹⁶⁶ *Id.* The 23 September 2004 settlement agreement stated that the parties would "resolve their pending appeal" at the Federal Circuit Court if the COFC lifted the injunction preventing award of the contract to Hunt. *Id.*

¹⁶⁷ *Id.* The parties jointly filed a motion with the COFC under FRCP 60(b), Relief from Judgment or Order, requesting that the COFC lift the injunction based on the new fact that Hunt had decided that it no longer wanted to participate in this procurement. *Id.*

¹⁶⁸ *Id.*

¹⁶⁹ *Id.*

¹⁷⁰ *Id.* at 142-43.

¹⁷¹ *Id.*

¹⁷² *Id.* at 143.

In *American Water Services*,¹⁷³ the GAO denied a protest involving a DOD utilities privatization contract concerning waste water and storm water systems at Fort Knox, Kentucky. The Defense Energy Support Center (DESC)¹⁷⁴ awarded the utilities privatization contract to Hardin County Water District #1 (Hardin).¹⁷⁵ The protester, American Water Services (AWS), argued that the agency improperly applied the solicitation's evaluation criteria and that Hardin was ineligible for award.¹⁷⁶ In denying the protest, the GAO found that the agency reasonably evaluated the offers submitted and that Hardin was, in fact, eligible for award.¹⁷⁷

The DESC issued the utilities privatization solicitation on 9 April 2001.¹⁷⁸ The solicitation stated that the utilities privatization contract would be awarded to the offeror whose proposal was the best value to the government considering five evaluation factors: (1) technical capability, (2) past performance, (3) risk, (4) socioeconomic plan, and (5) price. Some of these evaluation factors also included subfactors.¹⁷⁹ For the purpose of the protest, the subfactors included within the "risk" evaluation factor—performance, assurance of long-term price and service stability, and price realism—are relevant.¹⁸⁰ The solicitation also envisioned the receipt of offers by both regulated and unregulated entities.¹⁸¹ In this regard, the solicitation stated that the agency would evaluate proposals "on the degree to which . . . *long-term price and service stability* are enhanced as a result of regulation by an independent federal, state, or local regulatory authority with jurisdiction over the applicable utility service."¹⁸² In response to the solicitation, AWS and Hardin submitted offers.¹⁸³

The agency determined that the offers submitted by AWS and Hardin were technically acceptable; however, Hardin's offer presented less risk and Hardin's price was significantly lower.¹⁸⁴ Although the agency gave both AWS and Hardin an overall rating of "low" on the "risk" evaluation factor, AWS received a "moderate" rating in the assurance of long-term price and service stability (risk) subfactor, while Hardin received a "low" rating.¹⁸⁵ Both AWS and Hardin received ratings of "low" in the price realism subfactor of the risk factor.¹⁸⁶ Because the source selection authority found Hardin's offer presented the best overall value to the government based on the evaluation criteria, the agency decided to award the contract to Hardin.¹⁸⁷ After DESC notified AWS of the source selection decision, AWS filed its protest at the GAO.¹⁸⁸

¹⁷³ B-295376, 2005 U.S. Comp. Gen. LEXIS 57 (Feb. 8, 2005).

¹⁷⁴ *Id.* at *3. The Defense Energy Support Center (DESC) is a DOD agency which awards utilities privatization contracts to private entities on behalf of the Army and Air Force. *Id.*

¹⁷⁵ *Amer. Water Servs.*, 2005 U.S. Comp. Gen. LEXIS 57, at *2-3. DESC awarded the contract pursuant to 10 U.S.C. § 2688 which grants the military services the authority to convey utilities infrastructure to private or public sector offerors so long as such a conveyance is in the "interests of the United States." This authority states that in consideration for conveying all or part of a utilities infrastructure, the service secretary may require payment of a lump sum payment or a reduction in charges for utility services. Where the contract allows for utility services, this contract may not exceed fifty years. *See* 10 U.S.C.S. § 2688 (LEXIS 2005).

¹⁷⁶ *Amer. Water Servs.*, 2005 U.S. Comp. Gen. LEXIS 57, at *2-3.

¹⁷⁷ *Id.* at *34-35.

¹⁷⁸ *Id.* at *3. The solicitation envisioned that the agency would convey the utilities infrastructure to the awardee and that the awardee would provide utilities services to the agency for a fifty-year period. *Id.*

¹⁷⁹ *Id.* at *4.

¹⁸⁰ *Id.* Further, the solicitation stated that the first three evaluation factors listed above were equally important, the socioeconomic evaluation factor was the least important, and that these four factors, when combined, were significantly more important than price. *Id.* at *4-5.

¹⁸¹ *Id.* at *5.

¹⁸² *Id.* (emphasis added).

¹⁸³ *Id.* at *8. AWS was a non-regulated private sector offeror while Hardin was a regulated public sector offeror. *Id.* at *16. Hardin was a "political subdivision of Hardin County, charged with providing water service to the northern part of the county surrounding Fort Knox" and was regulated by the Kentucky Public Service Commission. *Id.* at *8.

¹⁸⁴ *Id.* at *18.

¹⁸⁵ *Id.* at *14.

¹⁸⁶ *Id.*

¹⁸⁷ *Id.* at *18.

¹⁸⁸ *Id.*

American Water Services protested the award to Hardin on three grounds.¹⁸⁹ First, AWS stated that the agency improperly evaluated the offers with regard to the long-term price and service stability subfactor.¹⁹⁰ Second, AWS stated that the agency failed to properly analyze Hardin's prices pursuant to the price realism subfactor.¹⁹¹ Third, AWS stated that Hardin was ineligible for award because the agency awarded the contract on the condition that the State public service commission (PSC) approves Hardin's proposed prices.¹⁹²

Regarding the evaluation of the assurance of long-term price and service stability subfactor, the GAO found that the agency had a rational basis for assigning Hardin a "low" rating and for assigning AWS a "moderate" rating.¹⁹³ The agency determined that Hardin's proposal warranted a "low" rating in this subfactor because Hardin, as an entity regulated by the State PSC, would not be able to increase prices if that commission found the increase to be unreasonable.¹⁹⁴ As mentioned above, the solicitation specifically stated that the agency could consider the effect, if any, that federal or state regulation of the offeror would have on this subfactor.¹⁹⁵ Consequently, the GAO found that the agency reasonably applied this evaluation subfactor.¹⁹⁶ Regarding the agency's analysis of Hardin's prices pursuant to the price realism subfactor, AWS argued that the agency failed to reasonably evaluate Hardin's offer by not considering its transition costs and that some of its costs were "suspiciously low."¹⁹⁷ The GAO considered the fact that the agency's cost realism analysis was based on thorough discussions regarding pricing with Hardin.¹⁹⁸ The GAO also determined that AWS misstated some of Hardin's prices.¹⁹⁹ Subsequently, GAO found no basis for AWS's argument and concluded that the agency's price realism analysis was reasonable.²⁰⁰

Regarding the issue of whether Hardin's proposal was qualified and was therefore, unacceptable, the GAO responded in the negative.²⁰¹ The GAO opined that Hardin's offer was unqualified and that the requirement for post-award approval of prices by the PSC was a contract administration issue and not an evaluation issue.²⁰² To conclude that Hardin's proposal was unacceptable because the PSC had to approve its prices would prevent regulated offerors from participating in the procurement.²⁰³ After a thorough analysis of AWS's allegations, GAO found that none of the protest grounds were meritorious.²⁰⁴ Accordingly, GAO denied the protest.²⁰⁵

The decision is significant in that it illustrates what the GAO considers an adequate evaluation of proposals submitted by both regulated and non-regulated entities in a utilities privatization protest. Despite the protester's allegations that the agency improperly evaluated Hardin, the regulated offeror, the GAO found that agency's evaluation and award was proper. Further, the case represents one of a handful of GAO protest decisions concerning utilities privatization.

¹⁸⁹ *Id.* at *19.

¹⁹⁰ *Id.*

¹⁹¹ *Id.*

¹⁹² *Id.* Hardin was regulated by the Kentucky Public Service Commission (PSC). The Hardin stated in its proposal that the PSC would regulate the cost of utility service at Ft. Knox if the agency awarded the contract to Hardin. *Id.* at *8. During discussions, Hardin stated that the prices contained in its proposal were still subject to approval by the PSC and as such, were not final. *Id.* at *9-10.

¹⁹³ *Id.* at *20-21. This subfactor is listed under the overall risk evaluation factor and so, Hardin's "low" rating on this subfactor is a better rating than AWS' "moderate" rating. *Id.*

¹⁹⁴ *Id.*

¹⁹⁵ *Id.* at *5.

¹⁹⁶ *Id.* at *20.

¹⁹⁷ *Id.* at *26.

¹⁹⁸ *Id.* at *27.

¹⁹⁹ *Id.* at *30.

²⁰⁰ *Id.* at *33.

²⁰¹ *Id.* at *34-35.

²⁰² *Id.*

²⁰³ *Id.*

²⁰⁴ *Id.* at *35.

²⁰⁵ *Id.*

GAO's First Big Utilities Privatization Report

On 12 May 2005, the GAO issued its “first detailed report on DOD’s utility privatization program.”²⁰⁶ The GAO studied DOD’s utility privatization program’s²⁰⁷ overall status and whether the DOD’s cost savings estimates for utilities privatization projects were accurate.²⁰⁸ After assessing the program, the GAO made findings and recommendations to the Secretary of Defense.²⁰⁹

The GAO found that DOD’s progress in implementing the utility privatization program has been much slower than anticipated.²¹⁰ In 1997, the DOD expected to develop a plan to privatize all eligible utilities by January of 2000; however, as of the date of the report, the DOD had privatized only ninety-four utility systems out of 1,499 utility systems eligible for privatization.²¹¹ In 1997, the DOD issued Defense Reform Initiative (DRI) Directive, Number 9, requiring the DOD to “develop a plan for privatizing” all DOD’s utilities systems by 1 January 2000.²¹² In December of 1998, the DOD revised its privatization goal stating that by 30 September 2003, the DOD should privatize all non-exempt utilities.²¹³ In October 2002, the DOD again revised its goal stating that the DOD must make a privatization evaluation decision on all utility systems at every active duty, reserve, and National Guard installation by 30 September 2005.²¹⁴ The GAO Report stated that it was unlikely that any of the Armed Services would meet the latest goal.²¹⁵ In November 2005, the DOD again revised its goal.²¹⁶

The Government Accountability Office also found that while utilities privatization often results in an overall improvement of the utilities services, it may not result in overall cost savings.²¹⁷ The GAO found that privatization may even result in increased costs for utilities because if the contractor enhances utilities services, then the DOD will likely reimburse the contractor for these enhanced services via increased contract costs.²¹⁸

The GAO stated that unnamed Air Force officials reported that its costs could increase as much as \$200 million per year “for the first five to ten years of privatization” for systems already privatized.²¹⁹ The GAO further opined that DOD is

²⁰⁶ U.S. GOV’T ACCOUNTABILITY OFF., GAO-05-433, MANAGEMENT ISSUES REQUIRING ATTENTION IN UTILITY PRIVATIZATION 10 (May 12, 2005) (Report to Subcommittee on Readiness, Committee on Armed Servs., House of Representatives) [hereinafter GAO PRIVATIZATION REPORT]. The GAO has issued four other reports mentioning the utility privatization program. *Id.*

²⁰⁷ *Id.* at 8. In 1997, DOD decided that privatization of utilities was the most cost-effective means of improving utilities services for military installations. This program envisions two transactions—the conveyance of the utility system infrastructure and also the acquisition of utility services for a period up to fifty years. The transaction ordinarily does not include the conveyance of real property on which the utility system is located. *Id.*

²⁰⁸ *Id.* at 2.

²⁰⁹ *Id.* at 36. See also National Defense Authorization Act for FY 1998, Pub. L. No. 105-85, § 2812, 111 Stat. 1629 (1997). In 1997, Congress passed permanent legislation authorizing the privatization of utilities at military installations. This legislation permits the secretary of a military department to convey a utility system to a private or public entity if doing so would be in the best interests of the United States. Consideration for the conveyance may be a lump sum payment or a reduction in the cost of utilities. *Id.*

²¹⁰ *Id.* at 11.

²¹¹ GAO PRIVATIZATION REPORT, *supra* note 206, at 3.

²¹² U.S. DEP’T OF DEF., OFF. OF THE DEPUTY SECRETARY OF DEF., DEFENSE REFORM INITIATIVE DIRECTIVE No. 9 (Dec. 1997) [hereinafter DEFENSE REFORM INITIATIVE DIRECTIVE No. 9].

²¹³ U.S. DEP’T OF DEF., OFF. OF THE DEPUTY SECRETARY OF DEF., DEFENSE REFORM INITIATIVE, DIR. No. 49 (Dec. 1998) [hereinafter DEFENSE REFORM INITIATIVE DIR. No. 49].

²¹⁴ GAO PRIVATIZATION REPORT, *supra* note 206, at 11.

²¹⁵ *Id.* at 3. DOD stated that its implementation of the program had been slower than anticipated because of unforeseen complexities in assessing the fair market value of utilities systems and private sector reluctance to submit offers on privatization contracts. *Id.* at 14.

²¹⁶ See Memorandum, Undersecretary of Defense for Acquisition, Technology, and Logistics to Secretaries of the Military Departments et al., subject: Supplemental Guidance for the Utilities Privatization Program (2 Nov. 2005) [hereinafter DOD Privatization Memo]. This memo directs the Armed Services to continue the completion of these privatization evaluation or exemption decisions. The memorandum also directs that the services send a report to that office by 14 February 2006 listing the number of systems privatized as of 31 December 2005. The memo is available at <http://www.acq.osd.mil/ie/irm/utilities/utilities.htm>.

²¹⁷ *Id.* at 17.

²¹⁸ *Id.*

²¹⁹ *Id.* at 18.

sometimes unprepared for the actual cost of utilities privatization because the “services’ economic analyses do not depict actual expected costs of continued government ownership.”²²⁰

After analyzing the DOD’s utilities privatization program, the GAO made some specific recommendations to the Secretary of Defense.²²¹ First, the GAO recommended that the DOD modify its guidance for conducting economic analyses of utilities privatization projects so that these analyses reflect the actual expected cost of privatization.²²² Second, the DOD should obtain an independent review of its economic analyses supporting each proposed privatization project to verify the accuracy of its analyses.²²³ Third, the GAO recommended that the DOD draft guidance requiring the services to methodically plan for cost increases for privatized utilities.²²⁴ Fourth, the GAO suggested that the DOD issue guidance requiring more oversight of privatized utilities contracts.²²⁵ Finally, the GAO recommended that the DOD re-evaluate whether conveyance of utilities systems should continue to be DOD’s approach in this program.²²⁶

Practitioners should be aware of GAO’s utility privatization report not only because it is the first of its kind, but also because it provides a lengthy summary and analysis of this long-standing program. While implementation goals of this program have changed over the years, the overarching objective of evaluating the feasibility of privatizing every DOD-owned utility system remains unchanged.²²⁷

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Construction Contracting

Federal Circuit Overturns McMullan Presumption

In *England v. Sherman R. Smoot Corporation*,²²⁸ the Court of Appeals for the Federal Circuit (CAFC) vacated and remanded a decision of the ASBCA. In the process, the court overturned a twenty-nine year old judicially created presumption that the government was at fault for any delay coupled with an extension of the period of performance.²²⁹ The presumption had been in existence since the ASBCA’s decision in *Robert McMullan & Son, Inc.*²³⁰ The CAFC held that the *McMullan* presumption was in conflict with the CDA.²³¹

In *Smoot Corp.*, the contractor had entered a fixed-price construction contract with the Navy for renovation work at the Washington Navy Yard.²³² As a result of various design and construction changes, the contractor notified the Navy contracting officer that there would be a completion delay of fifty-one days.²³³ The contractor submitted a claim for extended overhead costs attributable to the delay and requested a completion extension.²³⁴ After receiving notice from the contractor, the Navy Project Engineer wrote a letter to the contractor officer stating that “the construction schedule recently submitted is approved. . . . This time is fully compensable, and upon approval for related costs associated with this time, a modification

²²⁰ *Id.* at 19.

²²¹ *Id.* at 36. The DOD submitted comments to the GAO’s report disagreeing with its findings and recommendations. The DOD stated that GAO’s findings were flawed in that they were based out-of-date information and based on a limited understanding of DOD’s utility privatization program. *Id.*

²²² *Id.*

²²³ *Id.*

²²⁴ *Id.*

²²⁵ *Id.* at 56.

²²⁶ *Id.*

²²⁷ DOD Privatization Memo, *supra* note 216.

²²⁸ 388 F.3d. 844 (Fed. Cir. 2004).

²²⁹ *Id.*

²³⁰ The presumption takes its name from the case of *Robert McMullen & Son, Inc.*, ASBCA No. 19023, 76-IBCA ¶ 11,728, at 55,903. This case predates the Contracts Disputes Act.

²³¹ *Smoot Corp.*, 388 F.3d. at 845.

²³² *Id.* at 846.

²³³ *Id.*

²³⁴ *Id.*

will be issued. This has been discussed and approved by the [contracting officer].”²³⁵ Five months later, the contracting officer informed the contractor that although the full period of delay will be accounted for in an extension of performance, only twenty-one days of the delay were compensable as being the fault of the government.²³⁶

The contractor submitted a claim for the full period of delay. After the contracting officer failed to issue a final decision on the claim, Smoot Corp. appealed the deemed denial to the ASBCA.²³⁷ The ASBCA held for the contractor by invoking the so-called “McMullan presumption.” This rebuttable presumption holds the government liable for a contractor’s costs associated with a delay if, knowing all the material facts pertinent to the delay, the government extends contract performance to account for the delay.²³⁸ The Navy appealed to the CAFC.

On appeal, the CAFC held that “the McMullan presumption is at odds with the CDA.”²³⁹ The court determined that “Congress made clear in the CDA that any findings of fact by a contracting officer in a final decision are not binding in any subsequent proceeding.”²⁴⁰ By applying the presumption to a contracting officer’s decision to extend the performance period, the *McMullan* presumption gives the determination weight the CDA prohibits.²⁴¹ The court further found that “the McMullan presumption is logically inconsistent” because there are three potential causes of delay: contractor, government, or external forces.²⁴² The court found that the McMullan presumption ignores the possibility of events external to the government causing the delay and that applying the presumption in such a situation is unwarranted and “nothing in the [FAR] supports such a presumption.”²⁴³

Concurrent Delay Caused by Contractor and Government Prevents Recovery of Unabsorbed Overhead

In *Singleton Contracting Corporation*,²⁴⁴ the CAFC affirmed an ASBCA decision denying a contractor’s claim for unabsorbed overhead due to the fact that the cause of delay in contract performance was concurrently caused by the government and the contractor.²⁴⁵ In this case, the contractor appealed the ASBCA’s determination that it was not entitled to unabsorbed overhead following a termination for convenience about a year after a construction contract was entered, but prior to any work commencing.²⁴⁶ During a preconstruction conference after award, it became apparent that the government’s construction drawings were flawed and work could not commence until new drawings were prepared.²⁴⁷ Ultimately, the government never provided corrected drawings prior to terminating the contract for convenience several months later.²⁴⁸ Such a government-caused delay typically permits the contractor to recover costs associated with such a delay. However, Singleton was required to provide proof of insurance at the preconstruction meeting since the contract required Singleton to maintain certain insurance policies “during the entire period of performance of the contract.”²⁴⁹ Fortunately for the government, Singleton never obtained such insurance.²⁵⁰

²³⁵ *Id.*

²³⁶ *Id.*

²³⁷ *Id.* at 847

²³⁸ Sherman R. Smoot Corp., ASBCA No. 53115, 03 -1 BCA ¶ 32,198.

²³⁹ *Smoot Corp.*, 388 F.3d. at 856.

²⁴⁰ *Id.*

²⁴¹ *Id.* In this case, the decisions of the contracting officer were actually only interim decisions. *Id.* However, the court deemed the interim decisions in this case indistinguishable from a final decision of a contracting officer because the interim decision, coupled with the deemed denial of the claim, satisfied the required elements of a final decision. *Id.*

²⁴² *Id.* at 857.

²⁴³ The importance of this point, obviously, is that while both government caused delays and delays caused by many factors outside the government’s control may be “excusable delays” pursuant to FAR 52.249-10 (Default - Fixed Price Construction), generally only those delays caused by the government will be *compensable* excusable delays.

²⁴⁴ *Singleton Contracting Corp. v. Harvey*, 395 F.3d. 1353 (Fed. Cir. 2005).

²⁴⁵ *Id.*

²⁴⁶ *Id.* at 1354.

²⁴⁷ *Id.*

²⁴⁸ *Id.* at 1355.

²⁴⁹ *Id.*

²⁵⁰ *Id.*

The court, finding that the contractor's failure to provide proof of insurance was a concurrent cause of delay along with the government's failure to provide correct drawings, affirmed that the contractor was barred from recovering unabsorbed overhead under either the *Eichleay*²⁵¹ formula or the methodology set out in *Nicon, Inc.* for delays caused prior to contract performance.²⁵² As is so often the case, *Singleton Contracting Corp.* appears to be a case where the government simply got lucky on the facts.

Architect-Engineer Firm Entitled to Recovery under Quantum Meruit Basis

In a case of first impression, the COFC held that an Architect—Engineer firm (Fluor Enter., Inc., hereinafter Fluor) was entitled to recover in *quantum meruit*²⁵³ despite its illegal contract with the National Oceanographic and Atmospheric Administration (NOAA).²⁵⁴ The source of the illegality in the contract was a violation of the fee limitations for architect-engineer (A&E) services prescribed at 41 U.S.C. § 254(b) which provides, in pertinent part:

. . . in the case of a cost-plus-fixed-fee contract . . . a fee inclusive of the contractor's costs and not in excess of 6% of the estimated cost, exclusive of fees, as determined by the agency head at the time of entering into the contract, of the project to which such fee is applicable is authorized in contracts for architectural or engineering services relating to any public works or utility project. . . .²⁵⁵

Because of a variety of factors, the NOAA was unable to estimate project costs for the A&E services at the time the contract was entered.²⁵⁶ Because of the complexity of the requirement, the parties employed “a form of the cost-plus-fixed-fee contract--called a “level of effort” or “term” contract--that obligated Fluor to provide only a predetermined number of man-hours towards the project rather than completing the project itself.”²⁵⁷ Despite the flaws in the contract, and the lack of the required prospective estimate of project costs, both parties performed.²⁵⁸ Nearly three years after completion of performance (and nearly ten years after the onset of the contract), the contracting officer sought to retroactively impose the statutory six percent fee limitation on required for A&E contracts and, thereby, recover overpayments based on a “substitute estimate.”²⁵⁹

The case presented the court with a “quandary” because the project was already completed and the government had received the benefits of its contract whose illegality should make it void *ab initio* since the contracting officers have no authority to enter into illegal contracts.²⁶⁰ The court stated that “[w]ithout the mandatory project estimate, the contracting officer lacked the authority to procure A&E services under § 254(b) and [f]ailure to follow the applicable rules negates the agent's authority to enter into a contract binding on the government. To permit otherwise would be to nullify those very statutes, regulations, and determinations--a result clearly contrary to the public interest.”²⁶¹

²⁵¹ *Eichleay Corp.*, ASBCA No. 5183, 60-2 BCA ¶ 2,688 (1960), *aff'd on recon.*, 61-1 BCA ¶ 2,8994 (1961)

²⁵² *Nicon v. U.S.*, 331 F.3d. 878, 885 (Fed. Cir. 2003) (holding that while the *Eichleay* formula is the exclusive method for calculating unabsorbed overhead in cases where contract performance has begun, “there is no bar to the award of home office overhead in a termination for convenience settlement provided a reasonable method of allocation is available on the particular facts of the case”).

²⁵³ At common law, *quantum meruit* refers to the quasi-contractual recovery for the value of services rendered. *Fluor Enter., Inc. v. United States*, 64 Fed.Cl. 461, 495 n. 31 (2005).

²⁵⁴ *Id.*

²⁵⁵ 41 U.S.C.S. § 254(b) (Lexis 2005) (emphasis added). One unique aspect of the architect-engineer industry that is codified in this provision is that price competition between competing contractors is ethically inappropriate. *Fluor Enter., Inc.*, 64 Fed.Cl. at 463. The six percent fee limitation, including the contractor's costs and their fee, in A&E cost-plus fixed fee contracts “helps ensure the integrity of the contractor's A&E costs because the maximum amount of reimbursable costs, *plus the fixed fee*, is fixed prior to contract performance. *Id.*

²⁵⁶ *Id.* at 463. Chief among the factors the court cited was the fact that the scope of NOAA's project was uncertain and Fluor was hired to perform an array of services, among which included tailoring the scope of NOAA's project and, therefore, Fluor's own undertaking. *Id.*

²⁵⁷ *Id.*

²⁵⁸ *Id.*

²⁵⁹ *Id.*

²⁶⁰ *Id.* at 491. “The real problem that is implicated by these facts is a rule of constitutional law that a government agency can not validly contract to pay funds in contravention of a federal statute because any ‘payment of funds from the Treasury must be authorized by a statute.’” (citing *Off. of Pers. Mgmt. v. Richmond*, 496 U.S. 414, 424, 110 L. Ed. 2d 387, 110 S. Ct. 2465 (1990) (citing U.S. CONST. art. I, § 9 cl.7)).

²⁶¹ *Id.* at 492 (citing *United States v. Amdahl Corp.*, 786 F.2d 387, 392 (Fed. Cir. 1986)).

Despite the illegality of the contract, the court determined that the appropriate remedy would be to allow the contractor to recover in this case on a theory of implied contract.²⁶² The court stated that “when a contract or a provision thereof is in violation of law but has been fully performed, the courts have variously sustained the contract, reformed it to correct the illegal term, or allowed recovery under an implied contract theory; the courts have not, however, simply declared the contract void *ab initio*.”²⁶³ In those circumstances where *quantum meruit* is appropriate, the court concluded that finding only certain contract provisions unenforceable does not have the same harshness as allowing a single party to bear the entire risk and penalty of unenforceability.²⁶⁴

The court ultimately held that the contractor was entitled to recover the “reasonable value” of the services rendered to the government, not exceeding the six percent statutory cap based on the estimate of the project.²⁶⁵ The court recognized that it was a bit of a circular argument since it is nearly impossible to go back in time to create an estimate for a now-completed project that could not have been accurately estimated at the time the contract was entered into.²⁶⁶ However, the court determined that since the government was trying to recover what they contended was an overpayment, the government has the burden of overcoming this deficiency.²⁶⁷ The court determined that further proceedings would be necessary to resolve the *quantum* of Fluor’s entitlement and, “given the convoluted nature of the facts in this case, and the guidance provided in the opinion,” the court strongly encouraged the parties to seek a settlement on the issue of *quantum*.²⁶⁸

Architect-Engineer Small Business Set-Aside Threshold Increased

Effective 22 November 2004, the Defense Federal Acquisition Regulation Supplement (DFARS) was amended by final rule to increase the small business set-aside threshold for acquiring A&E services for military construction or family housing projects.²⁶⁹ The threshold was increased from \$85,000 to the new threshold of \$300,000.

Major Michael S. Devine

Bonds, Sureties, and Insurance

Facially Valid Bid Bond Can’t be Basis for Nonresponsive Bid Determination

In *Aeroplite Corporation v. United States*,²⁷⁰ the COFC held that despite clear extrinsic evidence, a contracting officer may not look beyond a facially valid bid bond to determine whether it conforms to the invitation for bids.²⁷¹

In this case, the contractor submitted a bid bond for the \$7.3 million amount of their bid, but the bid bond did not have a corporate seal which led the contracting officer to investigate it.²⁷² Upon investigation, the surety on the bid bond informed the contracting officer that they would only issue performance and payment bonds up to \$5.5 million, and the \$7.3

²⁶² *Id.* at 495.

²⁶³ *Id.* (citing AT&T Co., 177 F.3d 1376, 1378 (CAFC 1999)).

²⁶⁴ *Fluor Enter., Inc.*, 64 Fed.Cl. at 495.

²⁶⁵ *Id.* at 496.

²⁶⁶ *Id.*

²⁶⁷ *Id.* at 496-97.

²⁶⁸ *Id.* at 497.

²⁶⁹ Defense Federal Acquisition Regulation Supplement; Contracting for Architect-Engineering Servs., 69 Fed. Reg. 67,855 (Nov. 22, 2004) (to be codified at 48 C.F.R. pt. 219). This final rule implements Section 1427 of the National Defense Authorization Act for Fiscal Year 2004, Pub. L. No. 108-136, 117 Stat. 1522 (2004).

²⁷⁰ 67 Fed. Cl. 4 (2005).

²⁷¹ A “bid bond” is a bond that serves as a bid guarantee. Such bonds are frequently used in public construction contracts to ensure the bidder will not withdraw their bid and will execute a written contract and submit any required performance and payment bonds specified in the IFB if they are awarded the contract. U.S. GEN. SVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. pt. 28.001 (July 2005) [hereinafter FAR].

²⁷² 67 Fed. Cl. at 8. One of the bases that the government initially found the bid to be non-responsive was the lack of corporate seal on the bid bond. The government later recognized this determination was in error, but the lack of certification is still relevant because it led to the investigation of the bid bond which led to the primary reason that the contracting officer held the bid nonresponsive, *i.e.*, it did not provide full bid coverage. *Id.*

million bid bond was, therefore, invalid.²⁷³ Based on this information, the contracting officer determined that Aeroplate's bid was nonresponsive and Aeroplate protested.

Aeroplate argued that the relevant FAR provision²⁷⁴ mandates that as long as a bid guarantee (bid bond) is proper on its face, the bidder has satisfied its requirements for the bid.²⁷⁵ Aeroplate argued that the FAR provides remedies in the form of termination for default if the winning offeror later fails to provide performance or payment bonds as required.²⁷⁶ The government pressed the argument that, as a matter of regulation and policy, the "procuring officer is not restricted to the 'superficial, truncated review [of the bid bond] urged by plaintiff.'²⁷⁷ The government contended that the express purpose of the bid guarantee is to "provide assurances that the bidder 'will execute a written contract and furnish required bonds, . . . within the time specified in the bid.'²⁷⁸

The COFC believed that the government's position "would carve out an exception" to the rule that the validity of a bid bond must be determined at the time of bid opening.²⁷⁹ The court was not willing to carve such an exception based on the facts of this case. Citing *Hawaiian Dredging Construction Co. v. United States*,²⁸⁰ the COFC held that "the overarching issue is whether the contracting officer reasonably concluded that he could not establish unequivocally at the time of bid opening that the plaintiff's bid bonds were enforceable against the surety."²⁸¹ Despite the fact the court recognized that this firm rule could result in a waste of time and resources to award a contract knowing it would be terminated for default when required bonds are not submitted, the court held that such an exception would "deprive the established law of suretyship of the certainty that has been its hallmark"²⁸²

The court found that the agency's nonresponsiveness determination was arbitrary, capricious, or otherwise contrary to law, and granted Aeroplate's protest on this ground. The case was referred to the Small Business Administration (SBA) for a responsibility determination since the contracting officer had also incorrectly determined that Aeroplate was nonresponsive without first referring the matter to the SBA.²⁸³

²⁷³ *Id.* at 9.

²⁷⁴ FAR 52.228-1 provides that:

- (a) Failure to furnish a bid guarantee in the proper form and amount, by the time set for opening of bids, may be cause for rejection of the bid.
- (b) The bidder shall furnish a bid guarantee in the form of a firm commitment, e.g., bid bond supported by good and sufficient surety or sureties acceptable to the Government, postal money order, certified check,
- (c) The amount of the bid guarantee shall be __ percent of the bid price or \$ __ , whichever is less.
- (d) If the successful bidder, upon acceptance of its bid by the Government within the bid period, fails to execute all contractual documents or furnish executed bonds within 10 days after receipt of the forms by the bidder, the Contracting Officer may terminate the contract for default.
- (e) In the event that the contract is terminated for default, the bidder is liable for any cost of acquiring the work that exceeds the amount of its bid, and the bid guarantee is available to offset the difference.

FAR, *supra* note 271, pt. 52.228-1.

²⁷⁵ *Aeroplate*, 67 Fed. Cl. at 11.

²⁷⁶ *Id.*

²⁷⁷ *Id.*

²⁷⁸ *Id.*

²⁷⁹ *Id.*

²⁸⁰ 59 Fed. Cl. 305 (2004).

²⁸¹ *Aeroplate*, 67 Fed. Cl. at 11.

²⁸² *Id.* at 12.

²⁸³ *Id.* at 14.

In 2002, the CAFC upheld the ASBCA's determination that the Tucker Act does not confer jurisdiction to the boards of contract appeal to entertain surety claims that arose prior to a takeover agreement between the government and the surety.²⁸⁴ This past year, the CAFC had the opportunity to again address this issue in *United Pacific Insurance Company v. Roche*.²⁸⁵

In *United Pacific*, the CAFC again sustained the ASBCA's determination that they did not have jurisdiction to hear a surety's appeal of a contracting officer's denial of claims which arose prior to the surety and the government entering a takeover agreement.²⁸⁶ The CAFC again held that the ASBCA was correct in determining that sureties in such a position did not constitute "contractors" under the Contracts Disputes Act at the time the claim arose.²⁸⁷ Given the developments over the last couple of years, it is likely that sureties will get the message and file such claims in the future with the Court of Federal Claims, and not the ASBCA.

Interestingly, however, the Labor Board of Contract Appeals (LBCA) decided a case this year in which it distinguished the decisions discussed above which limited the rights of sureties to file claims for actions arising before a takeover agreement is in effect. In *Maharaj Construction, Inc.*,²⁸⁸ the LBCA allowed a surety to dismiss a defaulted contractor's appeal of their termination for default, despite the fact that the grounds for the appeal arose prior to the takeover agreement between the surety and the government. The LBCA held that the surety had standing to dismiss the contractor's appeal because in this case, unlike those discussed above, there was a General Indemnification Agreement (GIA) between the contractor and the surety which provided for an assignment of claims to the surety in the event of default, and the GIA was later incorporated into the takeover agreement between the surety and the government.²⁸⁹

Major Michael S. Devine

Cost & Cost Accounting Standards

Some Fear the Treasury Doors Have Been Opened Too Wide but the Lump-Sum Reimbursement Is Allowed for an Expanded List of Relocation Costs

Three years ago, the FAR Councils issued a final rule increasing the limit from \$1,000 to \$5,000 for lump-sum reimbursement of miscellaneous relocation costs.²⁹⁰ As we reported two years ago, the FAR Councils were next considering the appropriateness of allowing an appropriate lump-sum reimbursement for an expanded list of relocation costs under FAR 31.205-35 instead of an actual cost basis.²⁹¹ After further consideration of the issue through review of public comments and a public meeting on 6 February 2003, the FAR Councils issued a final rule through Federal Acquisition Circular (FAC) 2005-06 that also allowed a lump-sum reimbursement for house hunting, travel costs to the new location, and temporary lodging expenses. However, the lump-sum reimbursement for the expanded relocation costs is still limited to \$5,000.²⁹²

²⁸⁴ *Fireman's Fund Ins. Co. v. England*, 313 F.3d 1344 (Fed. Cir. 2002). See also discussion of this case in *2004 Year in Review*, *supra* note 88, at 131.

²⁸⁵ 401 F.3d 1362 (Fed. Cir. 2005). A note of clarification for those who have been tracking this issue, this is the same case name, the same surety, and the same contractor that were subject of a CAFC decision in August 2004 (380 F.3d 1352 (Fed. Cir. 2004)) and discussed in *2004 Year in Review*, *supra* note 88, at 131. However, this case is dealing with a different defaulted contract on which *United Pacific* was also the surety.

²⁸⁶ *United Pac.*, 401 F.3d. at 1365.

²⁸⁷ *Id.*

²⁸⁸ No. 2001-BCA-3, 2005 DOL BCA LEXIS 1 (Jan. 25, 2005)

²⁸⁹ *Id.* at *19 (citing *Safeco Ins. Co., ASBCA No. 52,107, 03-2 BCA ¶32,341* for the proposition that express assignment of contractor's rights under contract, irrevocable power of attorney to surety, takeover agreement and government's knowledge of assignment entitles surety to pursue claims of the contractor).

²⁹⁰ Federal Acquisition Regulation: Relocation Costs, 67 Fed. Reg. 43,512 (June 27, 2002). The council amended the relocation cost allowability rules at FAR 31.205-35.

²⁹¹ Major Kevin J. Huyser et al., *Contract and Fiscal Law Developments of 2003—The Year in Review*, ARMY LAW., Jan. 2004, at 133 (discussing Federal Acquisition Regulation; Reimbursement of Relocation Costs on a Lump-Sum Basis, 67 Fed. Reg. 65,468 (Oct. 24, 2002) [hereinafter *2003 Year in Review*]).

²⁹² Federal Acquisition Regulation; Reimbursement of Relocation Costs on a Lump-Sum Basis, 70 Fed. Reg. 57,467 (Sept. 30, 2005).

Some respondents had expressed negative comments about whether an objective standard could be developed for cost reasonableness and allowability and whether lump-sum reimbursement was a common commercial practice.²⁹³ However, the FAR Councils ultimately determined an expanded lump-sum reimbursement would “reduce the accounting and administrative burden of that cost principle on contractors and lead to faster relocations.”²⁹⁴ Further, the new rule is intended to only allow an appropriate lump-sum reimbursement if the contractor has adequately supported its payments with auditable component costs projections.²⁹⁵ The Councils also determined that a lump-sum reimbursement for relocation expenses “may not be the predominant commercial practice at this time . . . [but it is a] common and growing practice.”²⁹⁶

Clarification of the Allowability of Contractor Training and Education Costs

Also through FAC 2005-06, the FAR Councils issued a final rule clarifying FAR 31.205-44 by eliminating confusing language and restrictions that created disparate treatment between similar education costs.²⁹⁷ Specifically, training and education costs are generally allowable if these costs are “related to the field in which the employee is working or may be reasonably expected to work” instead of a more restrictive principle that would have limited cost allowability to education costs to obtain an academic degree or to qualify for a job.²⁹⁸ Additionally, the final rule lists six specific unallowable costs for added clarity.²⁹⁹

A Good Guesstimate of Your Unallowable Costs Is Close Enough for Government Work.

In 2003, the FAR Councils proposed to amend FAR 31.201-6, Accounting for Unallowable Costs, to add a new paragraph that allows statistical sampling identification of unallowable costs and acceptability criteria for contractor sampling methods.³⁰⁰ Subsequently through the same aforementioned FAC 2005-06, the FAR Councils amended FAR 31.201-6 to allow statistical sampling identification of unallowable costs if specific criteria are met.³⁰¹ First, the sampling must result in an unbiased and reasonably representative sample. Second, large dollar or high risk transactions are not included in the sampling process and must be reviewed separately. Last, the statistical sampling can be verified through an audit.³⁰²

Lieutenant Colonel Karl W. Kuhn

²⁹³ *Id.* at 57,467.

²⁹⁴ *Id.* at 57,468.

²⁹⁵ *Id.*

²⁹⁶ *Id.*

²⁹⁷ Federal Acquisition Regulation; Training and Education Cost Principle, 70 Fed. Reg. 57,470 (Sept. 30, 2005).

²⁹⁸ *Id.* at 57,472.

²⁹⁹ *Id.*

³⁰⁰ Federal Acquisition Regulation; Application of Cost Principles and Procedures and Accounting for Unallowable Costs, 68 Fed. Reg. 28,108 (May 22, 2003).

³⁰¹ Federal Acquisition Regulation; Accounting for Unallowable Costs, 70 Fed. Reg. 57,463 (Sept. 30, 2005).

³⁰² *Id.* at 57,466.

Information Technology (IT)

What Is IT?

In dealing with IT, and especially with IT acquisitions, it helps to know what exactly is meant by “information technology.” To that end, the FAR Councils recently published an interim rule³⁰³ in the *Federal Register* reflecting changes to the definition incorporated in the 2004 Consolidated Appropriations Act.³⁰⁴ Specifically,

The rule modifies the definition of “information technology” at FAR 2.101(b) to include “analysis” and “evaluation.” The rule also modifies the term “information technology” to include peripheral equipment designed to be controlled by the central processing unit of a computer, and clarifies the term “ancillary equipment” to include imaging peripherals, input, output, and storage devices necessary for security and surveillance.³⁰⁵

The FAR Councils also published an interim rule³⁰⁶ that emphasizes IT security, “focus[ing] much needed attention on the importance of system and data security by contracting officials and other members of the acquisition team.”³⁰⁷ The rule acknowledges “security as an important part of all phases of the IT acquisition life cycle.”³⁰⁸ Additionally, the DOD published proposed changes to the DFARS that would “delete obsolete procedures for the exchange or sale of Government-owned information technology,”³⁰⁹ and that would modify language concerning acquisition of telecommunications services.³¹⁰

Better Watch Those Contractors

The FAR Councils and the DOD are not the only entities issuing reminders about IT security. In April 2005, the GAO published a report³¹¹ encouraging better agency oversight over contractor access to sensitive IT systems. Noting that “[c]ontractors and users with privileged access to federal data and systems provide valuable services that contribute to the efficient functioning of the government,”³¹² the GAO also observed that the presence of contractors poses “a range of risks. . . .”³¹³ The GAO recommended incorporating “key elements of FISMA”³¹⁴ into the FAR and into agency contracting actions.³¹⁵

³⁰³ Federal Acquisition Regulation; Definition of Information Technology, 70 Fed. Reg. 43,577-43,578 (July 27, 2005) (to be codified at 48 C.F.R. pt. 2).

³⁰⁴ Consolidated Appropriations Act, 2004, Pub. L. No. 108-199, 118 Stat. 3 (2004).

³⁰⁵ 70 Fed. Reg. at 43,577.

³⁰⁶ Federal Acquisition Regulation; Information Technology Security, 70 Fed. Reg. 57,449-57,450 (Sept. 30, 2005) (to be codified at 48 C.F.R. pts. 1, 2, 7, 11, 39).

³⁰⁷ *Id.* at 57,450.

³⁰⁸ *Id.*

³⁰⁹ Defense Federal Acquisition Regulation Supplement; Exchange or Sale of Government-Owned Information Technology, 70 Fed. Reg. 54,697-54,698, (proposed Sept. 16, 2005) (to be codified at 48 C.F.R. pt. 239).

³¹⁰ Defense Federal Acquisition Regulation Supplement; Acquisition of Information Technology, 70 Fed. Reg. 54,698-54,699 (proposed Sept. 16, 2005) (to be codified at 48 C.F.R. pts. 239, 252).

³¹¹ U.S. GEN. ACCOUNTABILITY OFF., REP. NO. GAO-05-362, INFORMATION SECURITY: IMPROVING OVERSIGHT OF ACCESS TO FEDERAL SYSTEMS AND DATA BY CONTRACTORS CAN REDUCE RISK (APR. 2005) [hereinafter OVERSIGHT REPORT].

³¹² *Id.* at 2.

³¹³ *Id.*

³¹⁴ *Id.* at 3. “FISMA” is the Federal Information Security Management Act of 2002, Pub. L. No. 107-347, 116 Stat. 2899 (2002).

³¹⁵ OVERSIGHT REPORT, *supra* note 311, at 3.

IPv6—Say That Three Times Fast!

Internet protocol version 6 (IPv6), like its predecessor IPv4, is an Internet “addressing mechanism that defines how and where information such as text, voice, and video move across interconnect networks.”³¹⁶ Its developers designed it “to increase the amount of available IP [Internet protocol] address space.”³¹⁷ While recognizing that “transition is already underway” largely because IPv6 can greatly increase address space, the GAO also cautioned agencies that IPv6 can “introduce additional security risks,” such as unauthorized traffic and more direct access from the Internet.³¹⁸ Fortunately, the DOD appears ahead of other agencies in planning for the transition to this updated Internet protocol.³¹⁹

Who Let the Data Out?

In July 2005, the GAO strongly criticized the federal government for a general lack of IT security.³²⁰ Using sweeping language, the GAO castigated executive branch agencies for “[p]ervasive weaknesses in . . . information security policies and practices [that] threaten the integrity, confidentiality, and availability of federal information and information systems” and that “put federal operations and assets at risk of fraud, misuse, and destruction.”³²¹ Though the report acknowledges that “the government is making progress in its implementation of FISMA,” it nonetheless asserts that agency weaknesses “place financial data at risk of unauthorized modification or destruction, sensitive information at risk of inappropriate disclosure, and critical operations at risk of disruption.”³²² If the IT sky really is falling across the government, at least it’s falling everywhere—the report attributes “pervasive weaknesses” to “24 major agencies.”³²³ Unfortunately, the report doesn’t address reactions from those twenty-four agencies to these allegations. However, it does include a two-page letter from the OMB disagreeing with several GAO suggestions for the OMB,³²⁴ as well as a two-page GAO response.³²⁵

Lieutenant Colonel John J. Siemietkowski

Intellectual Property

Trade Secrets and the Federal Tort Claims Act

In *Jerome Stevens Pharmaceuticals v. Food & Drug Admin.*,³²⁶ the Court of Appeals for the District of Columbia held that a contractor may sue the federal government for wrongful disclosure of trade secrets under the Federal Tort Claims Act (FTCA).³²⁷ Although *Jerome Stevens* is not the first case to have such a holding,³²⁸ it is the only case disposing of the issue as to whether disclosure of trade secrets is a discretionary function of a federal agency.³²⁹ In the opinion, the court

³¹⁶ U.S. GEN. ACCOUNTABILITY OFF., REP. NO. GAO-05-471, *Internet Protocol Version 6: Federal Agencies Need to Plan for Transition and Manage Security Risks* Highlights (May 2005).

³¹⁷ *Id.*

³¹⁸ *Id.* at What GAO Found.

³¹⁹ *Id.*

³²⁰ U.S. GEN. ACCOUNTABILITY OFF., REP. NO. GAO-05-552, INFORMATION SECURITY: WEAKNESSES PERSIST AT FEDERAL AGENCIES DESPITE PROGRESS MADE IN IMPLEMENTING RELATED STATUTORY REQUIREMENTS (JULY 2005).

³²¹ *Id.* at What GAO Found.

³²² *Id.*

³²³ *Id.*

³²⁴ *Id.* at 42-43.

³²⁵ *Id.* at 44-45. The report also includes a list of thirty-two GAO reports since 2002, all generally critical of federal IT security efforts. *Id.* at 47-49.

³²⁶ 402 F.3d 1249 (D.C. Cir. 2005).

³²⁷ 28 U.S.C.S. § 1346 (b) (LEXIS 2005).

³²⁸ See *Kramer v. Secretary, U.S. Dep't of the Army*, 653 F.2d 726 (2d Cir. 1980) (holding that the alleged wrongful disclosure of the name of a subcontractor amounted to an allegation of wrongful misuse of a trade secret, however mislabeled, within the district court's jurisdiction under the Federal Tort Claims Act).

³²⁹ *Jerome Stevens Pharm.*, 402 F.3d at 1252; see Ralph C. Nash & John Cibinic, *Government Disclosure of a Trade Secret: A Tort Claim?*, 9 NASH & CIBINIC REP. 6, 28 (Jun. 2005).

states "[t]he parties appear to agree that the disclosure of trade secrets is not a discretionary function because federal law prohibits it."³³⁰ In addition, the court found that wrongful disclosure of a trade secret did not fall under the intentional tort exception of the FTCA.

The FTCA grants federal district courts jurisdiction over claims arising from certain torts committed by federal employees in the scope of their employment, and waives the government's sovereign immunity from such claims.³³¹ Two important exceptions to jurisdiction and the waiver of sovereign immunity are relevant here: the discretionary function exception and the intentional tort exception.³³² The discretionary function exception prohibits claims "based upon the exercise or performance or failure to exercise or perform a discretionary function or duty on the part of a federal agency or an employee of the Government, whether or not the discretion, involved is abused."³³³ The intentional tort exception prohibits "[a]ny claim arising out of assault, battery, false imprisonment, false arrest, malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit or interference with contract rights."³³⁴

In *Jerome Stevens*, the court did not ask whether the wrongful disclosure of a trade secret fell within the discretionary function exception. The court simply concluded that the parties seemed to agree that the discretionary function exception did not apply because federal law prohibits disclosing trade secrets.³³⁵

As for the second exception, the "district court treated [plaintiffs] claims of misappropriation of trade secrets and breach of a confidential relationship as a claim of interference with contract rights,"³³⁶ which the intentional tort exception bars.³³⁷ On appeal, the DC Circuit disagreed finding that the duties underlying such claims are different.³³⁸ Unlike wrongful disclosure of trade secrets, claims regarding intentional interference with contracts involve an economic relationship with a third party.³³⁹ Consequently, the court narrowly construed the intentional tort exception to "those circumstances [that] are within the words and reason of the exception"—no less and no more.³⁴⁰

After *Jerome Stevens*, it appears that tort relief is available to contractors when the government misappropriates or wrongfully discloses trade secrets.

DD Form 882 over Substance: Caveat Forfeiture

In a case of first impression, the CAFC, in *Campbell Plastics Engineering & Manufacturing v. Brownlee*,³⁴¹ held that the government may obtain title to the subject invention³⁴² where a contractor fails to comply with FAR invention disclosure requirements set forth in the contract. Harm to the government is not required in order for the contracting officer³⁴³ to remain within the bounds of sound discretion in demanding forfeiture.³⁴⁴

³³⁰ *Jerome Stevens Pharm.*, 402 F.3d at 1252 (citing 18 U.S.C. § 1905 (2000); 21 U.S.C. § 331(j) (2000); 5 U.S.C. § 552 (b)(4) (2000); 21 C.F.R. § 314.430 (2004)).

³³¹ *Id.* (citing *Sloan v. U.S. Dep't of Housing & Urban Dev.*, 236 F. 3d 756, 759 (D.C. Cir. 2001); 28 U.S.C. §§ 1346(b), 2674 (2000)).

³³² *See* 28 U.S.C.S. § 2680 (LEXIS 2005).

³³³ *Jerome Stevens Pharm.*, 402 F.3d at 1252 (citing 28 U.S.C. § 2680(a) (2000)).

³³⁴ *Id.* (citing 28 U.S.C. § 2680(h)).

³³⁵ *Id.* (citing 18 U.S.C. § 1905; 21 U.S.C. § 331(j); 5 U.S.C. § 552 (b)(4); 21 C.F.R. § 314.430 (2004)).

³³⁶ *Id.* at 1255.

³³⁷ 28 U.S.C. § 2680(a) (2000).

³³⁸ *Jerome Stevens Pharm.*, 420 F.3d at 1255.

³³⁹ *Id.*

³⁴⁰ *Id.* at 1256 (citing *Kosak v. United States*, 465 U.S. 848, 853 n. 9 (1984) (quoting *Dalenite v. United States*, 346 U.S. 15, 31 (1953))).

³⁴¹ 389 F.3d 1243 (Fed. Cir. 2004).

³⁴² 35 U.S.C. § 201 defines "subject invention" as "any invention of the contractor conceived or first actually reduced to practice in the performance of work under a funding agreement." 35 U.S.C. § 201 (2000).

³⁴³ In this case, the administrative contracting officer made the decision. Nonetheless, he will be referred to as the contracting officer throughout this discussion. *Campbell Plastics Eng'g & Mfg.*, 389 F.3d at 1243.

³⁴⁴ *Id.* at 1250 (referring to the abuse of discretion test set forth in *McDonnell Douglas Corp. v. United States*, 182 F.3d 1319, 1326 (Fed. Cir. 1999)).

Campbell Plastics, a § 8(a) contractor, entered into a cost-plus-fixed-fee contract with the Army to develop components of an aircrew protective mask. Section I of the contract incorporated by reference the FAR Clause 52.227-11, Patent Rights-Retention by the Contractor. This clause "requires a contractor to disclose any subject invention developed pursuant to a [G]overnment contract and sets forth certain substantive requirements for doing so."³⁴⁵ This clause allows the government to "obtain title if the contractor fails to disclose the invention within two months from the date upon which the inventor discloses it in writing to contractor personnel responsible for patent matters."³⁴⁶

Section I of the contract also incorporated by reference DFARS Clause 252.227-7039, Patents-Reporting of Subject Inventions, "which requires the contractor to disclose subject inventions in interim reports furnished" periodically.³⁴⁷ Most importantly, to report on inventions and subcontracts, the contractor was required to submit a Department of Defense (DD) Form 882. Although the contractor failed, repeatedly, to disclose any subject inventions on the DD Form 882, contractor disclosed all technical aspects of the invention to the Army.³⁴⁸ The Army even admitted that it possessed an enabling disclosure of the invention.³⁴⁹ Technically, however, the contractor did not comply with the contract requirement that the subject invention be disclosed on DD Form 882.

At the ASBCA, contractor argued that its failure to comply with the contract requirement was in "form only" and should not result in title forfeiture.³⁵⁰ The ASBCA denied contractor's appeal ruling that contractor "failed to satisfy its contractual obligation"³⁵¹ to properly inform the Army of the subject invention. Although the Army eventually found out about the subject invention, this was only discovered from "its review of the patent application for secrecy determination purposes and its own June 1997 report," which contractor did not supply.³⁵² Finally, the board held that FAR 52.227-11(d) allows the government to obtain title to a subject invention and the contracting officer in this case did not abuse his discretion in doing so.³⁵³ Consequently, the contractor appealed.

The Federal Circuit agreed with the ASBCA.³⁵⁴ The court focused on the purpose behind requiring disclosure of subject inventions to the government within a reasonable time after it has become known to contractor personnel:

Though the [Bayh-Dole] Act provides nonprofit organizations and small business firms the right to elect title to a subject invention, it also vests in the [G]overnment the right to a paid-up license to practice the invention when the contractor elects to retain title..., and the right to receive title to the invention in the United States or any other country in which the contractor has not filed a patent application on the invention prior to any pertinent statutory bar date.³⁵⁵

In other words, the disclosure provisions ensure that the government has sufficient measures to protect its own rights. The court found that the contract was clear in that it required the contractor disclose subject inventions on the DD Form 882. The court was unsympathetic to contractor's argument that the Army had knowledge of the substance of the invention. The court said that the requirement to have the disclosure on an "easily identified form . . . is sound and needs to be strictly enforced."³⁵⁶ Without rigid application of the rule, the government would never be sure of which piece of paper or oral statement might comprise the subject invention disclosure.³⁵⁷

³⁴⁵ *Id.* at 1244.

³⁴⁶ *Id.* (referring to FAR 52.227-11).

³⁴⁷ U.S. DEP'T OF DEF., DEFENSE FEDERAL ACQUISITION REG. SUPP. 252.227-7039 (July 2004) [hereinafter DFARS].

³⁴⁸ *Campbell Plastics Eng'g & Mfg.*, 389 F.3d at 1246.

³⁴⁹ *Id.*

³⁵⁰ *Id.*

³⁵¹ *Id.*

³⁵² *Id.*

³⁵³ *Id.*

³⁵⁴ *Id.* at 1243.

³⁵⁵ *Id.* at 1247.

³⁵⁶ *Id.* at 1249.

³⁵⁷ *Id.*

Arguing that forfeiture is disfavored by common law, the contractor asserted that the contracting officer abused his discretion in insisting on forfeiture when the government is not benefited in any way by such a decision.³⁵⁸ The Federal Circuit agreed with the ASBCA to apply the four-prong abuse of discretion test of *McDonnell Douglas Corporation v. United States* by looking at:³⁵⁹

evidence of whether the government official acted with subject bad faith; (2) whether the official had a reasonable, contract-related basis for his decision; (3) the amount of discretion given to the official; and (4) whether the official violated a statute or regulation.

The CAFC agreed with the board's finding that the contracting officer did not abuse his discretion. Commentators have disagreed with the outcome of this case, specifically criticizing the use of the *McDonnell Douglas* test in ascertaining abuse of discretion.³⁶⁰ In that case, a review of the factors the contracting officer actually considered occurred.³⁶¹ Here, the ASBCA's decision does not demonstrate that such a review happened.³⁶²

In conclusion, *Campbell Plastics* makes it clear that contractors must strictly comply with subject invention disclosure requirements found in government contracts to avoid forfeiture to title of invention. It is now abundantly clear that form, more specifically DD Form 882, triumphs over substance.

Major Katherine E. White

Non-FAR Transactions

DOD Issues Interim Rule Regarding Other Transaction Agreements

In last year's *Year in Review*, we discussed the DOD's latest regulatory changes to its authority to enter into agreements that "do not comply with the normal statutory and regulatory contracting rules."³⁶³ The Secretary of Defense and the Secretaries of the military departments have the authority to enter into non-traditional binding agreements for the purpose of research under two separate statutes.³⁶⁴ Title 10, Section 2358, permits the DOD to utilize grants and cooperative agreements for research purposes.³⁶⁵ Additionally, Title 10, Section 2371, permits the DOD to enter into agreements "other than contracts, grants, and cooperative agreements" for the purpose of research; these agreements are called other transaction agreements (OTAs).³⁶⁶

While the original OTA legislation did not allow a contractor performing the research to produce the item it researched,³⁶⁷ a 1993 amendment allowed that contractor to produce prototypes derived from the research.³⁶⁸ Later, a 2001 amendment allowed the DOD to award a follow-on production contract, without competition, to the contractor that had

³⁵⁸ *Id.* at 1250.

³⁵⁹ *Id.* at 1326

³⁶⁰ Ralph C. Nash & John Cibinic, *Postscript: Forfeiture of Title to Patent*, 19 NASH & CIBINIC REP. 1, 2 (Jan. 2005). Dave Burgett, *Feature Comment: Federal Circuit Upholds Patent Forfeiture for Failure to Comply Strictly with Reporting Requirement, Despite Lack of Prejudice*, 46 GOV'T CONTRACTOR 44, 457 (Nov. 2004).

³⁶¹ Ralph C. Nash & John Cibinic, *supra* note 360, at 2.

³⁶² *Id.*

³⁶³ See 2004 *Year in Review*, *supra* note 88, at 152.

³⁶⁴ See Pub. L. No. 85-599, 72 Stat. 520 (1947) and Pub. L. No. 101-189, 103 Stat. 1403 (1989).

³⁶⁵ Pub. L. No. 85-599, 72 Stat. 520 (1947).

³⁶⁶ Pub. L. No. 101-189, 103 Stat. 1403 (1989).

³⁶⁷ Major Kevin J. Huyser et al., *Contract and Fiscal Law Developments of 2003—The Year in Review*, ARMY LAW., Jan. 2004, at 159-60 [hereinafter 2003 *Year in Review*].

³⁶⁸ Pub. L. No. 103-160, § 845, 107 Stat. 1547, 1721 (1993).

produced the prototype under an OTA.³⁶⁹ In 2003, another amendment expanded the DOD's authority to award such follow-on contracts.³⁷⁰ In November 2004, this 2003 amendment was incorporated into an interim rule within the DFARS.³⁷¹

This interim rule, located at DFARS 212.7000-212.7003, implements Section 847 of the National Defense Authorization Act for Fiscal Year 2004.³⁷² The interim rule permits a "non-traditional defense contractor" to use FAR part 12 (Acquisition of Commercial Items) procedures for a follow-on contract not exceeding \$50,000,000 for the "production of an item or process begun as a prototype process under an other transaction agreement."³⁷³ The interim rule defines a "non-traditional defense contractor" as a contractor that has previously entered into an OTA with the DOD under the following circumstances: (1) the contractor has not performed any contract that is "subject to full coverage under the cost accounting standards" per FAR part 30 for the past year, and (2) the contractor has not performed any contract "exceeding \$500,000 to carry out prototype projects or to perform basic, applied or advanced research projects for a federal agency" for the past year.³⁷⁴ This authority is further limited to firm fixed-price contracts or fixed-price contracts with an economic price adjustment awarded on or before 30 September 2008.³⁷⁵

The Future of the Future Combat Systems

In May 2003, the Army awarded an estimated \$21 billion OTA to the Boeing Corporation for the research, development and demonstration of the Army's newest weapons program, the Future Combat Systems (FCS).³⁷⁶ This OTA, although a non-FAR transaction, did contain some FAR and DFARS clauses.³⁷⁷ While the FCS is currently in the research and development stage, the Army predicts that the FCS will be fully operational by the year 2016.³⁷⁸

The FCS is not a stand-alone weapon system, but is rather a "family of 18 manned and unmanned ground vehicles, air vehicles, sensors, and munitions that will be linked, by an information network."³⁷⁹ The purpose of the FCS concept is to allow the modern Army to utilize a network of lighter, often unmanned vehicles to provide combat sensitive information to the battlefield commander.³⁸⁰ The OTA for the systems development and demonstration phase involves eighteen weapons platforms and seventeen different subcontractors.³⁸¹ The OTA requires Boeing to serve as the "Lead System Integrator" with the responsibility for exercising oversight over the various subcontractors involved with the research, development and production of the FCS subsystems.³⁸²

After some pressure from Congress,³⁸³ the Secretary of the Army announced that the OTA the Army had entered into with Boeing would be transformed into a FAR-based contract.³⁸⁴ In a press release, Army Secretary Harvey stated that

³⁶⁹ National Defense Authorization Act for FY 2002, Pub. L. No. 107-107, 115 Stat. 1012, 1182-83 (2001). This act permitted the DOD to award a follow-on production contract to the participant in an OTA for the development of a prototype without the use of competitive procedures. *Id.*

³⁷⁰ Pub. L. No. 108-136, § 847, 117 Stat. 1392 (2003).

³⁷¹ Defense Federal Acquisition Regulation Supplement; Transition of Weapons-Related Prototype Projects to Follow-on Contracts, 69 Fed. Reg. 63,329 (Nov. 1, 2004) (amending 48 C.F.R. pt. 212).

³⁷² *Id.*

³⁷³ *Id.*

³⁷⁴ *Id.*

³⁷⁵ *Id.*

³⁷⁶ U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-05-442T 10-12, DEFENSE ACQUISITIONS: FUTURE COMBAT SYSTEMS CHALLENGES AND PROSPECTS FOR SUCCESS (2005) (testimony before the Subcommittee on Airland, Committee on Armed Servs., U.S. Senate) (statement of Paul L. Francis, Director of Acquisition and Sourcing Management).

³⁷⁷ *Id.* at 12.

³⁷⁸ *Id.* at 23.

³⁷⁹ *Id.* at 4.

³⁸⁰ *Id.* at 6.

³⁸¹ *Id.* at 10.

³⁸² *Id.*

³⁸³ Jonathan Karp and Andy Pasztor, *Army Program Run by Boeing Faces Challenge by Sen. McCain*, WALL ST. J., Mar. 15, 2005, at A1.

while “the OTA was appropriate for the earlier phases of the FCS . . . we need a contractual arrangement that best ensures FCS is properly positioned” for the modern Army force.³⁸⁵

Major Marci Lawson, USAF

Payment and Collection

DFARS Sets the Example - FAR Catches Up with Final Rule Allowing Optional Withholding under Time-and-Materials and Labor-Hour Contracts

As we reported last year, the DOD issued a final rule adding DFARS 232.111(b) and DFARS 252.232-7006, Alternate A, that clarified determinations whether to withhold payments under time-and-materials and labor-hour contracts.³⁸⁶ The new clause notes that “there should be no need to withhold payment for a contractor with a record of timely submittal of the release discharging the Government from all liabilities, obligations, and claims.”³⁸⁷ However when determined necessary to protect the government’s interest, the Administrative Contracting Officer may issue a unilateral modification to withhold five percent of payment amounts due, up to a maximum of \$50,000.³⁸⁸

Subsequently, the FAR Councils issued a final rule as FAC 2005-05 that also revised the FAR to allow optional withholding for Time-and-Materials and Labor-Hour Contracts.³⁸⁹ The final rule amended FAR 32.111 and 52.232-7 by removing the prior withholding mandatory requirement to allow the contracting officer to issue a unilateral modification to withhold five percent of the payments due, up to a maximum of \$50,000 if considered necessary to protect the government’s interest.³⁹⁰ In response to comments on the initial proposed rule,³⁹¹ the FAR Councils clarified that the \$50,000 withhold ceiling applies to the entire contract and not to each individual order under a task order contract.³⁹²

“Ouch, that Hurts Mr. Taxman! Mr. KO, What is a Poor Contractor to do?”

The DOD has issued an interim rule through DFARS Case 2004-D033 addressing the effect of Internal Revenue Service (IRS) collections of tax debts against an indebted contractor’s payments for performance under DOD contracts.³⁹³ This process of IRS debt collection is referred to as a levy and authorizes the government to continuously withhold up to one hundred percent of every contractor payment until the tax debt is satisfied.³⁹⁴ Recognizing that there is a high risk of contract non-performance from the application of an IRS levy, DFARS 232.7100 and 252.232-7010 were added “to ensure that all parties understand their rights and obligations related to the assessment of a levy.”³⁹⁵ The DOD noted in the interim rule that it should be the contractor’s responsibility to identify and notify the government of any levy significantly impacting contract performance because it is the contractor’s tax delinquency creating the situation.³⁹⁶

Accordingly, DFARS 252.232-7010(b) requires the contractor to promptly notify the Contracting Officer of any levy that will jeopardize contract performance. The notification must include the dollar amount of the levy, the rationale and adequate supporting documentation of how the levy will jeopardize contract performance, and explain if an inability to

³⁸⁴ Press Release, U.S. Army Public Affairs, Army Announces Business Restructuring of the FCS Program (Apr. 30, 2005), at <http://www4.army.mil/ocpa/print..>

³⁸⁵ *Id.*

³⁸⁶ Defense Federal Acquisition Regulation Supplement; Payment Withholding, 68 Fed. Reg. 69,631 (Dec. 15, 2003).

³⁸⁷ DFARS, *supra* note 347, at 232.111(b)(ii).

³⁸⁸ *Id.* at 232.111(b)(iii).

³⁸⁹ Federal Acquisition Regulation; Payment Withholding, 70 Fed. Reg. 43,580 (July 27, 2005).

³⁹⁰ *Id.* at 43,581.

³⁹¹ Federal Acquisition Regulation; Payment Withholding, 69 Fed. Reg. 29,838 (May 25, 2004).

³⁹² 70 Fed. Reg. at 43,580.

³⁹³ Defense Federal Acquisition Regulation Supplement; Levy on Payments to Contractors, 70 Fed. Reg. 52,031 (Sept. 1, 2005).

³⁹⁴ See 26 U.S.C.S. §§ 6331-6332 (LEXIS 2005).

³⁹⁵ 70 Fed. Reg. at 52,031.

³⁹⁶ *Id.*

perform the contract will adversely affect national security. If the Contracting Officer determines in joint consultation with the Director, Defense Procurement and Acquisition Policy (DPAP) that a lack of performance will adversely affect national security, the DPAP will notify the IRS and “some or all of the monies collected will be returned to the contractor.”³⁹⁷

Proposed Rule Issued to Clarify Payments under Time-and-Materials (T&M) Contracts

The FAR Councils through FAR Case 2004-015 proposed to amend FAR part 16.307 and specify that FAR clause 52.216-7, Allowable Cost and Payment, is included in T&M contracts.³⁹⁸ The description of T&M contracts at FAR part 16.601 notes that supplies or services are acquired on the basis of “[d]irect labor hours at specified fixed hourly rates that include wages, overhead, , general and administrative expenses, and profit.”³⁹⁹ This pricing basis under a T&M contract would be the time portion and is usually referred to as loaded labor rates. The materials portion is for the materials used in contract performance “at cost, including, if appropriate, material handling costs.”⁴⁰⁰ Accordingly, the proposed rule would require the typical clause used in cost contracts, FAR part 52.216-7, “as applicable to the portion of the contract that provides for reimbursement of materials at actual cost.”⁴⁰¹ Additionally, the definition of materials at FAR part 16.601 would be amended to include other typical costs under a T&M contract associated with material costs, such as, subcontract costs for supplies and services and applicable indirect costs (e.g., general and administrative expenses).⁴⁰²

Re-do—\$45 Billion and Counting: Magnitude of Government Improper Payments Remains Unknown

As we reported have reported in prior years, Congress remains very interested in the identification and recovery of agency improper payments.⁴⁰³ Thus, Congress enacted the Improper Payments Information Act of 2002 (IPIA)⁴⁰⁴ that “requires each agency to annually identify all ‘programs and activities that may be susceptible to significant improper payments’ and report an annual estimate of improper payments to Congress.”⁴⁰⁵

For FY 2004, the GAO reviewed Performance and Accountability Reports (PAR) from twenty-nine agencies and reported on the challenges remaining in meeting the aforementioned requirements of the IPIA.⁴⁰⁶ Specifically the GAO noted that the federal government had made progress because twenty-three of the twenty-nine agencies reported they had completed identifying programs at risk for improper payments and seventeen of those agencies had estimated and reported over \$45 billion of improper payments.⁴⁰⁷ However, the full magnitude of the improper payments problem remains unknown because all of the reviewed agencies had neither completed identification of at-risk programs, nor provided an estimate of their improper payments in accordance with the IPIA.⁴⁰⁸

Specifically for the DOD, it reported that it had assessed all programs and estimated \$100 million in improper military health benefit payments and \$34 million in improper military retirement fund payments.⁴⁰⁹ Finally, true success in resolving the improper payments issue and complying with the IPIA involves implementing actions to identify and recover improper payments as well as eliminating the initial occurrence. Although the report noted that the OMB reported federal

³⁹⁷ *Id.*

³⁹⁸ Federal Acquisition Regulation; Payments Under Time-and-Materials and Labor-Hour Contracts, 70 Fed. Reg. 56,314 (Sept. 26, 2005).

³⁹⁹ FAR, *supra* note 274, at 16.601.

⁴⁰⁰ *Id.*

⁴⁰¹ 70 Fed. Reg. at 185.

⁴⁰² *Id.*

⁴⁰³ See 2003 Year in Review, *supra* note 367, at 163.

⁴⁰⁴ Pub. L. No. 107-300, 116 Stat. 2350 (2002) [hereinafter IPIA].

⁴⁰⁵ 2003 Year in Review, *supra* note 367, at 163 (quoting IPIA, § 2(a), 116 Stat. 2350).

⁴⁰⁶ U.S. GOV'T ACCOUNTABILITY OFF., REP. NO. GAO-05-417, FINANCIAL MANAGEMENT: CHALLENGES IN MEETING REQUIREMENTS OF THE IMPROPER PAYMENTS INFORMATION ACT (Mar. 2005).

⁴⁰⁷ *Id.* at 3.

⁴⁰⁸ *Id.* at 9.

⁴⁰⁹ *Id.* at 21.

agencies had “established a strong foundation for . . . identifying and implementing the necessary corrective actions,” the GAO had not specifically reviewed the effectiveness of improper payment identification and recovery actions.⁴¹⁰

Lieutenant Colonel Karl Kuhn

Performance-Based Service Acquisitions (PBSA)

Final Rule on PBSA Incentives

As discussed in last year’s *Year in Review*,⁴¹¹ the FAR Councils issued a final rule which expands the government’s authority to treat performance-based contracts or task orders for services as commercial items as long as the contracts meet specified criteria.⁴¹² This criterion includes a firm-fixed price for specific tasks, a contractor that provides similar services to the general public, and a contract under \$25 million which meets the FAR definition of performance-based contracting.⁴¹³ The FAR Councils made a small change intended to give contracting officers discretionary authority to tailor the remedies clause in the event that customary commercial practices do not exist for the types of services under contract.⁴¹⁴

Challenging the ‘Paradyne’ of PBSAs

The GAO rejected a challenge to a minimum staffing requirement in a performance-based contract in *United Paradyne Corporation*.⁴¹⁵ The Air Force issued a RFP for the award of a fixed-price contract for fuels management services at Wright-Patterson AFB, Ohio. United Paradyne, the incumbent, protested the requirement that only one person be continuously present for safety, security, and environmental reasons because the company traditionally had used two employees during the midnight shift.⁴¹⁶ The GAO noted that the FAR required performance-based work statements “to the maximum extent practicable.”⁴¹⁷ Given that standard, the GAO concluded that the Air Force’s requirement was neither unreasonable nor improper.⁴¹⁸ The GAO also noted that the Air Force attempted to use a performance-based standard in the prior contracts, but that problems with appropriate manning had led the Air Force not to exercise the option-year and resolicit the contract.⁴¹⁹

Major Andrew S. Kantner

Procurement Fraud

The past year saw a number of significant developments in False Claims Act litigation, particularly with regard to *qui tam* suits.⁴²⁰

⁴¹⁰ *Id.* at 4.

⁴¹¹ See 2004 *Year in Review*, *supra* note 88, at 157.

⁴¹² Federal Acquisition Regulation; Incentives for Use of Performance-Based Contracting for Services, 70 Fed. Reg. 33,657 (June 8, 2005) (to be codified at 48 C.F.R. pts. 2, 4, 12, 37 and 52).

⁴¹³ See FAR, *supra* note 274, at 2.101. Performance-based contracting is defined as, “structuring all aspects of an acquisition around the purpose of the work to be performed with the contract requirements set forth, in clear, specific, and objective terms with measurable outcomes as opposed to either the manner by which the work is to be performed or broad and imprecise statements of work.” *Id.*

⁴¹⁴ 70 Fed. Reg. at 33,659.

⁴¹⁵ Comp. Gen. B-296609, 2005 U.S. Comp. Gen. LEXIS 151 (Aug. 19, 2005).

⁴¹⁶ *Id.* at *6.

⁴¹⁷ See FAR, *supra* note 274, at 11.002 (a)(2)(i).

⁴¹⁸ *United Paradyne Corp.*, 2005 U.S. Comp. Gen. LEXIS 151, at *7.

⁴¹⁹ *Id.* at *7 n.1.

⁴²⁰ *Qui tam* suits are suits filed under the False Claims Act pursuant to 31 U.S.C. 3730, whereby private individuals known as a “relators” are permitted to act as like a private attorneys general and file action alleging fraud against the government. The government may or may not join the relator’s suit but regardless whether or not the government joins the suit, pursuant to the statute, relators are entitled to share in any recovery if the suit proves successful. RALPH. C. NASH ET AL., THE GOVERNMENT CONTRACTS REFERENCE BOOK, A COMPREHENSIVE GUIDE TO THE LANGUAGE OF PROCUREMENT (2d ed. 1998).

Custer (Battle)'s Last Stand?

In a case of particular interest to the military, on 8 July 2005, the District Court for the Eastern District of Virginia denied a motion for summary judgment and allowed a case to proceed in a *qui tam* action against Custer Battles, LLC (Custer Battles).⁴²¹ A former Custer Battles' employee and others brought the *qui tam* action alleging that Custer Battles had inflated claims on two contracts with the Coalition Provisional Authority (CPA) for security services at the Baghdad International Airport. Before denying the motion, the court addressed two interesting legal issues. The first issue was whether a claim against the CPA was sufficient to constitute a "claim" under the False Claims Act (FCA).⁴²² The second issue was whether a claim presented to the CPA was a claim "presented" to U.S. officials pursuant to the statute.⁴²³

On the first issue, the court determined that in order to be subject to the FCA, there must be a request for or actual payment from federal property.⁴²⁴ The court held that while "§ 3729(a)(1) requires a 'claim,' or a request or demand for payment that if paid would result in economic loss to the government fisc, i.e. a request for payment of government funds; it does not extend to cases where the government acts solely as custodian, bailee, or administrator, merely holding or managing property for the benefit of a third party."⁴²⁵ The court went on to determine that claims against CPA Vested Funds⁴²⁶ and Seized Funds⁴²⁷ constituted claims subject to the FCA,⁴²⁸ but that claims against the Developmental Fund for Iraq (DFI)⁴²⁹ were not subject to the FCA because "the CPA played a restricted role as an administrator or custodian of the funds in the DFI, required to expend Iraqi money for the benefit of the people of Iraq. Accordingly, if DFI funds were paid out in response to a fraudulent request for payment, the United States would not suffer any economic loss."⁴³⁰

On the second issue, as to whether or not the claim was "presented to a U.S. government official," the court found that "the undisputed facts in the record reflect that demand for payment from Seized and Vested Funds under [both] contracts were presented to a member of the Armed Forces [who were acting as contracting officers for the CPA] before payment."⁴³¹ The court held that this presentment satisfied the requirements of the FCA regardless of whether or not the CPA was determined to be an instrumentality of the United States.⁴³² The court held that, under a causation theory, the claim presented to the CPA officials ultimately caused those officials to present the claims to an officer of the United States Army.⁴³³ "The presentment requirement is satisfied in the case of all requests or demands in connection with [these cases] that were paid from Seized or Vested Funds."⁴³⁴

⁴²¹ United States *ex rel.* DRC, Inc. et al. v. Custer Battles, LLC et al., 376 F. Supp. 2d 617 (E.D. VA. 2005).

⁴²² 31 U.S.C.S. 3729 (LEXIS 2005). The *qui tam* provisions of the False Claims Act authorize "private persons" to bring action for a violation of the FCA in the government's stead. The FCA provides civil penalties against any person who: (1) knowingly presents, or causes to be presented, to an officer or employee of the United States Government or member of the Armed Forces of the United States a false or fraudulent claim for payment or approval; Section 3729(c) defines "claim" to include "any request or demand . . . for money or property which is made to a contractor, grantee, or other recipient if the United States Government provides any portion of the money or property which is requested or demanded, or if the Government will reimburse such contractor, grantee, or other recipient for any portion of the money or property which is requested or demanded."

⁴²³ *Custer Battles, LLC.*, 376 F. Supp. 2d at 635.

⁴²⁴ *Id.* at 639.

⁴²⁵ *Id.* at 641.

⁴²⁶ "Vested Funds" are Iraqi funds confiscated by the U.S. pursuant to an executive order authorized by the International Emergency Economic Powers Act (see 50 U.S.C. § 1702(a)(1)(C)) under which "all rights, title and interest" in the confiscated funds vests in the agency or person designated by the President, in this case the U.S. Treasury. *Custer Battles, LLC*, 376 F. Supp. 2d at 624.

⁴²⁷ "Seized Funds" are Iraqi state-owned funds seized by Coalition forces in Iraq. Under customary international law, Iraqi state-owned cash and other moveable property became U.S. government property once they were transferred to Army custody. *Custer Battles, LLC.*, 376 F. Supp. 2d at 626.

⁴²⁸ *Id.* at 647.

⁴²⁹ Developmental Funds for Iraq was not U.S. Government property because the DFI was created by the U.N. and the CPA as a depository for proceeds from the sale of Iraqi national resources and repatriated Iraqi funds to fund relief and reconstruction efforts for the Iraqi people. The court held that these funds always belonged to the Iraqi people. *Id.* at 645.

⁴³⁰ *Id.*

⁴³¹ *Id.* at 647.

⁴³² *Id.* at 648.

⁴³³ *Id.*

⁴³⁴ *Id.*

The denial of the motion for summary judgment in this case just means the case will be allowed to go forward. Whether or not Custer Battles⁴³⁵ will ultimately be found liable is a question for a future day. However, given the ever-increasing variety of roles the United States is playing in the world, the decision in this case is particularly noteworthy.

KBR Employee Convicted

Custer Battles was not the only contractor in Iraq facing allegations of price gouging. In March, two individuals, one, a former Kellogg, Brown, and Root (KBR) employee, and the other, the managing partner of a Kuwaiti business, were charged in a ten-count indictment for “charges of devising a scheme to defraud the United States of more than \$3.5 million related to the awarding of a subcontract to supply fuel tankers for military operations in Kuwait.”⁴³⁶ According to the indictment, the KBR employee negotiated and managed subcontracts on behalf of KBR under the Logistics Civilian Augmentation Program (LOGCAP) III prime contract.⁴³⁷ The indictment alleges that the KBR employee inflated bids of all competitors and ensured that one particular subcontractor won the contract.⁴³⁸

The subcontract was supposed to pay the subcontractor more than \$5.5 million dollars, despite KBR’s estimate of just over \$680,000 and the subcontractor allegedly paid the former KBR employee \$1 million for the favorable treatment they received.⁴³⁹ KBR reportedly brought the issue to the attention of the Department of Justice and the Department of Defense after discovering the discrepancy. The employee faces a maximum of ten years confinement and a fine of up to \$5 million for each count in the indictment under the Major Fraud Act and no more than twenty years in prison and a fine of up to \$250,000 for each count of wire fraud.⁴⁴⁰

Upon Further Review, the Call in the Field Is Reversed

In last year’s *Year in Review*, we reported that a divided Fourth Circuit concluded that retaliation claims are subject to the False Claims Act’s (FCA)⁴⁴¹ six-year statute of limitations, rather than the local state’s three year limitation period for wrongful discharge actions.⁴⁴² This created a split in the circuits on this issue and the Supreme Court granted certiorari to hear the appeal.⁴⁴³ In the *Graham County Soil and Water Conservation District, et al. v. United States ex rel. Wilson*, the Supreme Court reversed the Fourth Circuit and held that because the statute is ambiguous, the statute of limitations

⁴³⁵ See generally Jason McLure, *How a Contractor Cashed in on Iraq*, LEGAL TIMES, Mar. 4, 2005, available at www.law.com/jsp/article.jsp?id+11098526942 (last visited Oct. 15, 2005), for an interesting article detailing how, for critics of the Bush administrations handling of postwar Iraq, Custer Battles has become something of a symbol of contractor excess during the fourteen-month period that the Coalition Provisional Authority governed Iraq.

⁴³⁶ Press Release, U.S. Attorney for the Central District of Illinois, *Former KBR Employee and Subcontractor Charged with \$3.5 Million Government Contract Fraud in Kuwait* (Mar. 17, 2005), available at <http://www.usdoj.gov/isao/ilc/press/2005/march/Mazon%20indict031705.pdf>

⁴³⁷ *Id.*

⁴³⁸ *Id.*

⁴³⁹ *Id.*

⁴⁴⁰ *Id.* at 2. The Kuwaiti businessman was also indicted, but has not been apprehended due to his residence outside the United States. *Id.* at 1.

⁴⁴¹ 31 U.S.C.S. § 3729(a) (LEXIS 2005).

⁴⁴² 2004 *Year In Review*, *supra* note 88, at 159.

⁴⁴³ The source of the split in the circuit court’s was caused by the 1986 amendments to the FCA that created a third enforcement mechanism—that being a private cause of action for an individual retaliated against by his employer for assisting an FCA investigation or proceeding. This new mechanism was in addition to the longstanding government right and an individual relator’s right to sue the alleged violator, but the statute of limitation language contained in the FCA only addressed the original two causes of action and does not specifically address the newer whistleblower retaliation claims. 31 U.S.C. § 3730(h). Remedies for retaliation claims include reinstatement, two times the amount of back pay plus interest, special damages, litigation costs, and attorney’s fees. 31 U.S.C.S. § 3730(h) (LEXIS 2005). The 1986 amendments also revised the language of the 6-year statute of limitations applicable to FCA actions. The current provision reads:

- (b) A civil action under section 3730 may not be brought—
 - (1) more than 6 years after the date on which the violation of *section 3729* is committed, or
 - (2) more than 3 years after the date when facts material to the right of action are known or reasonably should have been known by the official of the United States charged with responsibility to act in the circumstances, but in no event more than 10 years after the date on which the violation is committed

31 U.S.C.S. § 3731(b)(1) (emphasis added).

provisions pertaining to causes of action seeking a remedy for a false claim under the FCA do not govern whistle-blower retaliation claims made pursuant to 31 U.S.C. 3730.⁴⁴⁴ Instead, the Court held that the most analogous state statute of limitations applies.⁴⁴⁵

“False Claim” by Subcontractor not a Claim until Prime Makes It So

In an interesting case from the District Court for the Southern District of Ohio, the court held that evidence of an allegedly false claim from a subcontractor to a prime contractor is not sufficient, as a matter of law, to meet the civil FCA requirement for a claim “to the Government,” even if the subcontractor’s claim was paid with federal funds.⁴⁴⁶ Two relators brought this *qui tam* suit regarding alleged failures by subcontractors on the Navy’s Arleigh Burke destroyer program.⁴⁴⁷ Normally, knowingly false claims submitted by a subcontractor through a prime contractor for payment by the government would constitute a false claim under the FCA.⁴⁴⁸ However, in this case, the court held that relators offered no evidence of claims or certifications from the prime contractors to the Navy and that claims between contractors themselves were insufficient to satisfy the relators’ burden of proof that a claim was actually made to the government.⁴⁴⁹

Employees with Oversight of Government Contracts Have Special Rules in Retaliation Claims

In a blow to potential whistle-blowers working for contractors with duties as a government contract overseer, the Court of Appeals for the First Circuit granted summary judgment in favor of the defendant in a case where a relator brought suit against his company under the Rhode Island Whistle-Blowers’ Protection Act⁴⁵⁰ alleging that his company was double-billing the government for the salaries of some employees.⁴⁵¹ In this case, the relator was the president of McLaughlin Research Corporation (MRC) with responsibility for overseeing MRC contracts with the DOD.⁴⁵² Mr. Maturi discovered the billing problems and alerted the MRC Chairman of the Board of the potential liability if Defense Contract Audit Agency (DCAA) auditors scrutinized MRC’s billing practices.⁴⁵³ The board chairman found the letter threatening and constituted the “last straw” for an employee whose job performance was already under scrutiny so she fired Mr. Matsui.⁴⁵⁴

The court held that

ordinarily an employer is charged with knowledge that an employee is engaged in protected conduct when the employer is put on notice that the employee is taking action that could reasonably lead to an FCA case, . . . where an employee’s job responsibilities involve overseeing government billings or payments, his burden of proving that his employer was on notice that he was engaged in protected conduct should be heightened. Yet, such an employee can put his employer on notice by any action which . . . [regardless of his job duties,] would put the employer on notice that [FCA] litigation is a reasonable possibility.⁴⁵⁵

⁴⁴⁴ 125 S. Ct. 2444 (2005).

⁴⁴⁵ *Id.* at 2451.

⁴⁴⁶ U.S. *ex rel.* Sanders and Thacker v. Allison Engine Co., Inc., Gen. Motors Corp., Gen. Tool Co., & Southern Ohio Fabricators, Inc., 2005 U.S. Dist. LEXIS 5612, 2005 WL 713569 (S.D. Ohio Mar. 11, 2005).

⁴⁴⁷ *Id.*

⁴⁴⁸ 31 U.S.C.S. § 2729(a)(2) (LEXIS 2005); *see also* United States v. Bornstein, 423 U.S. 303, 309 (1975); U.S. *ex rel.* Totten v. Bombardier Corp., 380 F.3d 488, 493, *reh’g en banc denied* (D.C. Cir. 2004).

⁴⁴⁹ U.S. *ex rel.* Sanders and Thacker v. Allison Engine Co., Inc., *et al.*, 2005 U.S. Dist. LEXIS 5612, at 30-31.

⁴⁵⁰ R.I. Gen. Laws § 28-50-1.

⁴⁵¹ Maturi v. McLaughlin Research Corp., 413 F.3d 166 (1st Cir. July 1, 2005).

⁴⁵² *Id.* at 169-70.

⁴⁵³ *Id.* at 171.

⁴⁵⁴ *Id.*

⁴⁵⁵ *Id.* at 173.

In this case, the court held that the relator's notice to the board chairman of billing problems and potential liability "could not reasonably have put [the company] on notice that FCA litigation was a realistic possibility" prior to his termination.⁴⁵⁶

Government Need Not Intervene Prior to Seeking Dismissal of FCA Qui Tam Suit

Ordinarily, in order to intervene for purpose of pursuing the litigation in a *qui tam* action after the sixty-day seal period expires,⁴⁵⁷ the government needs to first make a showing of good cause.⁴⁵⁸ In an interesting case which extends recent case law, the Tenth Circuit held that "the Government, in a case in which it has declined to intervene in the [60-day] seal period, is not required to intervene [in a *qui tam* suit] with a showing of good cause under [31 U.S.C.] § 3730(c)(3) before moving to dismiss the action under § 3730(c)(2)(A)."⁴⁵⁹ This case extends what had previously been established law that the government does not have to intervene in a case in order to bring a motion to dismiss the case *during* the seal period.⁴⁶⁰

The court also adopted the Ninth Circuit's standard for determining whether dismissal of a relator's *qui tam* suit under the FCA is appropriate.⁴⁶¹ The court held that the appropriate test is "identification of a valid government purpose; and a rational relationship between dismissal and accomplishment of the purpose."⁴⁶² The court went on to find that the government's stated purpose of protecting classified information from disclosure and the timely closing of an installation "were valid governmental purposes supporting its motion to dismiss the *qui tam* action" and that the government satisfied the second part of the test "by advancing a 'plausible, or arguable' reason for the dismissal."⁴⁶³

Undervalued Bids May Constitute Fraud in the Inducement under the FCA

In a case that failed to resolve the issue, but instead raised another interesting issue to watch for in the future, the Court of Appeals for the District of Columbia failed to address whether a contractor's intentional underbidding with the intent to win the contract award and later obtain upward modifications constituted a valid basis for a fraud in the inducement claim under the FCA.⁴⁶⁴ Courts have held that when a "fraud in the inducement" theory applies, a contractor is liable under the FCA for all claims submitted on the awarded contract even if the claims themselves were not fraudulent.⁴⁶⁵

In this case, the lower District Court had acknowledged that, "if construed broadly," the fraud in the inducement theory could apply to claims such as the one in this case.⁴⁶⁶ The lower court held, however, that "while claims submitted under a contract obtained after a fraudulently *inflated* bid are actionable even though the claims are neither false nor fraudulent themselves where it is alleged that the defendant has submitted a fraudulently deflated bid, it must be shown not only that the low bid was fraudulent, but also that one or more of the requests for payment under the contract induced by the low bid were also fraudulent."⁴⁶⁷

⁴⁵⁶ *Id.*

⁴⁵⁷ The "seal period" is a window of time following the relator's filing of a *qui tam* action in district court during which the Department of Justice is notified of the suit, but the defendant is not. The period is used by DOJ to determine whether it wants to intervene in the case.

⁴⁵⁸ 31 U.S.C.S. § 3730(c)(3) (LEXIS 2005).

⁴⁵⁹ *Ridenhour v. KaiserHill Co., LLC*, 397 F.3d 925, 935 (10th Cir. 2005).

⁴⁶⁰ *See Swift v. United States*, 318 F.3d 250 (D.C. Cir. 2003).

⁴⁶¹ *Ridenhour*, 397 F.3d at 936 (citing *Sequoia v. Baird-Neece*, 151 F.3d 1139 (9th Cir. 1998)).

⁴⁶² *Id.*

⁴⁶³ *Id.* at 936-37.

⁴⁶⁴ *United States ex rel Alva Bettis v. Oderbrecht Contractors of California, Inc.*, 393 F.3d 1321 (D.C. Cir. 2005). Note, generally, that fraud in the inducement as a form of procurement fraud is a judicial creation gleaned from the legislative history of the 1986 amendments to the FCA. Specifically, Congress noted that under FCA case law "each and every claim submitted under a contract, loan guarantee, or other agreement which was originally obtained by means of false statements or other corrupt or fraudulent conduct, or in violation of any statute or applicable regulation, constitutes a false claim." S. Rep. No. 99-345, at 9 (1986), *reprinted in* 1986 U.S.C.A.N. 5266, 5274.

⁴⁶⁵ *Oderbrecht Contractors of California, Inc.*, 393 F.3d. at 1326 (citing *United States ex rel. Harrison v. Westinghouse Savannah River Co.*, 176 F.3d 776, 787-88 (4th Cir. 1999) (surveying the case law on fraud in the inducement FCA liability)).

⁴⁶⁶ *Id.* at 1327.

⁴⁶⁷ *Id.*

However, the Tenth Circuit Court of Appeals in this case did not address the issue raised by the lower court, instead holding that “on the evidence of this case, no reasonable jury could find that [defendant] fraudulently induced the [contract].”⁴⁶⁸

The (Continuing) Sad Saga of Darlene Druyun

Last year’s *Year in Review* reported on the sad saga of Darlene Druyun, the former Principal Deputy Assistant Secretary of the Air Force for Acquisition and Management.⁴⁶⁹ FY 2005 witnessed significant fall-out from Ms. Druyun’s case to include the criminal conviction of a senior Boeing executive and the GAO sustaining two major protests against the Air Force.

While many in the contracting community are well aware of the Druyun saga by now, it is important to first recap the Druyun case for those who are not yet familiar with her misdeeds. On 1 October 2004, Ms. Druyun was sentenced by a federal judge after earlier pleading guilty to one felony count of conspiracy in connection with her discussions with Boeing concerning potential employment with Boeing following her retirement from the Air Force.⁴⁷⁰ Ms. Druyun was sentenced to nine months in prison, seven months of community confinement, one hundred fifty hours of community service, and a fine of \$5,000.⁴⁷¹ Following her plea, but before her sentencing, Ms. Druyun admitted she provided “favors” to Boeing on several matters in her last several years with the Air Force.⁴⁷² Ms. Druyun admitted that she favored Boeing in certain negotiations as a result of her employment negotiations and other benefits provided to her by Boeing. Ms. Druyun acknowledged that Boeing’s employment of her future son-in-law and her daughter in 2000, at the defendant’s request, along with the defendant’s desire to be employed by Boeing, influenced her government decisions in several matters affecting Boeing.⁴⁷³

⁴⁶⁸ *Id.* at 1328.

⁴⁶⁹ *2004 Year in Review*, *supra* note 88, at 159.

⁴⁷⁰ Supplemental Statement of Facts, the Defendant’s Post Plea Admissions, *U.S. v. Darlene Druyun*, U.S. District Court for the Eastern District of Virginia, Criminal No. 04-150-A, at <http://www.pogo.org/m/cp/cp-druyun-postpleaadmission-2004.pdf> (last visited 6 Oct. 2005) [hereinafter Supplemental Statement of Facts].

⁴⁷¹ *Procurement Integrity: Ex-USAF Official Druyun Admits Boeing Offers of Job Influenced Her, Draws 9 Months in Jail*, BNA FED. CONT. DAILY (Oct. 4, 2004). Ms. Druyun completed her sentence and was released from prison in Marianna County, Florida, on 30 Sept. 2005. Kimberly Palmer, *Former Air Force Acquisition Official Released from Jail*, GOVEXEC.com Daily Briefing, 3 October 2005 (on file with the author).

⁴⁷² *Id.*

⁴⁷³ As a result of the loss of her objectivity, Ms. Druyun admitted that she took actions which harmed the United States to include the following:

1. In negotiations with Boeing concerning the lease agreement for 100 Boeing KC 767A tanker aircraft, she agreed to a higher price for the aircraft than she believed was appropriate. She did so, in her view, as a “parting gift to Boeing” and because of her desire to ingratiate herself with Boeing, her future employer. She also acknowledges providing to Boeing during the negotiations what at the time she considered to be proprietary pricing data supplied by another aircraft manufacturer.
2. During 2002 she, as chairperson of the NATO Airborne Early Warning and Control Program Management Board of Directors, was involved in negotiations with Boeing concerning a restructuring of the NATO AWACS program. She negotiated a payment of 100 million dollars to Boeing as part of that restructuring. She acknowledges that at the time she believed a lower amount to be an appropriate settlement and she did not act in the best interest of the United States and NATO.
3. As the selection authority in 2001 for the C-130 AMP which was an Air Force procurement of more than four billion dollars to upgrade the avionics of C-130 aircraft, she selected Boeing from four competitors, and now acknowledges that an objective selection authority may not have selected Boeing.
4. During 2000, she negotiated a settlement with Boeing concerning the C-17 H22 contract clause with a senior executive of Boeing. These negotiations occurred at the time she was seeking employment at Boeing for her daughter’s boyfriend. Her decision to agree to a payment of approximately 412 million dollars to Boeing in connection with the C-17 H22 clause was influenced by Boeing’s assistance to her.

Supplemental Statement of Facts, *supra* note 470.

The fallout from the Druyun case has been massive. First, and most significantly, in February 2005, the GAO sustained a series of bid protests on two major contract actions during which Ms. Druyun participated as either an advisor or source selection authority. The first sustained protest related to contracts for the Air Force's small diameter bomb (SDB) program.⁴⁷⁴ The SDB program "contemplated development of a 'miniature munition' weapon system to provide fighter and bomber aircraft with air-to-surface capabilities to attack 'fixed and mobile/relocatable targets.'"⁴⁷⁵ During the evaluation phase, the Air Force deleted one evaluation factor for which Lockheed Martin was already identified as being particularly strong.⁴⁷⁶ The Air Force argued that it deleted this evaluation factor because it was related to a requirement (moving targets) that the Air Force decided to delete from the procurement due to budget constraints.⁴⁷⁷

The GAO noted, however, that just after awarding the contract to Boeing, the "Air Force discovered that 'surplus funding may exist' that would facilitate reinstatement of the [moving target] requirement."⁴⁷⁸ The GAO found that Ms. Druyun was involved in the discussions that culminated in favor of Boeing; was involved in the decision to delete the moving target requirement; had performed in much the same source selection authority (SSA) role in this decision as she had previously held before allegedly being replaced as the SSA; and acknowledged bias in favor of the ultimate awardee.⁴⁷⁹ In this decision sustaining the protest, the GAO held that where a "a procurement official was biased in favor of one offeror, ... the need to preserve the integrity of the procurement process requires that the agency demonstrate [by compelling evidence] that the protester was not prejudiced by the procurement official's bias."⁴⁸⁰

The second major group of protests sustained by the GAO was related to the Air Force's award to The Boeing Company of various contracts, totaling approximately four billion dollars, for the avionics modernization upgrade program for the C-130 aircraft.⁴⁸¹ On much the same grounds as they used to sustain the SDB protests discussed above, the GAO sustained this series of protests as well stating that where "the record establishes that a procurement official was biased in favor of one offeror, our Office believes that the need to preserve the integrity of the procurement process requires that the agency demonstrate that the protester was not prejudiced by the procurement official's bias in order for us to deny the protest."⁴⁸² The GAO required that the agency provide "compelling evidence that the protester was not prejudiced."⁴⁸³ Because the Air Force could not satisfy this burden, the GAO sustained the protests.⁴⁸⁴

Just prior to the GAO releasing their decisions on the SDB and C-130 cases, Mr. Michael Wynne, acting Under Secretary of Defense for Acquisition, Technology, and Logistics, announced that he asked the DOD Inspector General (IG) to review eight additional contracts that were "under the decision-making purview" of Darlene Druyun.⁴⁸⁵ The eight cases referred to the DOD IG, worth a total of approximately three billion dollars, had been flagged by the Defense Contract Management Agency which had conducted a sweeping review of significant Air Force procurements and identified these eight as ones which appeared "to have anomalies in them which warrant further review."⁴⁸⁶ To date the DOD IG has not

⁴⁷⁴ Lockheed Martin Corp., B-295402, Feb. 18, 2005, 2005 CPD ¶ 24.

⁴⁷⁵ *Id.* at 1 n.1.

⁴⁷⁶ *Id.* at 6.

⁴⁷⁷ *Id.* at 6 n.12.

⁴⁷⁸ *Id.* at 7.

⁴⁷⁹ *Id.* at 11.

⁴⁸⁰ *Id.* at 14. Because much of the work was already completed on Phase I of the contract, GAO recommended that only Phase II be recompeted and that Lockheed be awarded attorney's fees for the protest. The GAO delayed a decision on whether Lockheed would receive reimbursement for their bid and proposal costs until the Air Force looked into some additional matters. *Id.*

⁴⁸¹ Matter of Lockheed Martin Aeronautics Co.; L-3 Comm'n Integrated Sys. L.P.; BAE Sys. Integrated Def. Solutions, Inc., Comp. Gen., B-295401, et al., Feb. 24, 2005, 2005 CPD ¶ 41, at 14 (discussed *supra* at section titled Competition at page 7).

⁴⁸² *Id.*

⁴⁸³ *Id.* at 7.

⁴⁸⁴ *Id.* at 14. Because of much of the work was complete on these contracts, the GAO recommended that the Air Force recompete certain portions of the contracts, review others to see if they could be recompeted, and pay the protesters attorneys fees for the protest as well as bid and proposal costs for any portion of the contracts that can not be recompeted. *Id.*

⁴⁸⁵ DOD Refers Contracts to IG Investigators, http://www.defenselink.mil/news/Feb2005/n02142005_2005021407.html (last visited Oct. 15, 2005).

⁴⁸⁶ DOD Refers Contracts to IG Investigators, http://www.defenselink.mil/news/Feb2005/n02142005_2005021407.html (last visited Oct. 15, 2005). The specific cases referred were the National Polar-orbiting Operational Environmental Satellite System—Conical Microwave Imager Sensor; C-5 Avionics Modernization Program; Financial Information Resource System; C-22 Replacement Program; 60K Tunner Program Contractor Logistics; KC-135 Programmed Depot Maintenance; F-16 Mission Training Center; and the C-40 Lease and Purchase Program. *Id.*

completed their investigation into the eight contracts. If the DOD IG finds improprieties, Mr. Wynne intends to ask the adversely affected contractors to file protests with the GAO, so stay tuned for more “Druyun protests” next year.⁴⁸⁷

If You Can't Do the Time, Don't Do the Crime

In addition to the extensive GAO protest actions in response to Ms. Druyun's conviction, FY 2005 also saw the Department of Justice (DOJ) bring a criminal case against Michael Sears, the former Boeing Chief Financial Officer.⁴⁸⁸ As a DOJ news release stated, “Mr. Sears pled guilty on November 15, 2004, to aiding and abetting acts affecting a personal financial interest. From September 23, 2002, through November 5, 2002, Sears aided and abetted Darleen Druyun, then the Principal Deputy Assistant Secretary of the Air Force for Acquisition and Management, in negotiating employment with Boeing while she was participating personally and substantially as an Air Force official overseeing the negotiation of a \$20 billion lease of 100 Boeing KC 767A tanker aircraft.”⁴⁸⁹

Mr. Sears troubled involvement with Ms. Druyun apparently started when he was contacted in September 2002 by Darleen Druyun's daughter, herself a Boeing employee.⁴⁹⁰ The release added, “In a series of e-mails to Sears, the daughter outlined her mother's intention to retire from the Air Force and the type of position her mother would accept after retirement. Druyun discussed these E-mails with the daughter, who relayed Druyun's interest in Boeing employment in a meeting with Sears.”

These e-mails and discussions between Mr. Sears and Ms. Druyun's daughter led to a private meeting between Mr. Sears and Ms. Druyun at the Orlando Airport on 17 October 2002.⁴⁹¹ As the release stated, “Druyun advised Sears at that meeting that she had not disqualified herself from matters involving Boeing and therefore they should not be discussing her possible employment by the Boeing Company,” but Mr. Sears continued with the employment negotiations knowing that their actions created a conflict of interest and then also “discussed issues concerning a major Air Force procurement which Boeing participated in as a subcontractor.”⁴⁹²

Mr. Sears was sentenced on 18 February 2005, to four months incarceration, a fine of \$250,000 and two hundred hours of community service.⁴⁹³ Mr. McNulty said, “Mr. Sears had a clear choice. Instead of respecting the integrity of the government's procurement system, he chose the financial interests of his company over the best interest for America.”⁴⁹⁴

*Well, We're Moving on Up, . . . to the [Top . . .]*⁴⁹⁵

While Mr. Sears and Ms. Druyun, as well as the Air Force and The Boeing Company, took substantial heat for their transgressions on various contracts, the DOD IG released a report in June in which they spread the blame for at least one of the Boeing-Druyun cases, the KC-767A tanker lease program, far wider than just to Ms. Druyun.⁴⁹⁶ The report found that Mr. Aldridge, Under Secretary of Defense for Acquisition, Technology, and Logistics; Mr. Wynne, Acting Under Secretary of Defense for Acquisition, Technology, and Logistics; Dr. James Roche, Secretary of the Air Force; Dr. Sambur, Assistant Secretary of the Air Force for Acquisition; Ms. Druyun; Principal Deputy Assistant Secretary of the Air Force (Acquisition

⁴⁸⁷ See *GAO Sustains Lockheed's Druyun Protest; DOD Refers Eight More Contracts to IG*, 47 GOV'T CONTRACTOR 8, ¶88 (Feb. 23, 2005).

⁴⁸⁸ News Release, U.S. Department of Justice, United States Attorney for the Eastern District of Virginia (Feb. 18, 2005), available at <http://www.DODig.osd.mil/IGinformation/IGInformationReleases/SearsSent021805.pdf>.

⁴⁸⁹ *Id.*

⁴⁹⁰ *Id.*

⁴⁹¹ *Id.*

⁴⁹² *Id.*

⁴⁹³ *Id.*

⁴⁹⁴ *Id.*

⁴⁹⁵ Theme Song, *The Jeffersons* (Columbia Tri-Star, 1975-85).

⁴⁹⁶ U.S. OFF. OF THE INSPECTOR GEN. OF THE DEP'T OF DEF., REP. NO. OIG-2004-171, MANAGEMENT ACCOUNTABILITY REVIEW OF THE KC-767A TANKER PROGRAM (13 May 2005), available at www.DODig.mil/tanker.htm.

and Management); Major General Essex, Director of Global Reach Programs; General Jumper, Air Force Chief of Staff, and various Air Force attorneys involved in the review process were all accountable for mistakes they made in the KC-767A tanker lease procurement process.⁴⁹⁷

The report, concluding that these officials did not comply in certain respects with DOD Directives and guidance, OMB Circulars, or the FAR, was issued to the Secretary of Defense Rumsfeld in May for his review and consideration, and certainly sheds some very interesting light on the acquisition processes taking place at the highest levels of our government.⁴⁹⁸

*Welcome Back, . . . to that Same Old Place that You Laughed About*⁴⁹⁹

Interestingly over the past year, despite a series of recent transgressions, The Boeing Corporation has apparently made a stunning comeback and managed to work their way back into the (moderately) good graces of the United States government. As reported in the 2003 Year in Review, the Air Force suspended Boeing Integrated System business units on 24 July 2003 for committing serious violations of the law with regard to the Evolved Expendable Launch Vehicle Contract (EELV).⁵⁰⁰ However, as reported last year, the Air Force waived the suspension of these Boeing units on two separate occasions and awarded two separate space launches to Boeing.⁵⁰¹ On 4 March 2004, the Air Force lifted the twenty month suspension of Boeing's satellite launch business clearing the way for Boeing to again compete for rocket launch contracts.⁵⁰² To help the Air Force reach their decision to lift the suspension, Boeing agreed to reimburse the Air Force for the costs incurred investigating Boeing (\$1.9 million).⁵⁰³

At the time the suspension was lifted, Mr. Peter Teets, the Acting Secretary of the Air Force, said that he hoped "that everyone who does business with the Air Force takes note of this case and is reminded that we tackle ethical breaches very seriously and will not hesitate to impose significant sanctions when necessary."⁵⁰⁴ Time will tell if Mr. Teets' hopes are realized or whether the Air Force's willingness to waive the suspension for significant contracts and ultimately restore the relevant Boeing units to the launch competitions is viewed more as a 'slap on the wrist.'

One thing is clear; Boeing has wasted little time getting back in the game. In May of this year, Boeing and Lockheed Martin announced that they entered a joint venture to produce the Air Force's EELV rocket.⁵⁰⁵ The joint venture, called United Launch Alliance, intends to reduce launch costs for future rocket launches by the DOD and NASA.⁵⁰⁶ This joint venture may very well end any legitimate competition in the rocket launch arena, and both companies agreed to seek an order in federal district court suspending the litigation between and dismissing their claims related to the EELV launches.⁵⁰⁷ Although both companies maintain that their respective versions of the EELV will remain available as alternatives for individual launch missions, the regulatory approval process will undoubtedly give this joint venture serious scrutiny. The consolidation of major defense contractors generally, and the rocket launch contractors specifically, has resulted in less than ideal competition problems and has hampered the use of suspension and debarment process as a deterrent.⁵⁰⁸

Boeing seems intent on concluding all their ongoing litigation related to their recent transgressions with regard to Ms. Druyun and the Lockheed Martin cases. In September, it was reported that the DOJ and Boeing are negotiating a

⁴⁹⁷ *Id.* at 32-46.

⁴⁹⁸ *Id.* at i.

⁴⁹⁹ Theme Song, *Welcome Back Kotter* (The Konack Co., Inc., 1975-79).

⁵⁰⁰ See 2003 Year in Review, *supra* note 367, at 173.

⁵⁰¹ *Id.* at 174 n. 2331.

⁵⁰² Renae Merle, *Boeing Cleared to Bid on Launches*, WASH. POST, Mar. 5, 2005, at E1.

⁵⁰³ *Id.*

⁵⁰⁴ *Id.*

⁵⁰⁵ *Boeing and Lockheed Team on EELV*, 47 GOV'T CONTRACTOR 20, ¶ 234 (May 18, 2005).

⁵⁰⁶ *Id.*

⁵⁰⁷ *Id.*

⁵⁰⁸ For an interesting article discussing these issues, including a case study on the Boeing EELV suspension, see generally, Jennifer S. Zucker, *The Boeing Suspension: Has Increased Consolidation Tied the Department of Defense's Hands?*, ARMY LAW, Apr. 2004, at 14.

settlement in which Boeing would pay up to \$500 million to the United States government, but would avoid prosecution in two federal probes related to illegally acquiring Lockheed Martin's proprietary data related to the EELV contracts and the illegal recruitment of Ms. Druyun.⁵⁰⁹ Based on these broad outlines, such a settlement would "entail the stiffest financial penalties ever imposed on a U.S. defense contractor for alleged procurement violations."⁵¹⁰ The settlement is apparently being pushed by Boeing's recently installed Chief Executive Officer who would undoubtedly like to move past its recent troubles and focus on the future.⁵¹¹

Qui Tam Settlements Are All the Rage, Too

This year saw several significant FCA settlements highlighted by two cases that were initiated as *qui tam* suits. In one of the largest False Claims settlements ever negotiated with a defense contractor, Northrop Grumman Corporation and the DOJ settled a fifteen-year-old civil lawsuit that was scheduled to go to trial in March.⁵¹² Northrop Grumman agreed to pay \$62 million to resolve allegations originally brought as a *qui tam* action back in 1989 that Northrop Grumman "overcharged the government by fraudulently accounting for materials purportedly used in multiple defense contracts and by fraudulently inflating the cost and misrepresenting the progress of a radar jamming device for the B-2 'Stealth' Bomber."⁵¹³ The settlement called for the government to pay \$12.4 million to the two former Northrop Grumman employees who first alerted the government to the alleged fraud.⁵¹⁴

In a second large settlement, PricewaterhouseCoopers LLP (PWC) agreed to pay the government \$41.9 million "to resolve allegations that it made false claims to the United States in connection with travel reimbursements under contracts it had with several federal agencies."⁵¹⁵ The settlement resulted from an investigation by a multi-agency joint taskforce "which confirmed allegations that PWC received rebates for its federally-financed travel expenses from its various travel and credit card companies, airlines hotels, rental car agencies, and travel service providers and, despite a duty to do so," did not reduce its travel reimbursement claims filed with the government.⁵¹⁶ The claim was originally brought under the *qui tam* provisions of the False Claims Act.⁵¹⁷

⁵⁰⁹ Andy Pasztor & Anne Marie Squeo, *Boeing Could Avoid Prosecution, Pay Up to \$500 Million to U.S.*, WALL ST. J, Sept. 9, 2005, at A1.

⁵¹⁰ *Id.*

⁵¹¹ *Id.*

⁵¹² Press Release, U.S. Dep't of Justice, United States Attorney for the Northern District of Illinois, Northrop Grumman to Pay U.S. \$62 Million to Settle Alleged Accounting Overcharges and False Claims about Radar Jamming Device for B-2 "Stealth" Bomber, (Mar. 1, 2005), *available at* http://www.dodig.osd.mil/IGInformation/IGInformationReleases/Northrop_030105B2.pdf.

⁵¹³ *Id.*

⁵¹⁴ *Id.*

⁵¹⁵ Press Release, United States Agency for International Development, PriceWaterhouseCoopers to Pay \$41.9 Million to Settle False Claims Regarding Travel Reimbursements (July 22, 2005), *available at* <http://www/isaod/gov/press/releases/2005/pr050722.html>.

⁵¹⁶ *Id.*

⁵¹⁷ *Id.*

Following the sentencing in Mr. Sears's case, discussed above, Paul J. McNulty, the U.S., Attorney for the Eastern District of Virginia, announced a broad initiative to combat procurement fraud.⁵¹⁸ The U.S. Attorney's Office created a Procurement Fraud Working Group to strengthen the integrity of the procurement system by focusing on "the early detection and prevention of procurement fraud associated with the increase in contracting activity for national security programs."⁵¹⁹ The Procurement Fraud Working Group will include representatives from the Federal Bureau of Investigations, the Defense Criminal Investigations Service, the Naval Criminal Investigations Service, the National Reconnaissance Office, the DOD IG, the Department of Homeland Security and will "facilitate the exchange of information among participant agencies and assist them in developing new strategies to prevent and to promote early detection of procurement fraud."⁵²⁰ The goal of the group is to "promote collaboration and exchange of ideas to increase effectiveness in this vital area of law enforcement" by improving the training of special agents, auditors, contracting officers and program managers and to provide "increased collaboration between field agents and government contractors to educate them on effect means for preventing waste, fraud, and abuse."⁵²¹

Another One Bites the Dust: COL Moran's Target Employer Convicted

Last year's edition of *The Year in Review* chronicled the sordid details of the bribery and corruption scandal that Colonel Richard Moran, the former Commander, U.S. Army Contracting Command, Korea (USACC-K), engaged in during his time in Korea.⁵²² As that article discussed, Colonel Moran and his wife were ultimately convicted in federal court and Colonel Moran was sentenced to fifty-four months in prison.⁵²³ On 25 July 2005, two executives of Information Systems Support, Inc. (ISS), a Maryland based military contractor, pleaded guilty to conflict of interest charges relating to illegal job negotiations with a Colonel Moran.⁵²⁴ Young Lee and Lorn MacUmbur each pled guilty to one count of aiding and abetting a conflict of interest involving Colonel Moran.⁵²⁵ ISS offered Moran post-retirement employment and Moran had accepted their offer on 7 January 2002.⁵²⁶ As commander USACC-K, Colonel Moran accepted numerous dinners and special favors from ISS and directed that numerous contracts be awarded to ISS. Colonel Moran ultimately never went to work for ISS because he was arrested nine days after he accepted the employment offer.

Major Michael S. Devine

Taxation

Must Uncle Sam Reimburse Your Personal Tax Liability? Maybe –If You're a Subchapter S Corporation

Buoyed by its victory in an earlier COFC decision⁵²⁷ which determined that state income taxes paid by the Subchapter S corporation's⁵²⁸ sole shareholder were reimbursable expenses under the corporation's various cost-reimbursement contracts, Information Systems & Networks Corporation (ISN) sought to extend that ruling to its negotiated

⁵¹⁸ News Release, U.S. Department of Justice, United States Attorney, Eastern District of Virginia, Combating Procurement Fraud: An Initiative to Increase Prevention and Prosecution of Fraud in the Federal Procurement Process (Feb. 18, 2005), available at <http://www.dodig.osd.mil/IGInformation/IGInformationReleases/SearsSent021805.pdf>.

⁵¹⁹ *Id.*

⁵²⁰ *Id.* at 3.

⁵²¹ *Id.* at 1.

⁵²² *2004 Year in Review*, *supra* note 88, at 174.

⁵²³ *Id.* at 175.

⁵²⁴ Press Release, U.S. Department of Justice, United States Attorney for the District of Maryland, Two Military Contractor Executives Plead Guilty to Conflict of Interest Charges Relating to Job Negotiations with Army Contract Officer (July 25, 2005) (on file with author).

⁵²⁵ *Id.*

⁵²⁶ *Id.* at 4.

⁵²⁷ *Info. Sys. & Networks Corp. (ISN I) v. United States*, 48 Fed. Cl. 265 (2000), *later proceeding at*, *Info. Sys. & Networks Corp. (ISN II) v. United States*, 64 Fed. Cl. 599 (2005). See *supra* section titled Contract Types at page 20 for an additional discussion of this case.

⁵²⁸ Subchapter S corporations are so called because they are organized under Subchapter S of the Internal Revenue Code, 26 U.S.C. §§ 1361-1379. They are typically small businesses, closely held by no more than 75 shareholders, and often by a sole shareholder.

fixed-price contracts as well.⁵²⁹ ISN also demanded lost profits on its cost-reimbursement contracts, based on the contracting officer's failure to classify state tax costs as reimbursable expenses.

In the earlier case, the Court had recognized that, as a Subchapter S corporation, ISN's income tax liability is "passed through" to its sole shareholder⁵³⁰ and held that state income taxes paid by the shareholder are allowed under the Taxes provision.⁵³¹

However, when ISN returned to Court to seek the same result for its fixed-price contracts, the Court easily dismissed its claim, pointing out the fundamental difference between cost-reimbursement and fixed-price contracts, with the contractor being responsible under the latter for all costs and resulting profit and loss. Additionally, the Court found ISN was not entitled to any "lost profits" under its cost-reimbursement contracts based on its claim that its negotiated fixed-fee for those contracts should have been greater because the costs should have included the state tax costs (which the earlier decision found to be reimbursable). The Court held that to do so would violate the prohibition against cost-plus-percentage-of-cost contracts⁵³² and would lead to a windfall.⁵³³

Note the breathtaking implications if in the future this decision is extended beyond Subchapter S corporations, to include other business arrangements, such as partnerships, individual proprietorships, or limited liability corporations where there are pass-throughs of tax liability.

Another Subchapter S Corporation Tries to Follow in Footsteps

In *Environmental Chemical Corporation*,⁵³⁴ the board had an opportunity to address the issue of whether state income taxes paid by shareholders of a Subchapter S corporation⁵³⁵ are allowable as general and administrative (G&A) expenses. DCAA had disallowed these expenses, deeming them to be a personal expense of the shareholders and not allocable in accordance with FAR 31.201-4.⁵³⁶ After *Environmental Chemical Corporation* (ECC) submitted a certified claim requesting a contracting officer's final decision on the allowability and allocability of these taxes, the contracting officer denied the claim on the basis that exemptions from these taxes were available to ECC under State law. That is, the various states in which ECC does business exempt Subchapter S corporations from state income tax.

On appeal to the board, ECC filed a motion for summary judgment, urging the Board to adopt the rationale of the COFC in the first *Information Systems* case⁵³⁷ that these taxes were not exempt for the purposes of FAR 31.205-41,⁵³⁸ but

⁵²⁹ *ISN II*, *supra* note 527.

⁵³⁰ *ISN I*, *supra* note 527, at 266.

⁵³¹ FAR 31.205-41, which provides that certain federal, state, and local taxes are allowable if they are required to be and are paid or accrued in accordance with generally accepted accounting principles. FAR, *supra* note 271, at 31.205-41.

⁵³² See 10 U.S.C.S. § 2306 (LEXIS 2005).

⁵³³ *ISN I*, *supra* note 527, at 609.

⁵³⁴ ASBCA No. 54141, 2005 ASBCA LEXIS 32 (Apr. 13, 2005).

⁵³⁵ *Black's Law Dictionary* describes a Subchapter S corporation as a corporation whose income is taxed through its shareholders rather than through the corporation itself. BLACK'S LAW DICTIONARY 344 (7th ed. 1999).

⁵³⁶ FAR, *supra* note 274, at 31.201-4. The section, titled Determining Allocability, states:

A cost is allocable if it is assignable or chargeable to one or more cost objectives on the basis of relative benefits received or other equitable relationship. Subject to the foregoing, a cost is allocable to a Government contract if it-

- (a) Is incurred specifically for the contract;
- (b) Benefits both the contract and other work, and can be distributed to them in reasonable proportion to the benefits received; or
- (c) Is necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown.

Id.

⁵³⁷ *ISN I*, *supra* note 527.

⁵³⁸ FAR, *supra* note 274, at 31.205-41. The section provides in pertinent part:

- (b) The following types of costs are not allowable:

rather than the State exemption results not in an absence of payment of the tax, but a transfer of liability for the tax to the individual shareholders. Not convinced it should follow that rationale, and finding there were unresolved factual issues, the board denied ECC's motion for summary judgment.

Be Aware of Exemptions from Foreign Taxation

Effective 30 September 2005, the DFARS was amended to implement a statutory prohibition on foreign taxation of commodities acquired under contracts funded with U.S. assistance.⁵³⁹ The underlying statutory prohibition is contained in annual legislation, and requires that a bilateral agreement providing for U.S. assistance to a foreign country must specify that the U.S. assistance will be exempt from value added taxes and customs duties.⁵⁴⁰ The added DFARS language⁵⁴¹ requires prompt notification to appropriate parties if a foreign government imposes such taxes, so that corrective action can be taken.

Ms. Margaret K. Patterson

Government Furnished Property

Tag, You're It!

Recent changes to the FAR have placed more responsibility on contracting officers to use their judgment to determine the best course of business in dealing with government furnished property.⁵⁴² In September of 2005, the DOD, the GSA, and National Aeronautics and Space Administration proposed sweeping changes to the rules for use of government property.⁵⁴³ The proposed changes simplify complicated language and reduce recordkeeping and management requirements. The changes follow up on a change issued in July, and reflect current thinking in the procurement arena: sound business practice is required.⁵⁴⁴ As part of the aim toward sound business practice, the changes incorporated streamlining of the procedures for using government furnished property. To that end, the proposed change deletes clauses that are obsolete, duplicative, or unclear.⁵⁴⁵

Some of the more significant changes are associated with the requirement for "contracting officers, property administrators and other personnel involved in awarding or administering contracts with Government property to be aware of industry-leading practices and standards for managing Government property," as follows:

- (a) Stricter policy for contracting officers to follow when determining whether or not to provide property to contractors.

-
- ...
- (3) Taxes from which exemptions are available to the contractor directly. . . .

The term "exemption" means freedom from taxation in whole or in part and includes a tax abatement or reduction resulting from mode of assessment, method of calculation, or otherwise.

Id.

⁵³⁹ The affected contracts will primarily be Foreign Military Sales contracts. Defense Federal Acquisition Supplement; Prohibition of Foreign Taxation on U.S. Assistance Programs, 70 Fed. Reg. 57,191 (interim rule Sept. 30, 2005). The affected contracts will primarily be Foreign Military Sales contracts.

⁵⁴⁰ Omnibus Appropriations Act, 2003, Pub. L. No. 108-7, div. E, § 579 (2003); Consolidated Appropriations Act, 2004, Pub. L. No. 108-199, div. D, § 506 (2004); Consolidated Appropriations Act, 2005, Pub. L. No. 108-447, div. D, § 506 (2004).

⁵⁴¹ See DFARS, *supra* note 347, at 229.170 through 229.170-4, and 252.229-7011.

⁵⁴² See, e.g., Federal Acquisition Regulation; Interim Rules and Final Rules, 70 Fed. Reg. 143, 43,576 (July 27, 2005) (to be codified at 48 C.F.R. Chapter 1, pts. 2, 4, 8, 14 et al.) [hereinafter July FAR change]. FAR Parts 45 and 52 were amended in July, 2005, in part, to "clarify the basis for determining rental charges for the use of Government property. . . . [The changes were] intended to promote the dual use of [government property], [and] will impact contracting officers and property administrators responsible for the management of Government property and contractors that desire to use Government property for commercial purposes." *Id.*

⁵⁴³ Federal Acquisition Regulation; Government Property, 70 Fed. Reg. 180, 54,878 (Sept. 19, 2005) (to be codified at 48 C.F.R. pts. 1, 2, 17, 31, 32, 35, 42, 45, 49, 51, 52 and 53).

⁵⁴⁴ July FAR change, *supra* note 542.

⁵⁴⁵ *Id.* at 54,880.

- (b) Possible contracting officer revocation of the Government's assumption of risk when the property administrator determines the contractor's property management practices are inadequate and/or present an undue risk to the Government.
- (c) An outcome-based framework for the management of property in the possession of contractors.
- (d) Identification by contractors of the standard or practice proposed for managing Government property.⁵⁴⁶

The GAO is clearly interested in accounting for government property, whether it is property under a contract, used by the DOD, or excess.⁵⁴⁷ Management controls are often cited as the reason for waste and inefficiency in dealing with government property.⁵⁴⁸ This proposed FAR change will require contracting officers to take the initiative to determine the best "business-savvy" way to provide contractors with government property to avoid such waste and inefficiency.

Major Jennifer C. Santiago

Contract Pricing

Stickin' it to the Fisc

In *Viacom, Inc. v. General Services Administration*,⁵⁴⁹ the General Services Administration Board of Contract Appeals (GSBCA) examined a defective pricing claim and held, among other things, that the proper time for determining when a contractor may have failed to provide accurate cost and pricing data is the point at which negotiations are concluded.⁵⁵⁰ In a rather animated opinion, the GSBCA also held that where the agency cannot provide proper documentary evidence that a contractor failed to provide accurate pricing data, the agency will not prevail.⁵⁵¹

In 1985, the GSA awarded a multiple award schedule contract to Westinghouse Furniture Systems ("Westinghouse") for various office furniture that lasted for three years.⁵⁵² In 1998, the GSA's Office of the Inspector General "issued an audit report concluding that Westinghouse had engaged in defective pricing."⁵⁵³ In 2002, the contracting officer issued a decision on the report, "concluding that there was due a defective pricing refund of \$3,804,316 and a refund due to incorrect payment terms of \$4191 for a total of \$3,808,316."⁵⁵⁴ The GSA's claim "is based on the assumption that Westinghouse did not disclose the full range of discounts it had given to its non-governmental (commercial) customer as shown on numerous invoices to those customers."⁵⁵⁵

Viacom, Inc., the successor in interest to Westinghouse, appealed the decision to the GSBCA. The GSBCA granted the appeal in substantial part because the "[GSA] has failed to meet the burden of proof the law requires to establish a defective pricing claim. The reasons for [GSA's] failure--and our conclusion that follows from that failure--are disparate and numerous."⁵⁵⁶

The Board held that since the contract "contained the [d]efective pricing clause usually found in contracts subject to the Truth in Negotiations Act (TINA)," it would rely on cases arising under TINA that involved defective pricing in

⁵⁴⁶ *Id.* at 54,879.

⁵⁴⁷ See, e.g., U.S. GOV. ACCOUNTABILITY OFF., REP. NO. GAO-05-15, DEFENSE INVENTORY: IMPROVEMENTS NEEDED IN DOD'S IMPLEMENTATION OF ITS LONG-TERM STRATEGY FOR TOTAL ASSET VISIBILITY OF ITS INVENTORY (Dec. 2004).

⁵⁴⁸ See, e.g., U.S. GOV. ACCOUNTABILITY OFF., REP. NO. GAO-05-729T, DOD EXCESS PROPERTY: MANAGEMENT CONTROL BREAKDOWNS RESULT IN SUBSTANTIAL WASTE AND INEFFICIENCY (June 2005).

⁵⁴⁹ GSBCA No. 15871, 2005 GSBCA LEXIS 158 (Sept. 21, 2005).

⁵⁵⁰ *Id.* at *48.

⁵⁵¹ *Id.* at *2.

⁵⁵² *Id.* at *1.

⁵⁵³ *Id.* at * 2. "The audit report calculated a defective pricing refund of \$3,804,316, an end of contract discount refund of \$484,386, and a prompt payment discount of [\$4,191] for a total of \$4,292,893." *Id.*

⁵⁵⁴ *Id.*

⁵⁵⁵ *Id.*

⁵⁵⁶ *Id.*

analyzing the issues presented.⁵⁵⁷ In order for the government to establish a claim for defective pricing, it must prove by a preponderance of the evidence that “information was required to be disclosed, and that the government relied to its detriment on appellant’s disclosure of defective data.”⁵⁵⁸ Once the government proves that the information was not provided, or that the cost or pricing data provided was inaccurate, “the Government is aided in meeting its burden of establishing that there was a significant overstatement in the contract price by a rebuttable presumption that the natural and probable consequence of the non-disclosure or use of noncurrent or inaccurate cost or pricing data is an increase in the contract price.”⁵⁵⁹

Here, the GSA argued that the relevant transaction date for the submission of cost or pricing data was the date of contract award, and “vigorously argues for this proposition . . . maintaining that block 22 of the award document, signed by [Westinghouse], represents a certificate of completion of price negotiations.”⁵⁶⁰ The board succinctly stated that the government’s “assumption is wrong”⁵⁶¹ because the completion of price negotiations marks the relevant time for determining whether cost or pricing data is either not disclosed or in noncurrent or inaccurate, not contract award.⁵⁶² In this case, contract award was over six months after what the Board determined to be the point at which “price negotiations were concluded.”⁵⁶³ The GSA argued that Westinghouse had “discount data” which existed after price negotiations were concluded (as determined by the Board) and before contract award that should have been submitted to the GSA so that the contracting officer could have negotiated a lower price.⁵⁶⁴ The GSBCA summarily dismissed the argument, stating that data existing after price negotiations is simply not required to be disclosed.⁵⁶⁵

The board then proceeded to address the GSA’s argument that information about discounts when selling individual furniture components is relevant to answering the question of whether there was defective pricing when the contract did not require the provision of individual components, only full furniture systems.⁵⁶⁶ The Board held that “commercial discounts shown for individual components or groups of components, not proven to have constituted a systems furniture workstation identical or similar to a workstation offered under [the contract], are not pricing data that Westinghouse was required to disclose.”⁵⁶⁷

⁵⁵⁷ *Id.* at * 47 (citing 10 U.S.C. § 2606(f)). The Board noted that at contract award, the controlling statute:

provided that for prime contracts expected to exceed \$100,000 not awarded through sealed bid, with certain exceptions, the prime contractor was required to submit cost or pricing data and a certification of the data’s completeness and accuracy. 41 U.S.C. § 254(d)(1)(A)(1984). An exception to the requirement for submission of cost or pricing data applied when the contract price was based upon adequate price competition and established catalog or market prices of commercial items sold in substantial quantities to the general public. 41 U.S.C. § 254(d)(5)(i),(ii).

Id. The Board found that the exception cited in the statutory provision did not apply because the contract terms required that “offerors submit cost or pricing data and certify that the pricing data submitted with the offer were accurate, complete and current representations of actual transactions to the date when price negotiations were concluded. *Id.*

⁵⁵⁸ *Id.* (citing *Sylvania Elec. Prods. v. United States*, 479 F.2d 1342, 1349 (Ct. Cl. 1973); *United States v. United Techs. Corp.*, 51 F. Supp. 2d 167, 168 (D. Conn. 1999); *Gelco Space*, GSBCA 7916, 91-1 BCA ¶ 23,387 (1990); *Lockheed Martin Corp.*, ASBCA 50464, 02-1 BCA ¶ 31, 784, at 156,943.)

⁵⁵⁹ *Id.* at *48 (citing *United Techs. Corp.*, 51 F. Supp. 2d at 189).

⁵⁶⁰ *Id.*

⁵⁶¹ *Id.*

⁵⁶² Cost or pricing data is certified in a “Certificate of Current Cost or Pricing Data.”

⁵⁶³ *Id.* The Board provides ample support for its proposition:

The relevant cost or pricing data is that data in existence at the time of price negotiations. *McDonnell Aircraft Co.*, ASBCA 44504, 97-1 BCA ¶ 28,977 at 144,315 (contractor has no duty to supply accurate and complete subcontractor cost data after prime and subcontractor have reached agreement on price); *Aydin Monitor Systems*, NASA BCA 381-1, 8301 BCA ¶ 16,500 at 81,997 (1983), reconsideration granted on other grounds, 84-2 BCA ¶ 17, 297; see *United States v. General Dynamics Corp.*, 19 F.3d 770 (2d Cir. 1994); *Plessey Industries, Inc.*, ASBCA 16720, 74-1 BCA ¶ 10,603 at 50,277 (citing *Paceco, Inc.*, ASBCA 16458, 73-2 BCA ¶ 10,119 (data created between cost and pricing data certification and award date not cost or pricing data that was required to be submitted)(in TINA context, duty to disclose complete, accurate and current data extends only to the date of price negotiations).

Id. at 48-49.

⁵⁶⁴ *Id.* at 49.

⁵⁶⁵ *Id.*

⁵⁶⁶ *Id.* Note here that the contract specifically called for “complete workstations.”

⁵⁶⁷ *Id.* at 50.

The GSBICA, obviously frustrated with the GSA's failure to provide evidence to prove its claim against Westinghouse, ultimately concluded that "[t]he Government's claim of defective pricing is simply not salvageable by correction of error."⁵⁶⁸

Major Jennifer C. Santiago

Auditing

Special Inspector General Created in Iraq

There are many agencies performing audits in Iraq, to include the newly created Special Inspector General for Iraq Reconstruction (SIGIR).⁵⁶⁹ Among other things, the SIGIR provides reports to Congress quarterly on the progression of Iraqi reconstruction, in which the status of various audits occurring in Iraq are listed.⁵⁷⁰ In addition to the Congressional Reports, the SIGIR also releases audit memoranda, and in October, 2005, it released an audit examining the administration of the Commanders' Emergency Response Program (CERP) in Iraq.⁵⁷¹

At the request of the Deputy Secretary of Defense, the SIGIR's objective for the audit "was to evaluate the adequacy of controls over CERP funds."⁵⁷² Specifically, the SIGIR examined whether and to what extent managers of the CERP "obtained and documented required contracting officer's approval. . . [and to what extent they] expended funds in accordance with authorized project limits [and] effectively controlled the distribution of appropriated funds."⁵⁷³ The SIGIR "concluded that, while CERP appropriated funds were properly used for intended purposes, overall controls over CERP processes required improvement. Federal Acquisition Regulation and Department of Defense controls over the distribution of appropriated funds were not consistently followed and the required documents were not consistently used to maintain accountability of projects."⁵⁷⁴

Major Jennifer C. Santiago

Major Systems Acquisitions

Do Performance-Based Logistics Contracts Really Save Money?

In a report published in September 2005, the GAO found that the DOD cannot prove that it is saving money by engaging in performance-based logistics (PBL) contracts.⁵⁷⁵ GAO studied PBL contracts in the DOD to determine whether the DOD could provide evidence that PBL was a cost-effective measure.⁵⁷⁶ The report summarized the GAO's findings and

⁵⁶⁸ *Id.* at 54. The Board also briefly addressed two other issues: one, whether the contracting officer detrimentally relied on any defective data, and two, whether the defective pricing calculations were reasonable. On both, the Board held against GSA. The Board did, however, award the \$4,191 to the Government based on Westinghouse's failure to provide a two percent prompt payment discount.

⁵⁶⁹ Currently, there are six agencies performing audits, drafting reports, and providing testimony on Iraq reconstruction. In addition to the newly created Special Inspector General for Iraq Reconstruction (SIGIR), established audit agencies performing audits in Iraq are the U.S. Army Audit Agency; Department of Defense Office of Inspector General; Department of State Office of Inspector General; the GAO; and U.S. Agency for International Development Office of Inspector General. See SPECIAL INSPECTOR GENERAL FOR IRAQ RECONSTRUCTION, QUARTERLY REPORT TO CONGRESS, APP. J (July 30, 2005), available at http://www.sigir.mil/reports_congress.html.

⁵⁷⁰ *Id.*

⁵⁷¹ Memorandum, Special Inspector General for Iraq Reconstruction, to Deputy Secretary of Defense, subject: Management of Commanders' Emergency Response Program for Fiscal Year 2004 (Report No. SIGIR 05-014) (13 October 2005) (on file with the author).

⁵⁷² *Id.*

⁵⁷³ *Id.*

⁵⁷⁴ *Id.*

⁵⁷⁵ U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-05-966, DEFENSE MANAGEMENT: DOD NEEDS TO DEMONSTRATE THAT PERFORMANCE-BASED LOGISTICS CONTRACTS ARE ACHIEVING EXPECTED BENEFITS (Sept. 2005) (report to Subcommittee on Readiness, Committee on Armed Servs., U.S. Senate) [hereinafter GAO PBL CONTRACTS REPORT]. The GAO report defined performance-based logistics as "a variation of other contractor logistics support strategies and involves defining a level of performance that the weapons system is to achieve over a period of time at a fixed cost to the government." *Id.* at 1.

⁵⁷⁶ *Id.* at 2. Simply put, PBL is the DOD's typical model for long-term maintenance for major weapons systems. Before awarding a PBL contract, however, the agency should conduct an economic analysis determine whether such a contract would be cost-effective. *Id.* at 1.

recommendations after conducting a ten month-long study of fifteen of DOD's PBL programs.⁵⁷⁷ Some of the contracts the GAO studied included the Air Force's C-17, F-117, and the C-130J programs; the Navy's F-18 E/F FIRST program; and the Army's TOW-ITAS and HIMARS programs.⁵⁷⁸ In brief, the GAO found that in fourteen of the fifteen programs, the DOD failed to analyze whether such contracts actually resulted in cost savings.⁵⁷⁹

While the DOD formally encourages the use of PBL contracts for major weapons systems⁵⁸⁰ maintenance as a cost-savings measure, the DOD also recommends that individual program offices collect data regarding cost savings.⁵⁸¹ In November 2004, the Office of the Undersecretary of Defense issued a memorandum urging all DOD program managers to use the guidebook attached to the memorandum (PBL Guidebook) in implementing performance-based logistics contracts.⁵⁸² The PBL Guidebook advises program offices to methodically collect cost data for the purpose of evaluating whether it would be economically wise to enter into performance-based logistics contracts.⁵⁸³ The PBL Guidebook further advises that after entering into such contracts, program offices should continue collecting cost data so that they can evaluate whether the contracts have, in fact, resulted in cost savings.⁵⁸⁴

During the study, the GAO found that only one program office tracked cost data in accordance with the DOD guidance.⁵⁸⁵ In other cases, while some of the offices collected certain cost data, their efforts did not conform to the DOD PBL Guidebook.⁵⁸⁶ In four of the cases, the program offices had not collected any cost data.⁵⁸⁷ In some cases, program offices acknowledged that they obtained their cost data from the same contractors these offices were evaluating.⁵⁸⁸

The GAO concluded that the DOD should gather sufficient data to prove that PBL contracts actually result in cost savings.⁵⁸⁹ In order to provide this evidence, the GAO made two recommendations to the Secretary of Defense.⁵⁹⁰ First, the GAO recommended that the Secretary "reaffirm DOD guidance that program offices updated their business case analyses following implementation of a performance-based logistics arrangements and develop procedures . . . to track whether program offices . . . validate their business case decisions consistent with DOD guidance."⁵⁹¹ Second, the GAO advised the Secretary to "direct program offices to improve their monitoring of performance-based logistics arrangements by verifying the reliability of contractor cost and performance data."⁵⁹² The DOD generally concurred with both recommendations.⁵⁹³

⁵⁷⁷ *Id.* at 2-3. The weapons systems programs that GAO studied were ones that that DOD considered to be examples of successful PBL contracts. *Id.*

⁵⁷⁸ *Id.* at 13-14. The other programs GAO studied included the following weapons systems: the Navy's ALR-67 (V3), the Navy's Auxiliary Power Units, the Navy's F-404, the Navy's T-45 engines, the Navy's V-22 engines, the Navy and Marine Corps' KC-130J, the Army's HIMARS, and Army's Javelin CLU, and the Army's TUAV Shadow.

⁵⁷⁹ *Id.* at 7.

⁵⁸⁰ *Id.* at 1. In a typical DOD performance-based logistics contract, the contractor is required to provide long-term maintenance of DOD weapon systems for a fixed price

⁵⁸¹ U.S. DEP'T OF DEF., *Performance-Based Logistics: A Program Manager's Product Support Guide* (March 2005) [hereinafter *PBL Guidebook*].

⁵⁸² See Memorandum, Michael W. Wynne, Acting Undersecretary of Defense of the United States, to Assistant Secretaries of the Military Departments, Director of Defense Logistics Agency, and President of Defense Acquisition University, subject: Performance-Based Logistics Product Support Guide (10 Nov. 2004) (advising DOD program managers to use the PBL Guidebook in overseeing PBL contracts).

⁵⁸³ *PBL Guidebook*, *supra* note 581, at 3-27.

⁵⁸⁴ *Id.*

⁵⁸⁵ GAO PBL CONTRACTS REPORT, *supra* note 575, at 7.

⁵⁸⁶ *Id.*

⁵⁸⁷ *Id.*

⁵⁸⁸ *Id.* at 9.

⁵⁸⁹ *Id.* at 12.

⁵⁹⁰ *Id.*

⁵⁹¹ *Id.*

⁵⁹² *Id.*

⁵⁹³ *Id.* The DOD responded to the GAO by stating that it would re-affirm DOD guidance regarding business case analyses following the award of a PBL contract and also that it would direct program offices to carefully monitor the costs of such contracts. *Id.* at 17.

Practitioners working in the area of PBL contracts should be aware of this report because it highlights deficiencies in DOD's implementation of the PBL program. DOD's positive response to the GAO report emphasizes its relevance to military program offices.

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Contractors Accompanying the Force

Contractor Personnel Supporting a Force Deployed Outside the United States

Last year, we discussed a proposed DOD rule governing contractor employees accompanying the forces on contingency, humanitarian, peacekeeping or combat operations.⁵⁹⁴ This proposed rule, with changes, became final on 5 May 2005.⁵⁹⁵

Like the proposed clause, the final clause requires contractors to acknowledge the inherent danger in the operation;⁵⁹⁶ specifies that contractors are required to comply with all host nation, U.S., and international laws;⁵⁹⁷ details that contractor employees have to abide by the combatant commander's orders and policies;⁵⁹⁸ requires contractors to provide current lists to the government identifying where their employees are located and have a plan for replacing deployed personnel;⁵⁹⁹ states that contractor personnel cannot wear military uniforms and carry weapons unless specifically authorized;⁶⁰⁰ addresses next of kin notification requirements;⁶⁰¹ contractor evacuation matters;⁶⁰² establishes that the contracting officer will identify the processing and departure locations;⁶⁰³ covers the purchase of scarce commodities;⁶⁰⁴ and, requires that the substance of this contract provision be included in all subcontracts.⁶⁰⁵

While the final rule adopted most of the proposal, it does differ in four ways. First, only a Contracting Officer may make changes to a contract governing contractors accompanying the force (not the ranking military commander).⁶⁰⁶ Despite the seemingly plain language in this clause, the way the drafters wrote clause could generate confusion. Specifically, the clause states "[i]n addition to the changes otherwise authorized by the Changes clause of this contract, the Contracting Officer may, at any time, by written order identified as a change order, make changes in Government furnished facilities, equipment, material, services, or site . . ."⁶⁰⁷ It is not clear what the term "[i]n addition to the changes otherwise authorized by the changes clause . . ." means. On its face, the clause appears to give the contracting officer authority to make out of scope changes related to Government furnished facilities, equipment, material, services, or site. If out of scope changes are authorized, then the government-contractor relationship has changed significantly. Contractors will now deploy with less

⁵⁹⁴ Defense Federal Acquisition Regulation Supplement; Contractors Accompanying a Deployed Force, 69 Federal Register 13,500 (proposed Mar. 23, 2004) (to be codified at 48 C.F.R. pts. 207, 212, 225, and 252).

⁵⁹⁵ Defense Federal Acquisition Regulation Supplement; Contractor Personnel Supporting a Force Deployed Outside the United States, 70 Federal Register 23,790 (May 5, 2005) (to be codified at 48 C.F.R. pts. 207, 212, 225, and 252).

⁵⁹⁶ *Id.* at 23,790.

⁵⁹⁷ *Id.*

⁵⁹⁸ *Id.*

⁵⁹⁹ *Id.*

⁶⁰⁰ *Id.*

⁶⁰¹ *Id.*

⁶⁰² *Id.*

⁶⁰³ *Id.*

⁶⁰⁴ *Id.*

⁶⁰⁵ *Id.*

⁶⁰⁶ *Id.* The proposed rule attempted to give the ranking military commander authority to direct contractor employees to undertake any action, except engaging in armed conflict, when the forces are located outside of the United States, the contracting officer is not available, and enemy action, terrorist activity or a natural disaster requires emergency action. See Defense Federal Acquisition Regulation Supplement; Contractors Accompanying a Deployed Force, 69 Federal Register 13,500 (proposed Mar. 23, 2004) (to be codified at 48 C.F.R. pts. 207, 212, 225, and 252).

⁶⁰⁷ *Id.* at 12. The full clause reads "In addition to the changes otherwise authorized by the Changes clause of this contract, the Contracting Officer may, at any time, by written order identified as a change order, make changes in Government furnished facilities, equipment, material, services, or site. Any change order issued in accordance with this paragraph (p) shall be subject to the provisions of the Changes clause of this contract. *Id.*

certainty and be required to adjust to circumstances it might not have contemplated. Similarly, critics could argue that the procurement process is becoming less transparent to the public.

Second, the clause clarifies that the security of contractor personnel operating in theater is the responsibility of the Combatant Commander.⁶⁰⁸ Third, the Contracting Officer has the authority to direct the contractor to remove any of its employees at the contractor's expense.⁶⁰⁹ Fourth, contractor personnel are entitled to resuscitative care, stabilization, and hospitalization at level III military treatment facilities and transportation in emergencies where loss of life, limb or eyesight could occur.⁶¹⁰ This medical care is provided on a reimbursable basis.

Training for Contractor Personnel Interacting With Detainees

On 1 September 2005, the DOD issued an interim rule⁶¹¹ for DOD contractors who interact with individuals detained by the DOD in the course of their duties. The rule requires DOD contractors, and any subcontractors, who interact with detainees, to receive annual training regarding international obligations and U.S. laws applicable to the detention of such persons. Each contractor is then required to acknowledge receipt of the training.⁶¹²

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⁶⁰⁸ *Id.*

⁶⁰⁹ *Id.*

⁶¹⁰ *Id.* On 3 Oct. 2005, the DOD issued U.S. DEP'T OF DEF., INST. 3020.41, CONTRACTOR PERSONNEL AUTHORIZED TO ACCOMPANY THE U.S. ARMED FORCES (3 Oct. 2005). This instruction addresses some of the contractor issues in DFARS 225.7402 in more detail. This new DODI is available at: http://www.dtic.mil/whs/directives/corres/pdf/i302041_100305/i302041p.pdf.

⁶¹¹ Defense Federal Acquisition Regulation Supplement; Training for Contractor Personnel Interacting With Detainees, 70 Fed. Reg. 52,032 (Sept. 1, 2005) (to be codified at 48 C.F.R. pts. 237 and 252).

⁶¹² *Id.*