Government Contracts

Alert™

http://www.friedfrank.com/practice_groups/gov_contracts.htm

This edition includes Recent Developments, Recent Decisions, and a Feature Article titled "Defective Pricing: GSBCA Holds that Defective Pricing Claim Government Pursued for Over 16 Years Was Not Based Upon Relevant Cost or Pricing Data."

Recent Developments

OFPP Administrator Arrested and Indicted: The Administrator of the Office of Federal Procurement Policy (OFPP), David H. Safavian, was arrested on September 19, 2005 and charged by Federal authorities with making false statements and obstructing an investigation conducted by the General Services Administration (GSA) Office of Inspector General. On October 5, 2005, a grand jury indicted Mr. Safavian on these charges. The criminal complaint filed against Mr. Safavian alleges that, during the time that he served in his prior position as Chief of Staff at the GSA, he aided a lobbyist in the lobbyist's attempts to acquire GSA-controlled property in and around Washington, D.C. The lobbyist allegedly took Mr. Safavian and others on a golf trip to Scotland in August 2002. The false statement and investigation obstruction charges relate to Mr. Safavian's statements to a GSA ethics officer and the GSA Office of Inspector General that the lobbyist had no business with the GSA prior to the golf trip. Mr. Safavian began serving as the OFPP Administrator in November 2004; he resigned from this position shortly after his arrest. In the wake of Mr. Safavian's arrest, Rep. Chris Van Hollen (D-Md.) and five other members of Congress issued a letter requesting the Government Accountability Office to conduct a comprehensive investigation of all matters directly or indirectly involving Mr. Safavian while he served as the GSA Chief of Staff and the OFPP Administrator.

Accounting for Unallowable Costs: Federal Acquisition Regulation (FAR) 31.201-6 was revised to provide that statistical sampling is an acceptable practice for contractors to follow in accounting for and presenting unallowable costs. 70 Federal Register (Fed. Reg.) 57463 (Sept. 30, 2005). However, this practice may only be used where (1) the statistical sampling results in an unbiased sample that is a reasonable representation of the sampling universe, (2) any large dollar value or high risk transaction is separately reviewed for unallowable costs and excluded from the sampling process, and (3) the statistical sampling permits audit verification. The FAR also was revised to provide that the use of statistical sampling methods should be the subject of an advance agreement with the Government. These FAR revisions go into effect on October 31, 2005.

Employee Relocation Costs: The FAR was revised to permit contractors the option of being reimbursed on a lump-sum basis for three types of employee relocation costs. 70 Fed. Reg. 57467 (Sept. 30, 2005). The three types of relocation costs are the costs of (1) finding a new home, (2) travel to the new location, and (3) temporary lodging. These costs are in addition to the miscellaneous relocation costs for which lump-sum reimbursement was already permitted. This FAR revision goes into effect on October 31, 2005.

Expiration of Small Disadvantaged Business Price Evaluation Adjustment: An interim rule was issued to amend the FAR to cancel the authority for civilian agencies (other than the National Aeronautics and Space Administration (NASA) and the U.S. Coast Guard) to apply a price evaluation adjustment to benefit certain small disadvantaged business concerns in competitive acquisitions. 70 Fed. Reg. 57462 (Sept. 30, 2005). This change, which went into effect on September 30, 2005, is necessitated by the expiration of the 1994 statutory authorization for the price evaluation adjustment. As a result, only the Department of Defense (DOD), NASA, and the U.S. Coast Guard are authorized to continue applying the adjustment. Comments to the interim rule must be submitted by November 29, 2005.

Contractor Personnel Interacting with Detainees: The DOD issued an interim rule amending the Defense FAR Supplement (DFARS) to require that DOD contractor personnel who interact with detainees receive training regarding the applicable international obligations and laws of the United States in order to prevent the abuse of detainees. 70 Fed. Reg. 52032 (Sept. 1, 2005), corrected 70 Fed. Reg. 53716 (Sept. 9, 2005). The combatant commander responsible for the area where the detention or interrogation facility is located will provide the training to contractor personnel. The interim rule went into effect on September 1, 2005; comments to the rule must be submitted by October 31, 2005.

Government Property: A proposed rule was issued to amend the FAR to streamline procedures and eliminate obsolete requirements regarding the management and disposition of Government property in contractors' possession. 70 Fed. Reg. 54878 (Sept. 19, 2005). The rule would require personnel dealing with contracts involving Government property to recognize industry-leading practices and standards for managing the property. The rule also would (1) institute a stricter policy for Contracting Officers to follow when determining whether or not to provide Government property to contractors, (2) require contractors to identify the standard or practice proposed for managing Government property, (3) impose an outcome-based framework for the management of Government property in possession of contractors, and (4) allow Contracting Officers to revoke the Government's assumption of risk when property administrators determine that contractor property management practices are inadequate or present an undue risk to the Government. Comments to the proposed rule must be submitted by November 18, 2005.

DOD Basic Ordering Agreements: The DOD issued a proposed rule amending the DFARS to increase to five years the standard maximum period during which orders may be placed under a basic ordering agreement. 70 Fed. Reg. 54694 (Sept. 16, 2005). The current standard maximum ordering period is three years. See DFARS 216.703(c). Comments to the proposed rule must be submitted by November 15, 2005.

Acquisition of Commercial Services: A proposed rule was issued to amend the FAR to authorize the use of time-and-materials and labor-hour contracts for certain categories of commercial services under specified conditions. 70 Fed. Reg. 56318 (Sept. 26, 2005). The FAR currently requires agencies to use firm-fixed-price contracts or fixed-price contracts with economic price adjustment provisions for the acquisition of commercial items, including commercial services, and expressly prohibits agencies from using other contract types for such items. See FAR 12.207. The proposed rule would permit the use of time-and-materials and labor-hour contracts for commercial services when (1) the service is acquired under a contract awarded using competitive procedures and (2) the contracting officer (a) executes a determination and findings that no other authorized contract is suitable, (b) includes a ceiling price in the contract or order, and (c) authorizes any subsequent change in the ceiling price only upon a documented determination that such a change is in the agency's best interest. The rule also would permit the use of indefinite-delivery contracts when rates are established for commercial services acquired on a time-and-materials or labor-hour basis. Comments to the proposed rule must be submitted by November 25, 2005.

Payments Under Time-and-Materials and Labor-Hour Contracts: A proposed rule was issued to amend the FAR regarding payments under time-and-materials and labor-hour contracts. 70 Fed. Reg. 56314 (Sept. 26, 2005). Among other things, the rule would revise FAR 16.601 and FAR clause 52.232-7 to add definitions for the terms "direct materials" and "materials" for use in time-and-materials contracts. The current FAR language has caused much confusion because it does not adequately describe what is included in "materials." Comments to the proposed rule must be submitted by November 25, 2005.

Glossary of Terms Used in the Federal Budget Process: The U.S. Government Accountability Office (GAO) published the fifth edition of A Glossary of Terms Used in the Federal Budget Process (GAO-05-734SP Sept. 1, 2005). The fifth edition is the first revision of the Glossary since 1993. The 178-page Glossary contains standard terms, definitions, and classifications for the Government's fiscal, budget, and program information. Although budget terms are emphasized, relevant economic and accounting terms are also defined to help the user appreciate the dynamics of the budget process and its relationship to other key activities. The Glossary can be accessed online at www.gao.gov.

Recent Decisions

Evaluations of Technical Proposals: The U.S. Court of Federal Claims (COFC) sustained a bid protest challenging the Navy's award of an intelligence support contract because the selection process followed by the agency and the resulting technical evaluations contained so many internal inconsistencies as to be arbitrary and capricious. Beta Analytics Int'l, Inc. v. United States, No. 04-556C (Fed. Cl. Sept. 6, 2005). The COFC sustained the protest despite the fact that the protester's arguments mainly concerned "what may accurately be termed the 'minutiae' of the process – such matters as whether it may appropriately be determined that proposals exceeded the solicitation's requirements, a comparison of the judgment of different evaluators, and second-guessing a number of technical scores."

Reimbursement for Bond Premiums: The General Services Administration Board of Contract Appeals (GSBCA) held that the General Services Administration improperly issued unilateral modifications reducing the prices of two fixed-price roof replacement contracts to reflect the fact that the contractor's actual bond premiums during performance were lower than the estimated bond premiums included in its proposals. Pangea, Inc., GSBCA No. 16688 et al., Sept. 29, 2005. The GSBCA stated that, in the absence of specific contractual language restricting the reimbursement of bond costs to actual bond premiums paid, the FAR's Payments Under Fixed Price Construction Contracts clause does not limit the contractor's right to receive the entire contract price, even if its actual bond premiums incurred after contract award are less than those estimated during the contract negotiation process.

Christian Doctrine: The COFC refused to apply the Christian Doctrine to read a termination for convenience clause into an implied-in-fact Immigration and Naturalization Service (INS) contract for training services. Advanced Team Concepts, Inc. v. United States, No. 02-197 (Fed. Cl. Sept. 28, 2005). The INS terminated the contract in order to award the work to the former Director of the agency's training facility requiring the services. Because it seemed clear that the INS's termination of the contract for convenience was not for the Government's benefit, but instead was for the benefit of the former INS employee, the COFC concluded that the termination was made in bad faith and, as a result, the Christian Doctrine did not apply. The court therefore held that the INS breached the contract by terminating it before the performance period was over.

Contract Termination Settlements: The U.S. Court of Appeals for the Federal Circuit (Federal Circuit) held that, where an agency terminates a contract for convenience, a higher-tier contractor cannot recover fee for the effort of its subcontractors when that contractor has a cost-plus-fixed-fee (CPFF) contract with its next-higher-tier contractor or with the Government. Lockheed Martin Corp. v. England, No. 04-1461 (Fed. Cir. Sept. 21, 2005). The court therefore affirmed an Armed Services Board of Contracts (ASBCA) decision that held that Lockheed Martin could not recover fee for costs incurred by its subcontractors under a terminated CPFF contract for the supply of antennas and transmitters for the Navy's AEGIS program. The Federal Circuit based its decision upon FAR 49.305-1(a), which explicitly states that, for cost-reimbursable contracts terminated for convenience, "[t]he contractor's adjusted fee shall not include an allowance for fee for subcontract effort included in subcontractors' settlement proposals." The court was not swayed by the contractor's argument that the recovery of such fees under termination settlements for cost-type contracts should be treated similarly to termination settlements for fixed-price contracts, where profit on certain subcontractor work is allowed. See FAR 49.202.

Federal Tort Claims Act: The U.S. Court of Appeals for the Ninth Circuit held that the Federal Tort Claims Act's certification process for tort claim immunity for "persons" acting on behalf of a federal agency does not include corporations. The court therefore concluded that the Bureau of Land Management (BLM) properly rejected petitions for certification filed by two BLM contractors seeking immunity under the Act from a lawsuit filed by over 400 farmers and landowners who alleged that the contractors' improper application of herbicide under BLM contracts caused more than $700 million in damages to the plaintiffs' land. Adams v. United States, No. 04-35129 et al. (9th Cir. Aug. 23, 2005)

Contract Disputes Act Jurisdiction: The U.S. Court of Appeals for the Fourth Circuit (4th Circuit) held that the Contract Disputes Act (CDA) applies only to claims by the Government against a contractor or by a contractor against the Government. The 4th Circuit therefore concluded that the CDA does not apply to a lawsuit between a third-party beneficiary (here, the United Kingdom Ministry of Defense) and a contractor even though the dispute related to the contractor's allegedly deficient performance of DOD contracts. United Kingdom Ministry of Defense v. Trimble Navigation Ltd., No. 04-1129 (4th Cir. Sept. 6, 2005). Accordingly, the 4th Circuit reversed a district court decision that held the court lacked jurisdiction under the CDA to consider a breach of contract action filed against the contractor by the third-party beneficiary.

Contract Disputes Act Claims: The ASBCA held that a CDA claim submitted under an Army construction contract was defective because it demanded payment of a "no less than" amount. Sandoval Plumbing Repair, Inc., ASBCA No. 54640, Sept. 14, 2005. The ASBCA stated that a "no less than" amount is not a "sum certain" as required by the FAR's Disputes clause. The board therefore dismissed the appeal, although it did so without prejudice to the contractor reinitiating the disputes process by filing a proper claim with the Contracting Officer.

Contract Disputes Act Interest: Under the CDA, a contractor submitting a claim is entitled to recover interest on the amounts to which it is found to be entitled. The Act provides that this interest runs from the date that the Contracting Officer received the claim. The COFC held that this interest start date applies even for claimed costs that were not yet incurred by the contractor at the time that it submitted its claim. Modeer v. United States, No. 03-2783C (Fed. Cl. Sept. 26, 2005). The COFC stated that, although the CDA's interest trigger date may lead to incongruous results – "as in this case, where interest begins to run on rent that is ultimately found owing even before some of that rent is actually due" – the statutory scheme is intended to promote prompt submission and resolution of claims.

Feature Article

Defective Pricing: GSBCA Holds that Defective Pricing Claim Government Pursued for Over 16 Years Was Not Based Upon Relevant Cost or Pricing Data

Under the Truth in Negotiations Act (TINA), offerors for certain Government contracts are required to submit cost or pricing data with their proposals and to certify that the submitted data are accurate, complete, and current. The submission and certification of cost or pricing data may also be required for certain contract modifications. If it is later determined that the company receiving the contract (or the contract modification) failed to submit accurate, complete, and current cost or pricing data as it certified, the Government is entitled to a price reduction to the extent that it is found that the price was increased by any significant amount due to the contractor's failure to provide the required data. In Viacom, Inc. – Successor in Interest to Westinghouse Furniture Systems, GSBCA No. 15871, Sept. 21, 2005, the General Services Board of Contract Appeals (GSBCA) addressed a case where the board rejected such a "defective pricing" claim, which the Government had pursued for over 16 years, because it was based upon the alleged nondisclosure of cost or pricing data that were not relevant to the contract at issue. Although the dispute involved now-aged statutory and regulatory

provisions that have since been revised, the board's decision nonetheless reflects basic principles that remain relevant under the present TINA framework.

The case involved a three-year multiple award schedule contract for systems furniture workstations that the General Services Administration (GSA) awarded to Westinghouse Furniture Systems (Westinghouse) in July 1985. As required by the solicitation for the contract, Westinghouse submitted cost or pricing data with its May 21, 1984 proposal. This submission included a completed "Discount Schedule and Marketing Data for Commercial Items" sheet in which the company disclosed discount and sales information regarding its commercial customers. Westinghouse's May 21, 1984 proposal also included a required certification that the submitted cost or pricing data were accurate, complete, and current representations of actual transactions "to the date when price negotiations [were] concluded" for the contract. Price negotiations for the contract were subsequently concluded on December 19, 1984. Although the GSA later revised the solicitation, it did not re-open price negotiations, and it awarded the contract to Westinghouse on July 1, 1985. The Government placed orders totaling more than $50 million over the life of the contract.

In January 1989, seven months after the contract ended, the GSA's Office of Inspector General (OIG) notified Westinghouse that the Government would conduct a post-award audit of the contract to determine if Westinghouse had submitted current, accurate, and complete cost or pricing data "prior to the award" of the contract. As a result of its audit, the OIG concluded that Westinghouse had failed prior to award to disclose the full range of discounts that it had offered to its commercial customers. However, although the OIG and Westinghouse traded written submissions regarding the alleged defective pricing, the OIG did not issue a final audit report until September 1998, more than ten years after the contract ended. The OIG's report concluded that Westinghouse had engaged in defective pricing for which GSA was entitled to a pricing refund of $3.8 million. Three and a half years later, on February 14, 2002, the Contracting Officer issued a Final Decision which, based upon the OIG audit report, demanded that Westinghouse refund $3.8 million for defective pricing. After Viacom, Inc., the successor-in-interest to Westinghouse, filed a timely appeal to the GSBCA, the GSA recalculated the alleged defective pricing damages to amount to $8.8 million plus $6.4 million for 16 years of interest, for a total of $15.2 million.

In its decision, the GSBCA held that the GSA failed for "disparate and numerous" reasons to prove that defective pricing had occurred. To begin with, the GSA erroneously based its claim upon the assumption that Westinghouse was required to submit cost or pricing data to the agency up to July 1, 1985, the date of contract award. As stated in its cost or pricing data certification, Westinghouse certified that the submitted cost or pricing data were accurate, complete, and current representations of actual transactions to the date when price negotiations were concluded, which occurred on December 19, 1984. The board therefore held that any discount data that existed only after December 19, 1984 were not relevant cost or pricing data that Westinghouse was required to submit to the Government. The GSA's defective pricing claim partially relied upon commercial invoices that were created after that date.

The GSBCA also found that the allegedly undisclosed discounts relied upon by the GSA were not for the same or similar products as those on the contract. The agency's defective pricing allegations were based upon

discounts for individual furniture workstation components. The contract, however, required Westinghouse to provide integrated systems of components resulting in complete workstations; individual workstation components were not permitted to be ordered. Moreover, the GSA partially relied upon invoices for products that were not even components of the same line of workstations that could be ordered under the contract. The board therefore held that the allegedly undisclosed discounts were not relevant cost or pricing data that Westinghouse was required to disclose to the Government. In so concluding, the board chastised the GSA for failing to conduct a proper examination of the invoices containing the allegedly undisclosed data and for relying upon "somewhat robotic 'automated audit techniques.'"

In addition, the GSBCA rejected the GSA's defective pricing claim because it was substantially based upon allegedly undisclosed cost or pricing data for orders exceeding the solicitation's $75,000 maximum order limitation. Although the GSA amended the solicitation to change the maximum order limitation to a basic order limitation and to allow agencies to place orders above $75,000, this amendment was issued after contract price negotiations were completed in December 1984, and the GSA never reopened price negotiations. The board therefore held that the GSA failed to establish that it detrimentally relied upon the allegedly defective cost or pricing data at the time of price agreement.

Finally, the GSBCA further concluded that the GSA's calculation of defective pricing damages was not reasonable because it was based upon the assumption that, had the allegedly undisclosed cost or pricing data been provided to the Government, the agency would have negotiated the same discounts that it negotiated with Westinghouse in a follow-on contract awarded in 1988. The board rejected this assumption because the follow-on contract contained estimated quantities and price terms and conditions that were considerably different than those involved in the allegedly defectively-priced contract.

As a result, the GSBCA concluded that Westinghouse owed the GSA "nothing" for the alleged defective pricing. If nothing else, the fact that the GSA pursued an apparently baseless defective pricing claim for more than 16 years should serve to remind contractors (and the public) that the allegations of Government auditors – which have become instant fodder for the media and political partisans with increasing frequency in recent years – are merely claims that often are ultimately proven to be unfounded or significantly overstated.

If you have any questions concerning this Feature Article or any other Government contracting issues, please contact any of the partners, counsel, or associates in the Fried Frank Government Contracts Practice Group listed below.

Washington, DC

James J. McCullough
202.639.7130

Steven A. Alerding
202.639.7092

Joseph J. LoBue
202.639.7493

Deneen J. Melander
202.639.7046

Michael J. Anstett
202.639.7390

Courtney J. Edmonds
202.639.7018

Joel R. Feidelman, P.C.
202.639.7150

Wendy P. Fischman
202.639.7219

Jason J. Enzler
202.639.7227

Fried, Frank, Harris, Shriver & Jacobson LLP

New York
One New York Plaza
New York, NY 10004-1980
Tel: 212.859.8000
Fax: 212.859.4000

Washington, DC
1001 Pennsylvania Avenue, NW
Washington, DC 20004-2505
Tel: 202.639.7000
Fax: 202.639.7003

Fried, Frank, Harris, Shriver & Jacobson (Europe)
5, boulevard de La Tour-Maubourg
75007 Paris
France
Tel: 33.140.62.22.00
Fax: 33.140.62.22.29

Frankfurt
Rahmhofstrasse 2-4
60313 Frankfurt am Main
Germany
Tel: 011.49.69.133.868.0
Fax: 011.49.69.133.868.90

Fried, Frank, Harris, Shriver & Jacobson (London) LLP
99 City Road
London EC1Y 1AX
England
Tel: 44.20.7972.9600
Fax: 44.20.7972.9602

Website
www.friedfrank.com

A Delaware Limited Liability Partnership

To view copies of previous Fried Frank Government Contracts Alert™, please visit our archives at http://www.friedfrank.com/govtcon/ffgalert/index.php3.
To view previous Government Contracts To Our Client Memoranda, please visit our archives at http://www.friedfrank.com/firmpubs.php?topic=Government+Contracts.