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CLIENT ALERT

Federal Circuit Clarifies When Affirmative Defenses Must Be Submitted as Claims, and When Interest Runs

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On July 9, 2019, the Federal Circuit issued a decision in *Army v. KBR*, which although nonprecedential, further clarifies when an affirmative defense constitutes a CDA claim that – for jurisdictional purposes – requires a prior Contracting Officer's Final Decision.

As background, the Army withheld $44M in allegedly unallowable security costs from KBR's invoices. KBR submitted consolidated claims arguing that the costs were allowable, and – later – a "protective" claim that the Army had separately breached the contract. In 2015, the Federal Circuit ruled that the costs were "unallowable," but remanded for a determination of whether KBR's breach allegation was properly asserted and, if so, could entitle KBR to the unallowable costs. On remand, KBR asserted that the Army's prior material breach of the contract entitled KBR to the unallowable $44M. KBR prevailed, and the Federal Circuit affirmed.

The Court agreed that the Army's withholding of $44M was a *Government* claim (even though KBR had submitted claims challenging the government's withholding), and that KBR's later assertion of prior material breach was an affirmative defense to the Government's $44M claim for unallowable costs. The Federal Circuit clarified that an affirmative defense of prior material breach, *as written*, may be asserted without a prior CO's Final Decision. In contrast, an affirmative defense that asks/requires (expressly or implicitly) the Court to consider an equitable adjustment to the contract terms – no matter how deserving – *must* first be submitted to the CO for a final decision. The Court explained "we have treated affirmative defenses asserted under the contract[] differently," and announced as a matter of first impression that "[w]hether prior material breach is asserted to eliminate debt as in *Laguna*, or to recover withheld payments as here, the effect is the same — the defense is asserted to defeat a wrongful monetary claim." Lastly, because KBR's claims were legally recharacterized as *Government* claims, and KBR merely prevailed on an affirmative defense to avoid recapture of prior payments, the Court considered whether KBR was entitled to interest under the CDA. The Court held that KBR was entitled to interest on the $44M running from the date that it submitted its various claims to the CO because "that is all that is required for the [CDA] interest clock to begin," and the Court was "aware of no authority instructing that a contractor must state in a claim the legal theory upon which it ultimately recovers to start the running of interest."

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