

## GOOD FAITH IN THE TERMINATION AND FORMATION OF FEDERAL CONTRACTS

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It remains a touchstone in federal contracting law that when the government enters the marketplace, it "contracts as does a private person, under the broad dictates of the common law."<sup>1</sup> As the Supreme Court stated over sixty years ago, "When the United States enters into contract relations, its rights and duties therein are governed generally by the law applicable to contracts between private individuals."<sup>2</sup> More recently, in *United States v. Winstar Corp.*,<sup>3</sup> the Supreme Court construed federal contracts by "applying ordinary principles of contract construction and breach that would be applicable to any contract action between private parties."<sup>4</sup>

The law of good faith, an aspect of the common law of contracts, is receiving heightened attention to befit its increasing importance.<sup>5</sup> Professors Steven Burton and Eric Andersen have recently published a book on this subject entitled *Contractual Good Faith: Formation, Performance, Breach, Enforcement*.<sup>6</sup> In their book, Professors Burton and Andersen collect, summarize, and synthesize the current state of the law in the area of contractual good faith and make suggestions for its proper application and further development.<sup>7</sup> They do not address, however, the concept of contractual good faith as it has developed in government contracts law.<sup>8</sup> In one sense, that is surprising. Although Burton and Andersen trace the origins of the recognition of good faith duties in common law cases to around 1885,<sup>9</sup> the first recognition of good faith duties in government contracts law arguably appeared even earlier. In the 1874 case of *Corliss Steam-Engine Co. v. United States*,<sup>10</sup> the newly constituted United States Court of Claims pronounced that the federal government must deal with its contractors "in the strictest fairness and justice."<sup>11</sup> Indeed, government contracts tribunals

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<sup>1</sup>*Torncello v. United States*, 681 F.2d 756, 762 (Ct. Cl. 1982) (en banc); see also *United States v. Bostwick*, 94 U.S. 53, 66 (1876) ("The United States, when they contract with their citizens, are controlled by the same laws that govern the citizen in that behalf."); *Cooke v. United States*, 91 U.S. 389, 398 (1875) (stating that when the federal government "enters the domain of commerce, it submits itself to the same laws that govern individuals there").<REF ID=FN1>[fm][eb]

<sup>2</sup>*Lynch v. United States*, 292 U.S. 571, 579 (1934); see also *Clearfield Trust Co. v. United States*, 318 U.S. 363, 369 (1943) ("The United States as drawee of commercial paper stands in no different light than any other drawee."); *United States v. Winstar Corp.*, 116 S. Ct. 2432, 2464-65 (1996) (plurality opinion) (referring to the above-quoted *Lynch* passage as a "general principle").<REF ID=FN4>[fm][eb]

<sup>3</sup>116 S. Ct. 2432 (1996).<REF ID=FN2>[fm][eb]

<sup>4</sup>*Id.* at 2453 (plurality opinion); see also *id.* at 2473 (Breyer, J., concurring) ("[sp10c] The United States are as much bound by their contracts as are individuals." (quoting *Sinking Fund Cases*, 99 U.S. 700, 719 (1879))).<REF ID=FN3>[fm][eb]

<sup>5</sup>See Eric G. Andersen, *Good Faith in the Enforcement of Contracts*, 73 IOWA L. REV. 299, 300 (1988) (indicating that the contractual duty of good faith, which had previously been neglected in legal literature, is now the subject of extensive scholarly examination); see also Steven J. Burton, *Breach of Contract and the Common Law Duty to Perform in Good Faith*, 94 HARV. L. REV. 369, 369 (1980) ("A majority of American jurisdictions, the *Restatement (Second) of Contracts*, and the Uniform Commercial Code (U.C.C.) now recognize the duty to perform a contract in good faith as a general principle of contract law.") (footnotes omitted); Steven J. Burton, *More on Good Faith Performance of a Contract: A Reply to Professor Summers*, 69 IOWA L. REV. 497, 497-500 (1984) (discussing differing views on the role that the law of good faith plays in the enforcement of contracts).<REF ID=FN5>[fm][eb]

<sup>6</sup>STEVEN J. BURTON & ERIC G. ANDERSEN, *CONTRACTUAL GOOD FAITH: FORMATION, PERFORMANCE, BREACH, ENFORCEMENT* (1995). Professors Burton and Andersen have written extensively in the field of contractual good faith, and their work has, deservedly, been critically acclaimed.<REF ID=FN6>[fm][eb]

<sup>7</sup>See *id.*<REF ID=FN6A>[fm][eb]

<sup>8</sup>Burton and Andersen make only one footnote reference to "good faith in federal government contracts," citing two recent Court of Federal Claims cases without significant import. *Id.* at 75 n.1.<REF ID=FN8>[fm][eb]

<sup>9</sup>*Id.* at 23-24; see also *Baltimore & O. R. Co. v. Brydon*, 3 A. 306, 309-10 (Md. 1886) (declaring that daily shipments of coal delivered pursuant to a three-year requirements contract could only be rejected in good faith); *Singerly v. Thayer*, 2 A. 230, 233 (Pa. 1885) ("To justify a refusal to accept [delivery] on the ground that it is not satisfactory, the objection should be made in good faith.").<REF ID=FN9>[fm][eb]

<sup>10</sup>10 Ct. Cl. 494 (1874), *aff'd*, 91 U.S. 321 (1875).<REF ID=FN10>[fm][eb]

<sup>11</sup>*Id.* at 502.<REF ID=FN11>[fm][eb]

have recognized that "because of its size, power, and potential ability to manipulate the market place, the Government may have obligations of fairness beyond those of the ordinary citizen."<sup>12</sup>

In another sense, it is not surprising that Burton and Andersen ignore government contracts law. Despite the admonitions of the Supreme Court that the government generally stands in the shoes of a private party when it enters the marketplace,<sup>13</sup> Congress has established special tribunals to adjudicate federal contracts law matters--the Court of Federal Claims<sup>14</sup> and the various boards of contract appeals.<sup>15</sup> Because Congress has legislated and agencies have regulated extensively in the area of federal contracts,<sup>16</sup> the tribunals deciding government contracts cases and those deciding common law contracts cases most frequently work without cross-pollination.<sup>17</sup>

The government contracts tribunals have not always kept abreast of the common law; that failure has been most marked in the area of contractual good faith. While government contracts tribunals have long recognized good faith duties of the government,<sup>18</sup> federal contracts law has not kept pace with the private law of contractual good faith in the specific areas of contract termination and contract formation. The law regarding appropriate limits on the government's exercise of its right to terminate a contract "for convenience" is especially confused.

This Article analyzes the current state of federal contracts law with respect to contract termination and contract formation, and compares it to the common law, using Burton and Andersen's work as a springboard. This Article argues that government contracts law has fallen out of step with the common law governing contracts between private parties with respect to good faith duties. Finally, this Article suggests that federal contracts law should return to the principal touchstone of common law interpretation.

Applying the common law of good faith duties to federal contracts law supports the following conclusions: First, the courts should recognize that the government must exercise its discretion to terminate for convenience in good faith, and, furthermore, the government can breach those duties even when it does not terminate in subjective bad faith. Second, in contract formation cases, the courts should recognize that a breach of good faith duties, as defined by law or

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<sup>12</sup>R&R Enters., 89-2 B.C.A. (CCH) ¶ 21,708 at 109,148 (1989).<REF ID=FN12>[fm][eb]

<sup>13</sup>See *supra* note <CITE ID=FN1> (citing cases standing for the proposition that contract principles apply equally to both government and private citizens).<REF ID=FN12A>[fm][eb]

<sup>14</sup>See Contract Disputes Act of 1978, Pub. L. No. 95-563, 92 Stat. 2383 (codified at 41 U.S.C. §§ 601-613 (1994)) (authorizing a party to a government contract to bring a claim against the government directly to the United States Court of Federal Claims).<REF ID=FN12B>[fm][eb]

<sup>15</sup>See 41 U.S.C. § 607(a), (d) (authorizing agencies to establish their own agency board of contract appeals and granting these boards concurrent jurisdiction with the Court of Federal Claims to decide appeals regarding contracts made by its agency). Prior to 1982, the Court of Claims was composed of an appellate and a trial division. The Federal Courts Improvement Act of 1982 eliminated the Court of Claims (in name) and gave its appellate functions to the newly constituted Court of Appeals for the Federal Circuit and its trial functions to the newly constituted Claims Court. See Pub. L. No. 97-164, 96 Stat. 25 (1982) (codified as amended in scattered sections of 28 U.S.C. and other titles). Many agencies have boards of contract appeals. Most Department of Defense contracts are handled by the Armed Services Board of Contract Appeals (ASBCA), the largest of the boards. Other active boards include the General Services Administration Board of Contract Appeals (GSBCA), the Department of Transportation Board of Contract Appeals (DOT BCA), the Agriculture Board of Contract Appeals (AGBCA), the National Aeronautics and Space Administration Board of Contract Appeals (NASA BCA), the Interior Board of Contract Appeals (IBCA), and the Army Corps of Engineers Board of Contract Appeals (ENG BCA). Decisions from the boards are published in the Commerce Clearing House volumes of Board of Contract Appeals Decisions (BCA).<REF ID=FN13>[fm][eb]

<sup>16</sup>See, e.g., Federal Acquisition Reform Act of 1996, Pub. L. No. 104-106, §§ 4001-4402, 110 Stat. 186, 642-679 (to be codified at scattered sections of 10, 18, 22, 31, 41, and other titles of U.S.C.); Contract Disputes Act of 1978, Pub. L. No. 95-563, 92 Stat. 2383 (codified at 41 U.S.C. §§ 601-613 (1994)); Federal Acquisition Regulation (FAR), 48 C.F.R. pts. 1-52 (1996).<REF ID=FN14>[fm][eb]

<sup>17</sup>Common law courts only infrequently must resort to federal contracts law. The most common instance in which they do is when a subcontract under a government prime contract contains standard federal contract clauses "flowed down" by the prime or higher-tier subcontractors. In such situations, the applicable common law requires the standard federal clause to be construed consistently with trade practice, which is generally supplied by federal precedent of the Federal Circuit, Court of Federal Claims, successor courts, and the boards of contract appeals. See *Linan-Faye Constr. Co. v. Housing Auth.*, 49 F.3d 915, 919-22 (3d Cir. 1995); *Brinderson Corp. v. Hampton Roads Sanitation Dist.*, 825 F.2d 41, 44 (4th Cir. 1987); *Westinghouse Elec. Corp. v. Garrett Corp.*, 437 F. Supp. 1301, 1329 (D. Md. 1977), *aff'd per curiam*, 601 F.2d 155 (4th Cir. 1979); see also *New SD, Inc. v. Rockwell Int'l Corp.*, 79 F.3d 953, 955 (9th Cir. 1996) (finding that federal common law applies to federal clauses flowed down in private contracts). As will be discussed further, the federal district courts also have jurisdiction to consider the propriety of agency awards of contracts. See *infra* notes <CITE ID=FN802> & <CITE ID=FN166> and accompanying text.<REF ID=FN15>[fm][eb]

<sup>18</sup>See, e.g., *Malone v. United States*, 849 F.2d 1441, 1445 (Fed. Cir.) (noting that a breach of good faith and fair dealing duties can be a material breach of contract), *modified*, 857 F.2d 787 (Fed. Cir. 1988); *Corliss Steam-Engine Co. v. United States*, 10 Ct. Cl. 494, 502 (1874) (stating that the government must deal with individuals with whom they contract in "the strictest fairness and justice"), *aff'd*, 91 U.S. 321 (1875).<REF ID=FN16>[fm][eb]

regulation, often allows the award of lost profits, as the contours of the aborted final contract can generally be ascertained with reasonable certainty to an even greater extent than in private contracts.

#### I. GOOD FAITH AS DEFINED IN THE COMMON LAW

Almost all common law jurisdictions in the United States now recognize an implied duty and covenant of good faith binding the parties to a contract.<sup>19</sup> Burton and Andersen have tracked the recent burgeoning of case law in this area. They report that in all the years before 1980, "there were perhaps 350 reported cases interpreting the obligation to perform a contract in good faith. In the dozen years following 1980, there were another 600 or more."<sup>20</sup>

The common law courts, particularly since 1980, have largely reached a consensus on the appropriate application of good faith duties.<sup>21</sup> The first key component of this consensus is that good faith theory serves, rather than rewrites, the intent of the parties as expressed in their contract document.<sup>22</sup> The second, corollary key concept is that good faith duties require the party that is to exercise discretion to do so consistently with the language and purposes of the contract.<sup>23</sup> The critical point of inquiry for this second key concept is the expectations of the parties at the time they formed the contract. Specifically, a party acts in "bad faith"--which the common law courts in this context use synonymously with not acting in contractual good faith<sup>24</sup>--when it uses "contractual discretion to recapture opportunities forgone when contracting,"<sup>25</sup> or performs "for reasons outside the justified expectations of the parties arising from their agreement."<sup>26</sup> Burton and Andersen summarize as follows:

The goal should be an accommodation of the contractual interests of the parties. The public has an interest in the security of contractual transactions: in contract performance and enforcement, we should protect the parties' justified expectations arising from agreements that have passed the tests of enforceability. . . .

A discretion-exercising party has an interest in maintaining the full range of discretionary action as agreed, and often bargained for, calling upon judges and juries to refrain from second-guessing amounting to ad hoc regulation. By contrast, the other party has an interest, also often bargained for, in securing some measure of protection from abuses of discretion by his contract partner. Focusing on a discretion-exercising party's reasons for action, finding liability only when a party acts for a reason given up when entering the contract freely, tends to hold a discretion-exercising party to its voluntary undertakings without engaging in second-guessing or hidden regulation. It protects one party's justified expectations that the other will act for expectable reasons in the relevant business context. This approach preserves a reasonable scope for discretion, rooting the limits on discretion in the parties' agreement.<sup>27</sup>

Although government contracts tribunals have recognized that implied obligations of good faith, cooperation, and fair dealing exist between parties to a government contract,<sup>28</sup> and in some areas have imposed on the government good faith duties consistent with the common law governing contracts between private parties,<sup>29</sup> none of the government

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<sup>19</sup>BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 21-22.<REF ID='FN17'>[fm][eb]

<sup>20</sup>*Id.* at 22.<REF ID='FN18'>[fm][eb]

<sup>21</sup>*Id.* at 38.<REF ID='FN18A'>[fm][eb]

<sup>22</sup>*Id.* at 62-63.<REF ID='FN19'>[fm][eb]

<sup>23</sup>*Id.* at 44-60, 85-90; *see also id.* at 53 n.35 (citing *Boone v. Kerr-McGee Oil Indus.*, 217 F.2d 63, 65 (10th Cir. 1954) ("[S]uch discretion must . . . be exercised in good faith. That simply means that what is done must be done honestly to effectuate the object and purpose the parties had in mind in providing for the exercise of power.")).<REF ID='FN20'>[fm][eb]

<sup>24</sup>*Id.* at 52-57; *see* RESTATEMENT (SECOND) OF CONTRACTS § 205 & cmts. (1981).<REF ID='FN21'>[fm][eb]

<sup>25</sup>BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 45.<REF ID='FN22'>[fm][eb]

<sup>26</sup>*Id.* at 57.<REF ID='FN23'>[fm][eb]

<sup>27</sup>*Id.* at 58.<REF ID='FN24'>[fm][eb]

<sup>28</sup>*See, e.g., Malone v. United States*, 849 F.2d 1441, 1445 (Fed. Cir.) (finding that the government breached contract by failing to comply with standards of good faith between contracting parties), *modified*, 857 F.2d 787 (Fed. Cir. 1988); *Cedar Lumber, Inc. v. United States*, 5 Cl. Ct. 539, 549 (1984) (stating that there is an implied obligation for parties to a contract to cooperate and not to hinder the performance of the other party); *Robert L. Merwin & Co., 83-2 B.C.A. (CCH) ¶ 16,745 at 83,273 (1983)* (recognizing that an implied contract of good faith and fair dealing exists between parties to a government contract).<REF ID='FN25'>[fm][eb]

<sup>29</sup>*See, e.g., Malone*, 849 F.2d at 1445-46 (finding that the government breached its duty to cooperate by failing to disapprove a contractual interpretation prior to the contractor's acting in reliance on the interpretation); *Helene Curtis Indus., Inc. v. United States*, 312 F.2d 774, 778 (Ct. Cl. 1963) (finding that the government breached good faith duties when it did not disclose to a contractor its superior knowledge about the specified manufacturing process). *See generally* Daniel E. Toomey et al., *Good Faith and Fair Dealing: The Well-Nigh Irrefragable Need for a New Standard in Public Contract Law*, 20 PUB. CONT. L.J. 87,

(continued...)

contracts cases articulates an overarching rationale for good faith duties and the application of those duties in contract settings.<sup>30</sup> Nowhere is this more apparent than in the field of government termination of contracts. After an initial movement in the proper direction by the Court of Claims,<sup>31</sup> the Federal Circuit has potentially imposed a full stop on the development of good faith duties consistent with the common law regarding termination of federal contracts.<sup>32</sup>

## II. GOOD FAITH IN THE TERMINATION OF GOVERNMENT CONTRACTS

Burton and Andersen note that only "[a] few very weak common law authorities suggest that a party whose exercise of discretion is motivated by malice or other wrongful motives is in breach of contract for failing to perform in good faith."<sup>33</sup> These "few very weak" cases do not focus on the dispositive inquiry. Although an improper, subjective motive may provide circumstantial evidence of bad faith because it suggests the party is seeking some advantage beyond that intended by the contract,<sup>34</sup> a majority of common law courts now hold to an *objective* standard of whether the party with discretion exercises it within the reasonable expectations of the parties stemming from the promises made at contract formation.<sup>35</sup> Thus, a party cannot be excused from an improper exercise of discretion because it had a "kind heart and an empty head."<sup>36</sup> Burton and Andersen remark:

On the question whether wrongful motives establish bad faith, our answer is clear and amply supported by the cases: wrongful reasons may establish bad faith, but an absence of wrongful reasons does not establish good faith. Wrongful reasons establish bad faith not because they are wrongful, but instead because they are outside the reasonable expectations of the parties. An absence of such reasons, however, does not suffice to establish good faith because bad faith may also consist of action for reasons that are disallowed by the contract even though not wrongful.<sup>37</sup>

These principles expressly apply to the termination of contracts.<sup>38</sup> As Burton and Andersen state, "When there is a contract [a party] with discretion to terminate should be required to terminate only in good faith."<sup>39</sup>

This lesson has been put into practice only spasmodically in government contracts law. The specialized government contracts tribunals have instead improperly focused exclusively on a *subjective* bad faith standard when assessing an agency's termination of a contract. In doing so, they have deviated from the proper application of good faith duties as elucidated by the common law.<sup>40</sup>

### A. Government Termination Law Prior to Torncello

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(...continued)

109-14 (1990) (discussing certain implied duties that are incorporated in the principle of good faith and fair dealing between parties to a contract).<REF ID=FN26>[fm][eb]

<sup>30</sup>Government contracts cases discussing good faith duties do not discuss common law precedents, although they do on occasion cite the *Restatement (Second) of Contracts*, which provides in part, "Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement," RESTATEMENT (SECOND) OF CONTRACTS § 205 (1981), and the U.C.C., which provides, "Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement." U.C.C. § 1-203 (1996). See, e.g., *Malone*, 849 F.2d at 1445 (citing RESTATEMENT (SECOND) OF CONTRACTS § 205); 6800 Corp., 83-2 B.C.A. (CCH) ¶ 16,581 at 82,449 (1983) (same); *John C. Kohler Co. v. United States*, 204 Ct. Cl. 777, 789 n.6 (1974) ("The Uniform Commercial Code is applicable to the field of public contracts."). Burton and Andersen note that the law of good faith has advanced, and in many respects crystallized, since the U.C.C. formulation in 1951 and the *Restatement* summation in 1973. BURTON & ANDERSEN, *supra* note <CITE ID=FN6>, at 34-40.<REF ID=FN27>[fm][eb]

<sup>31</sup>See *infra* notes <CITE ID=FN50>-<CITE ID=FN65> and accompanying text.<REF ID=FN27A>[fm][eb]

<sup>32</sup>See *infra* notes <CITE ID=FN66>-<CITE ID=FN71A> and accompanying text.<REF ID=FN27B>[fm][eb]

<sup>33</sup>BURTON & ANDERSEN, *supra* note <CITE ID=FN6>, at 75.<REF ID=FN28>[fm][eb]

<sup>34</sup>See *supra* notes <CITE ID=FN21>-<CITE ID=FN23> (defining common law bad faith).<REF ID=FN28A>[fm][eb]

<sup>35</sup>BURTON & ANDERSEN, *supra* note <CITE ID=FN6>, at 89-90.<REF ID=FN29>[fm][eb]

<sup>36</sup>*Id.* at 83 (internal quotations omitted).<REF ID=FN30>[fm][eb]

<sup>37</sup>*Id.* at 77-78, 289-90.<REF ID=FN31>[fm][eb]

<sup>38</sup>*Id.* at 91-95 (employment contracts), 142-46 (franchise contracts).<REF ID=FN32>[fm][eb]

<sup>39</sup>*Id.* at 93, 130-34; see also *Sons of Thunder, Inc. v. Borden, Inc.*, No. A-37, 1997 WL 104592, at \*14-16 (N.J. Mar. 11, 1997) (upholding jury verdict that defendant breached duty of good faith notwithstanding express right to terminate the contract).<REF ID=FN33>[fm][eb]

<sup>40</sup>See *infra* notes <CITE ID=FN72>-<CITE ID=FN308A> and accompanying text (discussing the common law precedent concerning good faith duties in terminations). <REF ID=FN34>[fm][eb]



A "termination-for-convenience" clause is a common feature in government contracts.<sup>41</sup> Although not essential to every contract in which the government is a party,<sup>42</sup> a termination-for-convenience clause is required in most government contracts under the applicable provisions of the Federal Acquisition Regulation (FAR).<sup>43</sup> Even when not expressly incorporated into a government contract, a termination-for-convenience clause will be incorporated by law if it was required to have been included by regulation.<sup>44</sup> Moreover, if the government terminates for an improper purpose--for default when the contractor was not truly in default, for example--the termination generally can be "constructively" converted into a termination for convenience if such a clause is present in the contract.<sup>45</sup>

The government is given broad discretion under a termination-for-convenience clause to terminate a contract.<sup>46</sup> The termination-for-convenience clause, which must be included in most fixed-price contracts over \$100,000,<sup>47</sup> provides, like other termination clauses, "The Government may terminate performance of work under this contract in whole or, from time to time, in part if the Contracting Officer determines that a termination is in the Government's interest."<sup>48</sup> When the termination-for-convenience clause is properly invoked, either expressly or constructively, it limits the recoverable damages of the contractor to the work performed, plus incidental expenses due to the termination,<sup>49</sup> thereby foreclosing breach damages.<sup>50</sup> Lost profits are allowed for work performed, but not for work terminated.<sup>51</sup>

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<sup>41</sup> See Stephen N. Young, Note, *Limiting the Government's Ability to Terminate for Its Convenience Following Torncello*, 52 GEO. WASH. L. REV. 892, 892 (1984).<REF ID=FN35A>[fm][eb]

<sup>42</sup> See, e.g., *United States v. Winstar Corp.*, 116 S. Ct. 2432 (1996) (contracts representing business arrangements without termination-for-convenience clause); *Wells Fargo Bank, N.A. v. United States*, 33 Fed. Cl. 233 (1995) (same), *aff'd in part and rev'd in part*, 88 F.3d 1012 (Fed. Cir. 1996), *cert. denied*, 117 S. Ct. 1245 (1997); *Johnson v. United States*, 15 Cl. Ct. 169 (1988) (lease contract); *Arrow Transfer Co.*, 81-1 B.C.A. (CCH) ¶ 14,842 at 73,267 (1980) (services contract).<REF ID=FN36>[fm][eb]

<sup>43</sup> See FAR, 48 C.F.R. § 49.501-05 (1996). The FAR requires termination-for-convenience clauses in various types of fixed-price and cost-reimbursement contracts. See *id.* § 49.501. The FAR also permits special purpose clauses to be negotiated and allows deviations from FAR requirements if approved at the specified level. See *id.* §§ 1.402 (allowing special purpose termination clauses), 49.501 (same).<REF ID=FN37>[fm][eb]

<sup>44</sup> This principle has taken the name of the "*Christian doctrine*" after the lead case in the area. See *G.L. Christian & Assocs. v. United States*, 320 F.2d 345, 351 (Ct. Cl. 1963) (holding that "an authorized regulation can impose . . . peremptory requirements on federal officials and those who seek to enter into transactions with the Government"). The *Christian doctrine* does not extend to situations in which a termination-for-convenience clause is not required by law to have been included in the contract. See *Johnson*, 15 Cl. Ct. at 171-72.<REF ID=FN38>[fm][eb]

<sup>45</sup> Constructive termination-for-convenience theory finds its leading exposition in the decision of *John Reiner & Co. v. United States*, 325 F.2d 438 (Ct. Cl. 1963). The *John Reiner* court found support for its position, in turn, from the Supreme Court's decision in *College Point Boat Corp. v. United States*, 267 U.S. 12 (1925). *John Reiner*, 325 F.2d at 443. In *College Point*, the Court held that the damages for the government's stopping work on a contract and being in anticipatory breach could be limited by a statute then in force that allowed the government to cancel World War I contracts after the war ended, even though the government agency did not purport to act under that statute. *College Point*, 267 U.S. at 15-16. The standard federal default clauses now expressly provide that if a defaulted contractor was not in default when terminated or the default condition was excusable, "the rights and obligations of the parties shall be the same as if the termination had been issued for the convenience of the Government." See, e.g., FAR, 48 C.F.R. § 52.249-8(g) (1996) (Default (Fixed-Price Supply and Service)).<REF ID=FN39>[fm][eb]

<sup>46</sup> See Young, *supra* note <CITE ID=FN35A>, at 897 (indicating that a contracting officer, in exercising his discretion to terminate a contract under a termination-for-convenience clause, may consider a "[sp10c]' host of variable and unspecified situations" (quoting *John Reiner & Co.*, 325 F.2d at 442)). The Supreme Court last term held, however, that the First and Fourteenth Amendments restrict the government's ability to terminate a contractor because he expresses or does not express specific political views. See *O'Hare Truck Serv., Inc. v. City of Northlake*, 116 S. Ct. 2353, 2356-61 (1996).<REF ID=FN39A>[fm][eb]

<sup>47</sup> See 48 C.F.R. § 49.502(b).<REF ID=FN39B>[fm][eb]

<sup>48</sup> 48 C.F.R. § 52.249-2; see also 48 C.F.R. § 52.249-1 ("The Contracting Officer, by written notice, may terminate this contract, in whole or in part, when it is in the Government's interest."); 48 C.F.R. § 52.249-6(a) ("The Government may terminate performance of work under this contract in whole or, from time to time, in part, if . . . [t]he Contracting Officer determines that a termination is in the Government's interest . . .").<REF ID=FN40>[fm][eb]

<sup>49</sup> The applicable termination-for-convenience clause and referenced FAR provisions spell out in some detail the recovery allowed to the contractor in a termination for convenience. See, e.g., 48 C.F.R. § 52.249-2; see also 48 C.F.R. § 31.205-42 (specifying recoverable costs due to a termination).<REF ID=FN41>[fm][eb]

<sup>50</sup> See *John Reiner*, 325 F.2d at 444 (indicating that a party to a contract may not recover anticipated profit when the government exercises a termination-for-convenience clause).<REF ID=FN42>[fm][eb]

<sup>51</sup> See 48 C.F.R. § 52.249-2(f) (Termination for Convenience of the Government (Fixed-Price)).<REF ID=FN43>[fm][eb]

Limits have always been placed on the government's discretion to use a termination-for-convenience clause.<sup>52</sup> For example, it has long been held that an agency may not properly terminate for convenience, either expressly or constructively, if it acted in "bad faith" or committed a "clear abuse of discretion."<sup>53</sup> Bad faith has been construed in federal contracts termination law, however, to mean *subjective* bad faith, rather than simply the failure to perform in good faith, *objectively* tested against the duties arising from the contract itself, as enjoined by the prevailing common law precedents.<sup>54</sup> Moreover, government contracts tribunals impose the rule that to prove subjective bad faith on the part of the government agency terminating the contract, the terminated contractor must put forward "well-nigh irrefragable proof."<sup>55</sup>

The high-water mark of the government's perceived discretion to exercise the termination-for-convenience clause was the 1974 Court of Claims decision in *Colonial Metals Co. v. United States*.<sup>56</sup> In *Colonial Metals*, the government contracted for a supply of copper from a contractor, but soon terminated the contract in order to get a better price from another source.<sup>57</sup> Notwithstanding the court's finding that the government "knew or ought to have known" that a better price was readily available,<sup>58</sup> the court validated the government's exercise of the termination clause solely to gain a better deal.<sup>59</sup> The court stated:

Termination to buy elsewhere at a cheaper price is essentially such a termination as has repeatedly been approved. The added element that the contracting officer knew of the better price elsewhere when he awarded the contract to plaintiff--in the absence of some proof of malice or conspiracy against the plaintiff--means only that the contract was awarded improvidently and does not narrow the right to terminate. The clause is not designed to perpetuate error, but to permit its rectification.

Termination for convenience is as available for contracts improvident in their origin as for contracts which supervening events show to be onerous or unprofitable for the Government.<sup>60</sup> The court in *Colonial Metals* effectively ruled that in the absence of bad faith,<sup>61</sup> there are no limits on the government's power to repudiate a contract under a termination-for-convenience clause if the government believes it is in its interest to do so.<sup>62</sup>

#### B. Torncello to the Present@

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<sup>52</sup>Torncello v. United States, 681 F.2d 756, 764-66 (Ct. Cl. 1982) (en banc) (discussing history of termination for convenience clauses).<REF ID=FN43A>[fm][eb]

<sup>53</sup>See, e.g., National Factors, Inc. v. United States, 492 F.2d 1383, 1385 (Ct. Cl. 1974) (per curiam) ("The termination of a contract for the convenience of the government is valid only in the absence of bad faith or a clear abuse of discretion." (citing Commercial Cable Co. v. United States, 170 Ct. Cl. 813, 821 (1965))); *John Reiner*, 325 F.2d at 442 ("[I]n the absence of bad faith or clear abuse of discretion the contracting officer's election to terminate is conclusive.").<REF ID=FN44>[fm][eb]

<sup>54</sup>See *infra* notes <CITE ID=FN308B>-<CITE ID=FN90> and accompanying text.<REF ID=FN43C>[fm][eb]

<sup>55</sup>See *Knotts v. United States*, 121 F. Supp. 630, 631 (Ct. Cl. 1954); see also *Kalvar Corp. v. United States*, 543 F.2d 1298, 1301-02 (Ct. Cl. 1976) (noting that "irrefragable proof" has been equated with evidence of some specific intent to injure the plaintiff), *cert. denied*, 434 U.S. 830 (1977).<REF ID=FN45>[fm][eb]

<sup>56</sup>494 F.2d 1355 (Ct. Cl. 1974) (per curiam) (adopting the recommended decision of the trial judge as the basis for its judgment in the case); see *Linan-Faye Constr. Co. v. Housing Auth.*, 49 F.3d 915, 924 (3d Cir. 1995) (describing *Colonial Metals* as the high-water mark of permissiveness in allowing government to terminate).<REF ID=FN46>[fm][eb]

<sup>57</sup>*Colonial Metals*, 494 F.2d at 1357.<REF ID=FN46A>[fm][eb]

<sup>58</sup>*Id.* at 1360.<REF ID=FN47>[fm][eb]

<sup>59</sup>*Id.* at 1361.<REF ID=FN47A>[fm][eb]

<sup>60</sup>*Id.* (citation omitted).<REF ID=FN48>[fm][eb]

<sup>61</sup>The court in *Colonial Metals* did not repudiate the "subjective bad faith or clear abuse of discretion" exception articulated in prior opinions. See *id.* at 1359. The abuse of discretion exception and its scope are not well defined, with few cases addressing how it differs from bad faith, even after *Colonial Metals*. Some tribunals, however, have made a distinction. See, e.g., *Vibra-Tech Eng'rs, Inc. v. United States*, 567 F. Supp. 484, 486-87 (D. Colo. 1983) (applying abuse of discretion standard without finding bad faith); *Viktoria Transp. GmbH & Co., KG*, 88-3 B.C.A. (CCH) ¶ 20,921 at 105,737 (1988) (defining abuse of discretion standard separately). Others have accepted the equivalence of the concepts *arguendo*. See, e.g., *Kalvar Corp. v. United States*, 543 F.2d 1298, 1301 n.1 (Ct. Cl. 1976) ("[M]any of our prior decisions seem implicitly to accept the equivalence of bad faith, abuse of discretion, and gross error.").<REF ID=FN1061A>[fm][eb]

<sup>62</sup>See Karl M. Elcessor, III, *Torncello and the Changed Circumstances Rule: "A Sheep in Wolf's Clothing," ARMY LAW.*, Nov. 1991, at 18, 19.<REF ID=FN49>[fm][eb]

Eight years later, the Court of Claims overruled *Colonial Metals* in *Torncello v. United States*.<sup>63</sup> In *Torncello*, the government had entered into a requirements contract, but after executing the contract, began to divert a particular portion of the business to a competitor that had offered to perform this specific component of the contract at a lower price.<sup>64</sup> At the Armed Services Board of Contract Appeals (ASBCA), the government had successfully defended on a theory that diversion of some of the requirements to the other company was a constructive partial termination for convenience by the government.<sup>65</sup>

Writing the plurality opinion, Judge Bennett undertook a historical analysis of the termination-for-convenience clause.<sup>66</sup> He explained that "the convenience termination clause developed as a wartime concept, and it was a way for the government to avoid the continuance of contracts that the rapid changes of war, or the war's end, had made useless or senseless."<sup>67</sup> Judge Bennett also noted that use of the clause had continued into peacetime procurement, but "the basic idea remained constant that convenience termination was an allocation of the risk of changed conditions."<sup>68</sup> Therefore, he found that the risk allocation justification for the termination-for-convenience clause, under all precedent other than *Colonial Metals*, could only be used "when the expectations of the parties had been subjected to a substantial change. The contractor risked losing the full benefit of his performance if something occurred, apart from the bargain and the expectations of the parties, that made continuance of the contract clearly inadvisable."<sup>69</sup> After reviewing the relevant history, Judge Bennett determined that "the termination for convenience clause was only to be applied where there was some change from the parties' original bargain and was not to be applied as broadly as an untutored reading of the words might suggest."<sup>70</sup>

Judge Bennett next noted that if the termination-for-convenience clause were interpreted to give the government an unrestricted "out," the contract would fail for want of consideration.<sup>71</sup> The government argued that the exercise of discretion to terminate the contract was sufficiently limited because the contracting officer was required to determine in good faith that termination would be in the best interest of the government.<sup>72</sup> The *Torncello* plurality rejected this argument because it read existing case law to require an "extremely difficult showing" of "well-nigh irrefragable proof" that the government acted in *subjective* bad faith<sup>73</sup>--with specific intent to injure the contractor by actions "motivated alone by malice,"<sup>74</sup> by "designedly oppressive" conduct,<sup>75</sup> or by conduct "actuated by animus" toward the contractor.<sup>76</sup> To the government's parallel assertion that its power to terminate was subject to a sufficient limitation, in that it could not properly

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<sup>63</sup>681 F.2d 756 (Ct. Cl. 1982) (en banc).<REF ID='FN50'>[fm][eb]

<sup>64</sup>*Id.* at 758.<REF ID='FN51'>[fm][eb]

<sup>65</sup>*Id.* at 758-59. A more appropriate rationale for rejecting the ASBCA's constructive use of the termination-for-convenience clause than that adopted by the Court of Claims would have been: (1) the covenant that the government would buy all of its requirements from the contractor is not principally a quantity term (subject to total or partial termination); (2) but, instead, is principally a condition of the contract not subject to the termination clause; and (3) thus, the termination clause was not appropriately brought into play at all, as the government concededly had requirements that it bought elsewhere. The Court of Claims, however, did not consider this argument and decided the case as if the termination clause could have been appropriately invoked in these circumstances, even if there were not a cessation of requirements.<REF ID='FN52'>[fm][eb]

<sup>66</sup>*Id.* at 763-66 (plurality opinion).<REF ID='FN52A'>[fm][eb]

<sup>67</sup>*Id.* at 763 (citing II RALPH C. NASH & JOHN CIBINIC, JR., FEDERAL PROCUREMENT LAW 1104-07 (3d ed. 1980)).<REF ID='FN53'>[fm][eb]

<sup>68</sup>*Id.*<REF ID='FN54'>[fm][eb]

<sup>69</sup>*Id.* at 766.<REF ID='FN55'>[fm][eb]

<sup>70</sup>*Id.* *Colonial Metals* did not involve a change of conditions and, therefore, violated this principle. See *Colonial Metals Co. v. United States*, 494 F.2d 1355 (Ct. Cl. 1974) (per curiam). In *Colonial Metals*, the use of the termination-for-convenience clause was to remake the contract with another party "for a reason that was known or should have been known to the government *before* the contract was awarded." *Torncello*, 681 F.2d at 766 (plurality opinion).<REF ID='FN57A'>[fm][eb]

<sup>71</sup>*Torncello*, 681 F.2d at 768-72 (plurality opinion). In Judge Bennett's terminology, he rejected a "free termination" right in the government. *Id.* at 771.<REF ID='FN57'>[fm][eb]

<sup>72</sup>*Id.* at 770-71.<REF ID='FN57A'>[fm][eb]

<sup>73</sup>*Id.* (quoting *Knotts v. United States*, 121 F. Supp. 630, 631 (Ct. Cl. 1954)).<REF ID='FN57B'>[fm][eb]

<sup>74</sup>*Id.* (quoting *Gadsden v. United States*, 78 F. Supp. 126, 127 (Ct. Cl. 1948)).<REF ID='FN57C'>[fm][eb]

<sup>75</sup>*Id.* at 771 (quoting *Struck Constr. Co. v. United States*, 96 Ct. Cl. 186, 222 (1942)).<REF ID='FN57D'>[fm][eb]

<sup>76</sup>*Id.* (quoting *Librach v. United States*, 147 Ct. Cl. 605, 614 (1959)).<REF ID='FN58'>[fm][eb]

invoke the termination clause if it would be "a clear abuse of discretion" to do so,<sup>77</sup> Judge Bennett responded that no limits on that discretion were stated, and so, in essence, the argument was circular.<sup>78</sup> He concluded:

[T]he requirement of good faith is not sufficient because the government's presumption of good faith dealing is rebuttable only in the most extreme circumstances, when there is a specific intent to harm the contractor. And the government's obligation to avoid clear abuses of discretion is only an illusion. Without any other limits, the concept of discretion is meaningless.<sup>79</sup>

In the plurality's view, the subjective bad faith and clear abuse of discretion restrictions on the government's exercise of its termination rights could not provide brakes on the government's power to exculpate itself sufficient to constitute adequate consideration to support the contract.<sup>80</sup> As a result, the *Tomcello* plurality held that the government may not employ the termination-for-convenience clause "to dishonor, with impunity, its contractual obligations."<sup>81</sup>

Writing in a concurring opinion, Chief Judge Friedman viewed the case narrowly. He stated that he understood the plurality's opinion to mean that the termination-for-convenience clause is only inapplicable when the government, at the time of contracting, knows it will not honor its requirements contract because it plans to place orders with a competing contractor.<sup>82</sup>

Concurring in the result, Judge Davis also stressed the government's preexisting knowledge that it planned to dishonor the requirements contract via the termination-for-convenience clause.<sup>83</sup> He expressly disagreed with the plurality's analysis of the abuse of discretion and bad faith exceptions, however, finding them less narrow than Judge Bennett portrayed them.<sup>84</sup> Based on the facts of *Tomcello*, Judge Davis found both of those standards to have been violated.<sup>85</sup>

Judge Nichols, who also wrote separately and concurred in the result, continued to embrace the bad faith and clear abuse of discretion standards, finding them sufficient to furnish consideration.<sup>86</sup> Based on the facts of *Tomcello*, however, Judge Nichols found it to be an abuse of discretion for the government to have acted the way it did.<sup>87</sup>

The plurality and three concurring opinions in *Tomcello* left its controlling rationale unclear. Only recently has the Federal Circuit (the successor court to the Court of Claims) apparently settled on how it will read *Tomcello*. The Federal Circuit initially repeated that "changed expectations" are a prerequisite to a proper termination for convenience.<sup>88</sup> In *Caldwell & Santmyer, Inc. v. Glickman*,<sup>89</sup> however, the Federal Circuit, in dicta, read *Tomcello* very restrictively. In a curious mix of references to Judge Bennett's plurality opinion and the three concurring opinions, the Federal Circuit reiterated the principle that the government is presumed to act in good faith unless a contractor can show "through

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<sup>77</sup> *Id.* <REF ID=FN58F>[fm][eb]

<sup>78</sup> *Id.* <REF ID=FN59>[fm][eb]

<sup>79</sup> *Id.* <REF ID=FN60>[fm][eb]

<sup>80</sup> See *id.* <REF ID=FN87A>[fm][eb]

<sup>81</sup> *Id.* at 772. <REF ID=FN62>[fm][eb]

<sup>82</sup> See *id.* at 773 (Friedman, C.J., concurring). <REF ID=FN63>[fm][eb]

<sup>83</sup> See *id.* (Davis, J., concurring in the result). <REF ID=FN63A>[fm][eb]

<sup>84</sup> See *id.* <REF ID=FN63B>[fm][eb]

<sup>85</sup> See *id.* at 773-74. Judge Davis had "no difficulty" in finding the government's conduct to have been an abuse of discretion and in bad faith. *Id.* He went on to add, however, that if the government became aware of a better price *after* executing the requirements contract, that would potentially be a changed circumstance sufficient to allow the government to terminate the original contract and to take advantage of the better price. *Id.* at 774; see *infra* notes <CITE ID=FN71A>-<CITE ID=FN308A> (discussing the inconsistency of this suggestion with common law precedent). <REF ID=FN64>[fm][eb]

<sup>86</sup> *Tomcello*, 681 F.2d at 774 (Nichols, J., concurring in the result). <REF ID=FN64A>[fm][eb]

<sup>87</sup> *Id.* Judge Nichols pointed out that the pest control services, which had been the subject of the requirements contract, were only one aspect of the overall contract, with other parts of performance also considered in the award of the contract. See *id.* He found it arbitrary and capricious for the government, after awarding the contract based on evaluation of each bid in its entirety, to grant subsequently a particular portion of the contract to an unsuccessful bidder that had offered to perform that aspect of the solicitation at a lower price. See *id.* <REF ID=FN65>[fm][eb]

<sup>88</sup> See *Salsbury Indus. v. United States*, 905 F.2d 1518, 1521-22 (Fed. Cir. 1990) (finding that a court injunction directing the postal service to terminate a contract was an "unanticipated change in circumstances, not merely justifying but compelling termination of the contract"); *Maxima Corp. v. United States*, 847 F.2d 1549, 1553, 1557 (Fed. Cir. 1988) (noting that both parties acknowledged that there must be some changed circumstances prior to exercising a termination-for-convenience clause). <REF ID=FN66>[fm][eb]

<sup>89</sup> 55 F.3d 1578 (Fed. Cir. 1995). <REF ID=FN67>[fm][eb]



'well-nigh irrefragable proof' that the government had a specific intent to injure it."<sup>90</sup> Despite Judge Bennett's rejection of the bad faith and abuse of discretion exceptions,<sup>91</sup> the Federal Circuit went on to identify *Torncello* as a subjective bad faith case that stood only for the "unremarkable proposition that when the government contracts with a party knowing full well that it will not honor the contract, it cannot avoid a breach claim by adverting to the convenience termination clause."<sup>92</sup> Building on the dicta in *Caldwell*, the Federal Circuit in *Krygoski Construction Co. v. United States*<sup>93</sup> declared the *Torncello* plurality's analysis to be moribund, except as limited to its facts as explained in *Caldwell*.<sup>94</sup>

### C. Good Faith Duties in Government Terminations

The Federal Circuit's apparent retrenchment in *Caldwell* and *Krygoski*, suggesting that a contractor must prove subjective bad faith to establish that the government abused its discretion to terminate for convenience, runs directly counter to the recent common law consensus regarding terminations.<sup>95</sup> Under the common law, proving bad faith—in the sense of a breach of good faith duties—does not require showing subjective bad faith.<sup>96</sup> Although the government understandably gives itself broad discretion to exercise its right to terminate, that discretion, like other exercises of discretion, should only be exercised in good faith. The failure of the courts and boards adjudicating government contracts disputes to recognize that the government has a duty to exercise its termination discretion in good faith has caused confusion in the case law.<sup>97</sup> This confusion could be alleviated by requiring that the government, like a private citizen, exercise its termination discretion in good faith.

Although Burton and Andersen find it "not problematic" that if a valid contract exists, a party's discretion to terminate is constrained by good faith duties,<sup>98</sup> that very proposition has escaped open and uniform recognition in the

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<sup>90</sup> *Id.* at 1581.<REF ID=FN68>[fm][eb]

<sup>91</sup> See *supra* notes <CITE ID=FN52A>–<CITE ID=FN62> and accompanying text.<REF ID=FN67B>[fm][eb]

<sup>92</sup> *Caldwell*, 55 F.3d at 1582 (quoting *Salsbury Indus.*, 905 F.2d at 1521). The ASBCA has consistently refused to follow the plurality opinion in *Torncello*. In assessing the legitimacy of express or constructive terminations for convenience, the ASBCA has continued to apply what it terms the subjective "bad faith/abuse of discretion" standard. The ASBCA purports to rely on the *Torncello* concurring opinions, but it does not specify which one or ones in particular. See *Special Waste, Inc.*, 90-2 B.C.A. (CCH) ¶ 22,935 at 115,129 (1990) ("A Government good faith determination after contract award that it did not need the contract item . . . was all that was required to support a termination for convenience."); *Viktoria Transp. GmbH & Co., KG*, 88-3 B.C.A. (CCH) ¶ 20,921 at 105,737 (1988) ("The authorities are clear that breach damages have been awarded in breach of requirements contract situations only where there is bad faith or abuse of discretion on the part of the Government."); *Vec-Tor, Inc.*, 85-1 B.C.A. (CCH) ¶ 17,755 at 88,677 (1984) ("We agree with the concurring opinions [in *Torncello*] and will follow the bad faith/abuse of discretion rule regarding convenience-termination until the 'change of circumstances' rule is adopted by a clear majority of the Court.").<REF ID=FN69>[fm][eb]

<sup>93</sup> 94 F.3d 1537 (Fed. Cir. 1996), *cert. denied*, 65 U.S.L.W. 3571 (U.S. May 12, 1997) (No. 96-1236). Correctly forecasting the Federal Circuit's further elucidation in *Krygoski*, a commentator on *Caldwell* stated, "Thus, the holding of *Torncello*, which placed reasonable limits on the government's broad right to terminate a government contract for convenience, has effectively been abandoned." Michael W. Clancy, 1995 *Year in Review: The Federal Circuit's Government Contracts Decisions*, 25 PUB. CONT. L.J. 537, 580 (1996).<REF ID=FN70>[fm][eb]

<sup>94</sup> *Krygoski*, 94 F.3d at 1542. The *Krygoski* court reaffirmed that a termination for convenience would be a breach if it were a clear abuse of discretion or taken in subjective bad faith. *Id.* at 1543. The *Krygoski* court sought to buttress its conclusion that the *Torncello* plurality opinion was not good law by referring to the Competition in Contracting Act (CICA). *Id.* at 1542-43. The only relevance of CICA, however, is to define the duties of the procuring agencies and, derivatively, the reasonable expectations of the parties. See Competition in Contracting Act of 1984, Pub. L. No. 98-369, 98 Stat. 1175 (codified in scattered sections of 5, 10, 31, 40, and 41 U.S.C.) (delineating, *inter alia*, government procurement procedures, competition requirements, and award guidelines). The actual facts of *Krygoski*, as explained by the Federal Circuit, would arguably meet the *Torncello* plurality's test of sufficiently changed circumstances to support a termination for convenience, but the panel sidestepped that obvious conclusion in favor of its limiting construction of *Torncello*. *Krygoski*, 94 F.3d at 1543 ("Although arguably the Government's circumstances had sufficiently changed to meet even the *Torncello* plurality standard, this court declines to reach this issue because *Torncello* applies only when the Government enters a contract with no intention of fulfilling its promises.").<REF ID=FN71>[fm][eb]

<sup>95</sup> See *infra* notes <CITE ID=FN308B>–<CITE ID=FN90> and accompanying text.<REF ID=FN71A>[fm][eb]

<sup>96</sup> BURTON & ANDERSEN, *supra* note <CITE ID=FN6>, at 89.<REF ID=FN72>[fm][eb]

<sup>97</sup> See *supra* notes <CITE ID=FN50>–<CITE ID=FN65> and accompanying text.<REF ID=FN72A>[fm][eb]

<sup>98</sup> BURTON & ANDERSEN, *supra* note <CITE ID=FN6>, at 91-93; see also *Danella Southwest, Inc. v. Southwestern Bell Tel. Co.*, 775 F. Supp. 1227, 1236 (E.D. Mo. 1991) ("The implied duty of good faith and fair dealing extends to the cancellation of a contract."). Burton and Andersen point out that some courts find that, because an at-will employee may be discharged for no reason or even a morally wrong reason, an at-will employee does not have a contractual relationship with her employer. BURTON & ANDERSEN, *supra* note <CITE ID=FN6>, at 92.<REF ID=FN73>[fm][eb]

government contracts termination-for-convenience cases.<sup>99</sup> While government contracts tribunals have no problem applying common law good faith principles in other contract performance settings,<sup>100</sup> they have failed to apply regularly the same good faith rules in termination settings.<sup>101</sup>

1. *Good Faith in Common Law Termination Cases.*--Common law jurisprudence has consistently implied a good faith duty in contract termination cases.<sup>102</sup> Employment situations provide a clear window to these common law cases. Burton and Andersen distinguish between "contracts promising employment for a definite duration, even if equal only to a required period following notice of termination, and those involving employment terminable at the employer's will."<sup>103</sup> In the former case, "[t]he applicability of a good faith performance covenant is not problematic,"<sup>104</sup> and "an employer with discretion to terminate should be required to terminate only in good faith."<sup>105</sup>

Even in employment-at-will situations, however, an employee may not be terminated for reasons contrary to the justified expectations of the parties.<sup>106</sup> *K Mart Corp. v. Ponsock*<sup>107</sup> provides a good example. In that case, a company used a pretext to fire an older, tenured employee so that it would not have to pay him retirement benefits.<sup>108</sup> The court found that the company's action "reek[ed] of oppression and malice" and that the company had violated its duty to act in good faith when terminating an employee.<sup>109</sup> In *Burnaman v. Bay City Independent School District*,<sup>110</sup> the court found the defendant school district to have acted in bad faith when it discharged a teacher on the basis of a written evaluation containing information that the defendants knew or should have known was false and inaccurate, and when school district employees then tried to cover up their actions in violation of their own regulations.<sup>111</sup> Recent cases considering similar issues have held that an employer violates good faith duties when it discharges an at-will employee to avoid paying her benefits earned, thus making the company more profitable.<sup>112</sup>

Common law courts have applied the same good faith principles in nonemployment situations. For example, a requirements buyer cannot, consistent with good faith duties, acquire goods or substitutes elsewhere (thus constructively

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<sup>99</sup> See *supra* notes <CITE ID='FN50'>-<CITE ID='FN65'> and accompanying text.<REF ID='FN73A'>[fm][eb]

<sup>100</sup> For example, the Federal Circuit recently imposed good faith duties during contract negotiation, noting that those duties provide the necessary mutuality of obligation to enforce an open-price term contract. See *Aviation Contractor Employees, Inc. v. United States*, 945 F.2d 1568, 1572-73 (Fed. Cir. 1991); see also *Malone v. United States*, 849 F.2d 1441, 1445-46 (Fed. Cir.) (holding that the government breached its good faith duty when an Air Force contracting officer's evasive conduct interfered with the contractor's performance), modified, 857 F.2d 787 (Fed. Cir. 1988); *Isadore & Miriam Klein*, 84-2 B.C.A. (CCH) ¶ 17,273 at 86,004 (1984) (finding that the government agency breached its good faith duty when it used a mistaken statutory limit during price negotiations).<REF ID='FN74'>[fm][eb]

<sup>101</sup> See *supra* notes <CITE ID='FN46'>-<CITE ID='FN71'> and accompanying text.<REF ID='FN308A'>[fm][eb]

<sup>102</sup> See *supra* notes <CITE ID='FN32'>-<CITE ID='FN33'> and accompanying text.<REF ID='FN308B'>[fm][eb]

<sup>103</sup> BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 91.<REF ID='FN75'>[fm][eb]

<sup>104</sup> *Id.* at 91-92.<REF ID='FN309A'>[fm][eb]

<sup>105</sup> *Id.* at 93.<REF ID='FN76'>[fm][eb]

<sup>106</sup> *Id.* at 94-95. Burton and Andersen are careful to note that the good faith doctrine does not convert a terminable-at-will contract into a contract that can only be terminated for "good cause." *Id.* at 93-94. Rather, the parties reserve broad discretion in such a situation, but not such discretion that the justified expectations of the parties can be violated. *Id.*<REF ID='FN77'>[fm][eb]

<sup>107</sup> 732 P.2d 1364 (Nev. 1987).<REF ID='FN78'>[fm][eb]

<sup>108</sup> *Id.* at 1365.<REF ID='FN78A'>[fm][eb]

<sup>109</sup> *Id.* at 1373. The court also found this conduct to be in subjective bad faith and, therefore, awarded punitive damages. *Id.*<REF ID='FN79'>[fm][eb]

<sup>110</sup> 445 F. Supp. 927 (S.D. Tex. 1978).<REF ID='FN80'>[fm][eb]

<sup>111</sup> *Id.* at 938-39.<REF ID='FN81'>[fm][eb]

<sup>112</sup> See, e.g., *Caton v. Leach Corp.*, 896 F.2d 939, 946-47 (5th Cir. 1990) (holding that, under California law, an employer violates the covenant of good faith when it denies an employee benefits allocated under a contract); *Mitford v. de Lasala*, 666 P.2d 1000, 1006-07 (Alaska 1983) (finding bad faith when an employer fired its employee to prevent him from sharing in future profits); *Maddaloni v. Western Mass. Bus Lines, Inc.*, 438 N.E.2d 351, 356 (Mass. 1982) ("An employer may not discharge an employee in order to avoid the payment of commissions or to reap for itself financial benefits due its employee."); *Hall v. Farmers Ins. Exch.*, 713 P.2d 1027, 1031 (Okla. 1985) ("[A] principal may not unfairly deprive his agent of the fruits of that agent's own labor by a wrongful, unwarranted resort to a clause in the agency contract which provides for termination at will."). Other courts have found public policy exceptions to an employer's discretion to terminate an at-will employee. See, e.g., *McClendon v. Ingersoll-Rand Co.*, 779 S.W.2d 69, 71 (Tex. 1989) (holding that firing an employee to avoid making a contribution to the pension fund is actionable when public policy supports such funds).<REF ID='FN82'>[fm][eb]

terminating the contract in whole or in part) when the market price falls below the contract price;<sup>113</sup> an output seller cannot reduce its output because a contract becomes unprofitable;<sup>114</sup> a lender improperly tries to recapture opportunities foregone at the time of contracting when it terminates a construction line of credit because it decides to stop making construction loans generally;<sup>115</sup> and a party breaches the covenant of good faith when it indirectly terminates a contract by taking actions to undermine the business arrangement so as to make more money by pursuing other deals.<sup>116</sup>

This is not to say that parties in their agreement cannot give each other broad discretion to terminate.<sup>117</sup> In such cases, the implied covenant of good faith should not be used "as a tool for rewriting the parties' Agreement based on unspecified notions of fairness."<sup>118</sup> Nevertheless, "too quick a reliance on express terms, literally construed, can do violence to the intentions and reasonable expectations of the parties."<sup>119</sup> Rather, express terms must be "interpreted in accordance with any course of performance, course of dealing, usage of trade, and similar contextual features shaping the reasonable expectations of the parties arising from their promises."<sup>120</sup>

2. *Application of Common Law Principles to Government Contracts.*--Application of common law precedent to the federal contracts termination setting would eliminate confusion in the federal law by imposing the same duties on a government agency as are imposed on a private contracting party. Application of the common law would (1) impose an objective, rather than a subjective, test of whether the government acted in good faith, reaffirming that the government does not have discretion to walk away from its bargains with impunity; (2) reject the implication in some cases that the government must premeditate a contract breach in order to abuse its termination discretion; (3) eliminate the well-nigh irrefragable standard imposed only on those contracting with the government; and (4) provide a firmer conceptual framework for those cases finding bad faith by the government in terminating.

a. *Subjective Bad Faith.*--The plurality opinion in *Torncello* is consistent with common law good faith precedent in many respects. The explication of the purposes and understandings of the parties with respect to the use of termination-for-convenience clauses provides the substance of the justified expectations of the parties. Moreover, common law precedent would not permit the termination-for-convenience clause to be used to remake the contract simply to get out of a bad deal or to take advantage of a better deal, whether known before or discovered after the contract was executed.<sup>121</sup> Common law precedent also supports the conclusion that, if the termination-for-convenience clause gives the government an unfettered right of exculpation, the contract is illusory, a contract interpretation not favored in the law.<sup>122</sup>

The *Torncello* plurality deviated from common law precedent in an important respect by continuing to adhere to the rule that, in order to upset the government's termination for convenience, a contractor must show that the government acted in *subjective* bad faith.<sup>123</sup> In order to denigrate the government's ability to provide effective consideration for a

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<sup>113</sup>BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 135-36 (citing Loudonback Fertilizer Co. v. Tennessee Phosphate Co., 121 F. 298 (6th Cir. 1903)).<REF ID='FN83'>[fm][eb]

<sup>114</sup>*Id.* at 136 (citing Empire Gas Corp. v. American Bakeries Co., 840 F.2d 1333 (7th Cir. 1988); Feld v. Henry S. Levy & Sons, Inc., 335 N.E.2d 320 (N.Y. 1975)).<REF ID='FN84'>[fm][eb]

<sup>115</sup>BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 161-62 (citing First Nat'l Bank v. Sylvester, 554 N.E.2d 1063 (1990)).<REF ID='FN85'>[fm][eb]

<sup>116</sup>See Hilton Hotels Corp. v. Butch Lewis Prods., Inc., 808 P.2d 919, 924 (Nev. 1991); Sons of Thunder, Inc. v. Borden, Inc., No. A-37, 1997 WL 104592, at \*14-16 (N.J. Mar. 11, 1997).<REF ID='FN86'>[fm][eb]

<sup>117</sup>See *Torncello v. United States*, 681 F.2d 756, 771 (Ct. Cl. 1982) (en banc).<REF ID='FN87'>[fm][eb]

<sup>118</sup>*General Aviation, Inc. v. Cessna Aircraft Co.*, 703 F. Supp. 637, 644 (W.D. Mich. 1988).<REF ID='FN88'>[fm][eb]

<sup>119</sup>BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 145.<REF ID='FN89'>[fm][eb]

<sup>120</sup>*Id.* at 130; see also RESTATEMENT (SECOND) OF CONTRACTS § 203 (1981) ("[E]xpress terms are given greater weight than course of performance, course of dealing, and usage of trade.").<REF ID='FN90'>[fm][eb]

<sup>121</sup>BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 80.<REF ID='FN90B'>[fm][eb]

<sup>122</sup>See *United States v. Winstar Corp.*, 116 S. Ct. 2432, 2477 (1996) (Scalia, J., concurring in the judgment) (interpreting a government contract in order to prevent it from being illusory); *Walsh v. Schlecht*, 429 U.S. 401, 408 (1977) (noting that a general rule of construction presumes the legality and enforceability of contracts); *Maxima Corp. v. United States*, 847 F.2d 1549, 1557 (Fed. Cir. 1988) (stating that, if possible, a government contract will not be construed to lack consideration and mutuality).<REF ID='FN91'>[fm][eb]

<sup>123</sup>*Torncello v. United States*, 681 F.2d 756, 772 (Ct. Cl. 1982) (plurality opinion) (en banc). The Court of Federal Claims recently read post-*Torncello* Federal Circuit precedent to require actual subjective bad faith by the procurement officials involved. See *Advanced Materials, Inc. v. United States*, 34 Fed. Cl. 480, 482-83 (1995).<REF ID='FN92'>[fm][eb]

termination-for-convenience right,<sup>124</sup> the plurality painted in the starkest possible terms the difficulty a contractor faces in proving subjective bad faith.<sup>125</sup> What the *Torncello* plurality should have done was recognize that the government has the same good faith duties as a private party and that the government cannot exercise its discretion to terminate contrary to the justified expectations of the parties, or to recapture an opportunity foreclosed at the time of contracting.<sup>126</sup> These justified expectations might very well not substantially confine the government, as the government's discretion to terminate is stated broadly.<sup>127</sup> Nevertheless, the good faith limits extend at least so far as not to permit the government to get out of a deal merely because its bargain might have turned sour or because it can avail itself of an even better opportunity to acquire the same goods or services.

Although the government has retained broad discretion to terminate under the standard termination-for-convenience clause when it is in its interest to do so, the government's obligation of good faith still restricts the exercise of that discretion to the justified expectations of the parties.<sup>128</sup> Government contractors acquire their justified expectations, at least in part, from the purpose of the standard termination-for-convenience clause. That purpose, as noted by the *Torncello* plurality, is to deal with changed or unexpected circumstances relating to the need for the product or services.<sup>129</sup> Unless the parties expressly so state in their agreement, however, those expectations should never be assumed to include the right to avoid the contract simply because it turned out to be a bad bargain or because an even better bargain came along.<sup>130</sup>

Supreme Court precedent amply supports this conclusion. In *United States v. Mississippi Valley Generating Co.*,<sup>131</sup> the Court stated: "Of course, the Government could not avoid the contract merely because it turned out to be a bad bargain."<sup>132</sup> Common law and common sense, as well as equity, lead to the same conclusion.<sup>133</sup>

*b. Premeditated Breach.*--In his *Torncello* concurrence, Judge Davis suggested that it might be appropriate for the government to use the termination-for-convenience clause to take advantage of a better deal that later

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<sup>124</sup>As Judge Davis pointed out, the *Torncello* plurality probably exaggerated the difficulty a contractor faces in trying to prove subjective bad faith in an attempt to negative any effective consideration. *Torncello*, 681 F.2d at 773-74 (Davis, J., concurring in the result).<REF ID=FN93>[fm][eb]

<sup>125</sup>*Id.* at 767-77 (plurality opinion).<REF ID=FN329A>[fm][eb]

<sup>126</sup>While Judge Bennett, writing for the *Torncello* plurality, stated that "the government's obligation to act in good faith hardly functions as the meaningful obligation that it may be for private persons," he defined the government's "good faith" obligation, based on his reading of prior precedent, as solely not to act in *subjective* bad faith. *Id.* at 771 (plurality opinion). In that sense, Judge Bennett was right that a good faith obligation defined in such a restrictive sense is inconsistent with common law precedent governing private parties. The appropriate common law rule, which should be applied in the federal contracting context as well, is illustrated in *Martin v. Prier Brass Manufacturing Co.*, 710 S.W.2d 466 (Mo. Ct. App. 1986). In *Martin*, the court held that a contract giving the ultimate power of interpretation to one party does not make an executed contract illusory because that power must be exercised in good faith so as not "to evade the spirit of the transaction or . . . deny the other party the expected benefit of the contract." *Id.* at 473; *cf.* *Aviation Contractor Employees, Inc. v. United States*, 945 F.2d 1568, 1572 (Fed. Cir. 1991) (stating that a contract with uncertain terms to be decided at a later date is sufficiently defined because the parties have an implied duty to negotiate in good faith).<REF ID=FN94>[fm][eb]

<sup>127</sup>See *supra* notes <CITE ID=FN39A>-<CITE ID=FN40> and accompanying text.<REF ID=FN331A>[fm][eb]

<sup>128</sup>*Torncello*, 681 F.2d at 771 (plurality opinion).<REF ID=FN94A>[fm][eb]

<sup>129</sup>The *Torncello* plurality stated:

[C]onvenience termination, as it was developing, was intended just to handle changed conditions, relieving the government of the risk of receiving obsolete or useless goods. . . . The contractor risked losing the full benefit of his performance if something occurred, *apart from the bargain and the expectations of the parties*, that made continuance of the contract clearly inadvisable.

*Id.* at 765-66 (emphasis added).<REF ID=FN96>[fm][eb]

<sup>130</sup>See *id.* at 772 (stating that the government may not terminate a contract to obtain a better price of which it had knowledge at the time the contract was formed); *Municipal Leasing Corp. v. United States*, 7 Cl. Ct. 43, 47 (1984) ("The termination for convenience clause can appropriately be invoked only in the event of some kind of change from the circumstances of the bargain or in the expectations of the parties."); *Tamp Corp.*, 84-2 B.C.A. (CCH) ¶ 17,460 at 86,977-78 (1984) (finding that the government did not act in good faith when it extended a contract for two months with the knowledge that it would terminate a month later when a better price would become available). If an agreement permitted the government an "out" for any and every reason, however, the agreement would likely fail for want of mutuality of obligation. See *Torncello*, 681 F.2d at 769 (plurality opinion) ("It is hornbook law . . . that a route of complete escape vitiates any other consideration furnished and is incompatible with the existence of a contract." (citing 1 SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 104 (3d ed. 1957); 1 ARTHUR LINTON CORBIN, CORBIN ON CONTRACTS § 145 (1963))).<REF ID=FN95>[fm][eb]

<sup>131</sup>364 U.S. 520 (1961).<REF ID=FN97>[fm][eb]

<sup>132</sup>*Id.* at 565-66 (citing *Muschany v. United States*, 324 U.S. 49, 66-67 (1945)).<REF ID=FN98>[fm][eb]

<sup>133</sup>BURTON & ANDERSEN, *supra* note <CITE ID=FN6>, at 91-95.<REF ID=FN99>[fm][eb]



came to its attention.<sup>134</sup> More recently, in *Caldwell Santmyer, Inc. v. Glickman*<sup>135</sup> and *Krygoski Construction Co. v. United States*,<sup>136</sup> the Federal Circuit similarly suggested that the government has not breached its duty of good faith unless it knew "full well," at the time of contracting, that it would not honor the contract.<sup>137</sup> These suggestions run directly counter to the common law and would allow the government to get out of a deal whenever it wants to do so. Either such a broad "right" to terminate will always be in violation of the justified expectations of the parties, or no contract will exist because it is illusory.<sup>138</sup>

It is conceded in government contracts law that having a preconceived intent to breach the contract is to terminate in *subjective* bad faith.<sup>139</sup> When the *objective* test of good faith duties is applied, however--measuring the discretion-exercising party's conduct by the justified expectations of the parties--the moment when a party forms the improper intent to abuse its discretion is no more relevant to a breach of the covenant of good faith than it is to the breach of any other contractual covenant.<sup>140</sup>

No party would be allowed to escape the consequences of a typical breach by arguing that it did not intend to breach at the time of contracting, even though it later did so, either innocently or intentionally.<sup>141</sup> The same rule should apply to a breach of the covenant of good faith in the government contracts termination context.

c. *Well-Nigh Irrefragable Proof.*--In the termination of contracts, an acknowledgement that the government is subject to the same good faith duties as a private party would eliminate the well-nigh irrefragable burden of proof now imposed on government contractors. This burden of proof has been imposed only when the good faith duties of the government have been equated with not acting in *subjective* bad faith.<sup>142</sup> Government contractors have not been required to show subjective bad faith in other situations involving good faith duties.<sup>143</sup>

Even under a continuing subjective-bad-faith regime, the well-nigh irrefragable standard has little to commend it except its frequent repetition. Well-nigh irrefragable (or in more common parlance, "almost indisputable") is not a standard commonly found in the law and is not a standard that has been defined, except on a case-by-case basis, in government contracts law.<sup>144</sup> Although commentators have suggested that well-nigh irrefragable is the functional equivalent of a "clear and convincing" standard,<sup>145</sup> the case law has not made that identification.

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<sup>134</sup> *Torncello*, 681 F.2d at 774 (Davis, J., concurring in the result).<REF ID='FN100'>[fm][eb]

<sup>135</sup> 55 F.3d 1578 (Fed. Cir. 1995).[fm][eb]

<sup>136</sup> 94 F.3d 1537 (Fed. Cir. 1996), *cert. denied*, 65 U.S.L.W. 3571 (U.S. May 12, 1997) (No. 96-1236).[fm][eb]

<sup>137</sup> *Caldwell*, 55 F.3d at 1582; *Krygoski*, 94 F.3d at 1544.<REF ID='FN101'>[fm][eb]

<sup>138</sup> See *Torncello*, 681 F.2d at 768-69 (plurality opinion); see also RESTATEMENT (SECOND) OF CONTRACTS § 77 (1981) ("A promise or apparent promise is not consideration if by its terms the promisor or purported promisor reserves a choice of alternative performances.")<REF ID='FN102'>[fm][eb]

<sup>139</sup> See *Caldwell*, 55 F.3d at 1582.<REF ID='FN103'>[fm][eb]

<sup>140</sup> Only two of the six *Torncello* judges rested their decisions on the basis that the agency had premeditated the breach. See *Torncello*, 681 F.2d at 773 (Friedman, C.J., concurring); *id.* at 773-74 (Davis, J., concurring in the result). That basis was, however, defined (incorrectly) by the Federal Circuit as the central rationale of the decision. See *Krygoski*, 94 F.3d at 1541-42 (stating that *Torncello* "overruled *Colonial Metals* because the Navy used the termination for convenience clause to escape a promise it never had an intention to keep")<REF ID='FN104'>[fm][eb]

<sup>141</sup> See, e.g., *Ideker, Inc. v. Missouri State Highway Comm'n*, 654 S.W.2d 617, 624 (Mo. Ct. App. 1983) (stating that *scienter* is not an element of a cause of action for breach of contract warranty).<REF ID='FN105'>[fm][eb]

<sup>142</sup> See *supra* notes <CITE ID='FN92'>--<CITE ID='FN331A'> and accompanying text.<REF ID='FN105A'>[fm][eb]

<sup>143</sup> See, e.g., *Malone v. United States*, 849 F.2d 1441, 1445 (Fed. Cir.) (holding that a government contracting officer's evasiveness and resulting interference with the contractor's performance amounted to a material breach of contract), *modified*, 857 F.2d 787 (Fed. Cir. 1988); *Neal & Co., Inc. v. United States*, 36 Fed. Cl. 600, 631 (1996) (finding that the government's failure to issue a timely direction can breach the duty to cooperate); Thomas S. Rhoades & Stephen L. Schluneger, 95-1 B.C.A. (CCH) ¶ 27,375 at 136,436-37 (1994) (affirming that the government has an affirmative duty to cooperate with the contractor); see also *Marine Constr. & Dredging, Inc.*, 95-1 B.C.A. (CCH) ¶ 27,286 at 136,026 (1994) (recognizing that proving subjective bad faith "requires more than showing that the contracting officer breached duties of 'good faith' and 'fair dealing' in administering the contract")<REF ID='FN106'>[fm][eb]

<sup>144</sup> See *infra* notes <CITE ID='FN108'>--<CITE ID='FN157'> and accompanying text.<REF ID='FN106A'>[fm][eb]

<sup>145</sup> See, e.g., *Toomey et al.*, *supra* note <CITE ID='FN26'>, at 92 (stating that by "well-nigh irrefragable," *Knotts v. United States*, 121 F. Supp. 630 (Ct. Cl. 1954), the court seemed to mean that contractors have the burden of showing bad faith by clear and convincing evidence).<REF ID='FN107'>[fm][eb]

The well-nigh irrefragable standard found its initial expression in the 1954 Court of Claims decision of *Knotts v. United States*<sup>146</sup>—an employee discharge case.<sup>147</sup> The standard has since been applied in more common government contracts cases without critical discussion.<sup>148</sup> The only scrap of rationale provided by the case law for this higher, but largely undefined, well-nigh irrefragable standard is that government agents are presumed to act in good faith.<sup>149</sup> The supposed distinction between government agents and private actors, however, is unfounded.<sup>150</sup> Private parties are also presumed to act in good faith, and as is true with respect to other alleged contract breaches, the party asserting the breach of good faith duties has the burden of proof.<sup>151</sup> Indeed, in other government contracts situations in which the government is held to good faith duties, although the burden is on the contractor to show a breach of those duties, a well-nigh irrefragable standard is rightfully not imposed.<sup>152</sup>

Most important, imposing a heightened, well-nigh irrefragable standard cannot be squared with the bedrock principle that the United States, upon entering the marketplace, is held to the same standards as a private citizen.<sup>153</sup> Further, imposing a heightened standard on the contractor runs contrary to those decisions which properly hold that, if anything, the government should be held to higher good faith duties than a private party, considering its power in the marketplace and its status as representative of the people.<sup>154</sup> The government has "an ever present obligation to perform its duties under a contract reasonably and in good faith,"<sup>155</sup> and it "must be held to the same general principles of equity and fair play in dealing with those who contract with it as are the contractors themselves."<sup>156</sup> The well-nigh irrefragable standard does not define the duties of private contractors, and neither should it define the duties of the government as a contracting party.

*d. Existing Federal Precedent.*—This is not to say that those cases which have found the government to have acted in subjective bad faith or to have abused its discretion in a termination setting have been wrongly decided or that they are wholly irrelevant. Under the common law, wrongful motives may well indicate a breach of good faith duties,<sup>157</sup> although an absence of wrongful reasons "does not suffice to establish good faith because bad faith may also

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<sup>146</sup> 121 F. Supp. 630 (Ct. Cl. 1954).<REF ID=FN108>[fm][eb]

<sup>147</sup> *Id.* at 630.<REF ID=FN108A>[fm][eb]

<sup>148</sup> See, e.g., *Caldwell & Santmyer, Inc. v. Glickman*, 55 F.3d 1578, 1581 (Fed. Cir. 1995) (reciting the well-nigh irrefragable proof standard without analysis); *Torncello v. United States*, 681 F.2d 756, 770-71 (Ct. Cl. 1982) (plurality opinion) (en banc) (same); *Kalvar Corp. v. United States*, 543 F.2d 1298, 1301-02 (Ct. Cl. 1976) (same).<REF ID=FN109>[fm][eb]

<sup>149</sup> See *Caldwell*, 55 F.3d at 1581 ("We assume the government acts in good faith when contracting."); *Torncello*, 681 F.2d at 770 (plurality opinion) (stating that "the government, unlike private parties, is assumed always to act in good faith"); *Librach v. United States*, 147 Ct. Cl. 605, 612 (1959) ("[I]n the absence of clear evidence to the contrary, it must be presumed that the public officials involved in the termination of the plaintiffs' contract were acting conscientiously . . . when the contract was terminated for the purported convenience of the Government.")<REF ID=FN110>[fm][eb]

<sup>150</sup> No common law precedent is cited in the government contracts cases for the incorrect premise that private contractors are not presumed to act in good faith.<REF ID=FN112>[fm][eb]

<sup>151</sup> BURTON & ANDERSEN, *supra* note <CITE ID=FN6>, at 107. Recently, the Court of Federal Claims in *Huna Totem Corp. v. United States*, 35 Fed. Cl. 603 (1996), while uncritically applying the well-nigh irrefragable standard, also correctly noted that "there is a presumption that both parties have fulfilled their duties of good faith and fair dealing." *Id.* at 613.<REF ID=FN113>[fm][eb]

<sup>152</sup> See, e.g., *Malone v. United States*, 849 F.2d 1441, 1445 (Fed. Cir.) (imposing the common law preponderance standard on a contractor to prove the government's breach of good faith duties during performance and not discussing the well-nigh irrefragable standard), *modified*, 857 F.2d 787 (Fed. Cir. 1988); *Pacific Far East Line, Inc. v. United States*, 394 F.2d 990, 998 (Ct. Cl. 1968) (per curiam) (adopting the opinion of the trial commissioner that the government must exercise its contractual discretion reasonably and not arbitrarily or capriciously); see also Toomey et al., *supra* note <CITE ID=FN26>, at 118-24 (discussing the importance of *Malone* and government contracts tribunals not using the well-nigh irrefragable proof standard in nontermination cases).<REF ID=FN114>[fm][eb]

<sup>153</sup> See *supra* notes <CITE ID=FN1>—<CITE ID=FN3> and accompanying text.<REF ID=FN354A>[fm][eb]

<sup>154</sup> See, e.g., *Corliss Steam-Engine Co. v. United States*, 10 Ct. Cl. 494, 502 (1874) (noting that the government must deal with a contractor "in the strictest fairness and justice"), *aff'd*, 91 U.S. 321 (1875); *R & R Enters.*, 89-2 B.C.A. (CCH) ¶ 21,708 at 109,148 (1989) ("[B]ecause of its size, power, and potential ability to manipulate the market place, the Government may have obligations of fairness beyond those of the ordinary citizen.")<REF ID=FN115>[fm][eb]

<sup>155</sup> *ASCO-Falcon II Shipping Co. v. United States*, 18 Cl. Ct. 484, 492 (1989).<REF ID=FN116>[fm][eb]

<sup>156</sup> *Kemp v. United States*, 38 F. Supp. 568, 570 (D. Md. 1941).<REF ID=FN117>[fm][eb]

<sup>157</sup> BURTON & ANDERSEN, *supra* note <CITE ID=FN6>, at 77.<REF ID=FN117A>[fm][eb]

consist of action for reasons that are disallowed by the contract even though not wrongful."<sup>158</sup> Many government contracts tribunals have reached an appropriate result under common law precedent by finding that when the government terminates just to avail itself of a better deal, it violates the "subjective bad faith/abuse of discretion" standard.

In *Municipal Leasing Corp. v. United States*,<sup>159</sup> for example, the Air Force had expressed its binding intent to purchase computer terminals for a base year and for option years from the contractor.<sup>160</sup> At the time of contracting, the Air Force had rejected the alternative of repairing its existing Hazeltine terminals.<sup>161</sup> After the base year, the Air Force breached its obligation by not seeking additional funding to allow exercise of the option and by pursuing, instead, the repair of the Hazeltine terminals.<sup>162</sup> The court rejected the Air Force's attempt to justify its conduct under a constructive termination theory:

The termination for convenience clause can appropriately be invoked only in the event of some kind of change from the circumstances of the bargain or in the expectations of the parties. In this instance, the government promised that it would not replace the leased terminals with functionally equivalent equipment. . . . The termination for convenience clause will not act as a constructive shield to protect [the government] from the consequences of its decision to follow an option considered but rejected before contracting with plaintiff.<sup>163</sup>

Moreover, government contracts tribunals' various formulations of subjective bad faith--"specific intent to injure" the contractor,<sup>164</sup> actions "motivated alone by malice,"<sup>165</sup> and "designedly oppressive" conduct<sup>166</sup>--when properly construed, all come into play when the government attempts to recapture opportunities knowingly given up at the time of contracting. For example, the ASBCA found "specific intent to injure" a contractor when Navy personnel disagreed with the decision to privatize what had been an operation handled by Navy employees and wanted the old regime reinstated.<sup>167</sup> The Board found that the Navy personnel acted in subjective, as well as objective, bad faith by sabotaging the private contractor's performance, even though the Navy employees were not motivated by animosity toward the particular contractor.<sup>168</sup> Indeed, while malice connotes willfulness, it does not require personal ill will, but merely intentional action for a wrongful purpose to gain some advantage at the other party's expense.<sup>169</sup> Thus, in many instances, applying the subjective bad faith/abuse of discretion standard will yield the same result as applying common law precedent.

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<sup>158</sup> *Id.* at 77-78.<REF ID=FN118>[fm][eb]

<sup>159</sup> 7 Cl. Ct. 43 (1984).<REF ID=FN119>[fm][eb]

<sup>160</sup> *Id.* at 44.<REF ID=FN119A>[fm][eb]

<sup>161</sup> *Id.*<REF ID=FN119C>[fm][eb]

<sup>162</sup> *Id.*<REF ID=FN119C>[fm][eb]

<sup>163</sup> *Id.* at 47 (citations omitted); see also *Operational Serv. Corp.*, 93-3 B.C.A. (CCH) ¶ 26,190 at 130,374 (1993) (disallowing a termination when the agency switched to another company of which it had full knowledge at the time of contracting); *Tamp Corp.*, 84-2 B.C.A. (CCH) ¶ 17,460 at 86,977-78 (1984) (setting aside an attempted termination for convenience when the agency and the contractor specifically negotiated for a two-month extension and the agency then terminated after one month).<REF ID=FN120>[fm][eb]

<sup>164</sup> See *Kalvar Corp. v. United States*, 543 F.2d 1298, 1301-02 (Ct. Cl. 1976).<REF ID=FN121>[fm][eb]

<sup>165</sup> See *id.*; *Marine Constr. & Dredging, Inc.*, 95-1 B.C.A. (CCH) ¶ 27,286 at 136,026 (1994); *Apex Int'l Management Servs., Inc.*, 94-2 B.C.A. (CCH) ¶ 26,842 at 133,550, *aff'd on reconsideration*, 94-2 B.C.A. (CCH) ¶ 26,852 at 133,622 (1994).<REF ID=FN122>[fm][eb]

<sup>166</sup> See *Kalvar*, 543 F.2d at 1302; *Struck Constr. Co. v. United States*, 96 Ct. Cl. 186, 220-22 (1942); *Marine Constr.*, 95-1 B.C.A. (CCH) at 136,026; *Apex*, 94-2 B.C.A. (CCH) at 133,550.<REF ID=FN123>[fm][eb]

<sup>167</sup> See *Apex*, 94-2 B.C.A. (CCH) at 133,550.<REF ID=FN123A>[fm][eb]

<sup>168</sup> See *id.* at 133,548-50.<REF ID=FN124>[fm][eb]

<sup>169</sup> See *Bitterman v. Louisville & Nashville R.R.*, 207 U.S. 205, 223 (1907) (stating that personal ill will is not required for malice in law, only wanton disregard of the rights of the other to gain personal advantage); *Getschow v. Commonwealth Edison Co.*, 444 N.E.2d 579, 584 (Ill. App. Ct. 1982) ("It is also well settled that 'malice,' when used in this context, does not require a showing of ill will, hostility or an intent to injure."), *aff'd in part and rev'd in part*, 459 N.E.2d 1332 (Ill. 1984); *Coleman v. Whisnant*, 35 S.E.2d 647, 656 (N.C. 1945) ("The word 'malicious' used in referring to malicious interference with formation of a contract does not import ill will, but refers to an interference with design of injury to plaintiff or gaining some advantage at his expense."); see also *In re Posta*, 866 F.2d 364, 367-68 (10th Cir. 1989) (stating that "malicious" intent under the Bankruptcy Code may be proven by either direct evidence of specific intent to injure or, "[m]ore commonly, . . . by evidence that the debtor had knowledge of the creditor's rights and . . . proceeded to take action in violation of those rights"); *Morey v. Page*, 802 S.W.2d 779, 787 (Tex. App. 1990) (finding that knowing conversion of property is malicious); *BALLENTINE'S LAW DICTIONARY* 768 (3d ed. 1969) (defining malice as an "improper motive, not necessarily positive malignity; a wilful disregard of the rights of another, whether in accomplishing an unlawful purpose or a lawful purpose by an unlawful means"); *BLACK'S LAW DICTIONARY* 956-57 (6th ed. 1990) ("Malice in law is not necessarily personal hate or ill will.").<REF ID=FN125>[fm][eb]

e. *Summary*.--The law governing termination of government contracts should conform with the general principle that the government has the same rights and responsibilities as a private party.<sup>170</sup> The law should expressly recognize that when the government exercises its discretion to terminate for convenience it must exercise that discretion in good faith, as defined in the common law.

Whether the government acted in subjective bad faith, although often relevant, is not the dispositive inquiry. The proper test is an objective one: If the government terminates within its discretion as defined by the justified expectations of the parties at the time they made their bargain, the termination is in good faith; if the government tries to recapture an opportunity foreclosed at the time of contracting, it acts in bad faith.

Whether the government contemplated breaching its good faith duties in advance of contracting is also not dispositive of the inquiry. A party does not have to premeditate a breach before actually forming a contract in order to be found later to have breached its obligations, regardless of whether the party breached innocently or intentionally. This recent, restrictive reading of *Torncello v. United States*<sup>171</sup> by the Federal Circuit<sup>172</sup> most probably stems from the fact that the specialized government contracts tribunals have not articulated a proper theoretical framework for limiting the government's exercise of discretion in termination situations--a theoretical framework that common law contractual good faith precedent provides.<sup>173</sup>

In *Caldwell Santmyer, Inc. v. Glickman*,<sup>174</sup> the Federal Circuit correctly held that the government's discretion to terminate for convenience is not restricted merely because the government is on notice that "at some future date, it may be appropriate to terminate the contract for convenience."<sup>175</sup> The government retains its discretion to terminate for convenience even though it might be able to prognosticate in general the reasons that such a termination might later legitimately be exercised.<sup>176</sup> Nevertheless, the government's discretion, like that of a private party, should be limited by good faith, as defined by the reasonable expectations of the parties at the time of contracting. Like a private party, the government cannot, consistent with good faith duties, recapture an opportunity foreclosed at the time of contracting.<sup>177</sup>

Finally, the well-nigh irrefragable proof standard imposed on government contractors should be scuttled because it lacks adequate precedential, philosophical, or policy underpinning. The government contractor, like an aggrieved party to a private contract, bears the burden of proving a breach of good faith and most other contractual covenants. The government does not stand on a special pedestal when it enters the marketplace.<sup>178</sup> It stands on the level of the citizens with whom it contracts: "The United States are as much bound by their contracts as are individuals. If they repudiate their obligations, it is as much repudiation, with all the wrong and reproach that term implies, as it would be if the repudiator had been a State or a municipality or a citizen."<sup>179</sup>

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<sup>170</sup> See *United States v. Winstar Corp.*, 116 S. Ct. 2432, 2464-65 (1996) (plurality opinion).<REF ID='FN126'>[fm][eb]

<sup>171</sup> 681 F.2d 756 (Ct. Cl. 1982) (en banc).[fm][eb]

<sup>172</sup> See *Krygoski Constr. Co. v. United States*, 94 F.3d 1537, 1545 (Fed. Cir. 1996) (reading *Torncello* to hold that the government does not act in bad faith unless it enters a contract with the intention of invoking the termination-for-convenience clause for known conditions already in being), *cert. denied*, 65 U.S.L.W. 3571 (U.S. May 12, 1997) (No. 96-1236); *Caldwell & Santmyer, Inc. v. Glickman*, 55 F.3d 1578, 1582 (Fed. Cir. 1995) (reading *Torncello* similarly in dicta).<REF ID='FN127'>[fm][eb]

<sup>173</sup> BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 52-60.<REF ID='FN127B'>[fm][eb]

<sup>174</sup> 55 F.3d 1578 (Fed. Cir. 1995).[fm][eb]

<sup>175</sup> *Id.* at 1582.<REF ID='FN128'>[fm][eb]

<sup>176</sup> See *Krygoski*, 94 F.3d at 1544-45.<REF ID='FN129'>[fm][eb]

<sup>177</sup> BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 45, 52-57. In *Nesbitt v. United States*, 345 F.2d 583 (Ct. Cl. 1965), as in *Colonial Metals Co. v. United States*, 494 F.2d 1355 (Ct. Cl. 1974) (per curiam), the Court of Claims apparently validated an agency's ability simply to walk away from its requirements contract. *Nesbitt*, 345 F.2d at 586. A close reading of the facts in *Nesbitt* reveals, however, that the contractor was unable and unwilling to meet the agency's total requirements. See *id.* Therefore, a partial constructive termination by placing some of the work elsewhere was appropriate. See *id.* at 586 n.3.<REF ID='FN130'>[fm][eb]

<sup>178</sup> See *Cooke v. United States*, 91 U.S. 389, 398 (1875) (stating that when the United States "comes down from its position of sovereignty, and enters the domain of commerce, it submits itself to the same laws that govern individuals there").<REF ID='FN131'>[fm][eb]

<sup>179</sup> *Sinking Fund Cases*, 99 U.S. 700, 719 (1879). The Court in *Lynch v. United States*, 292 U.S. 571 (1934), similarly declared:

Punctilious fulfillment of contractual obligations is essential to the maintenance of the credit of public as well as private debtors. No doubt there was in March, 1933, great need of economy. In the administration of all government business economy had become urgent because of lessened revenues and the heavy obligations to be issued in the hope of relieving widespread distress. Congress was free to reduce gratuities deemed excessive. But Congress was without power to reduce expenditures by abrogating contractual obligations of the United States. To abrogate contracts, in the attempt to lessen government expenditure, would be not the practice of economy, but an act of repudiation.

(continued...)



## II. GOOD FAITH IN THE FORMATION OF GOVERNMENT CONTRACTS

The other area in which government contracts law has deviated from the common law of good faith duties is contract formation. Government contracts law recognizes, as does the common law, good faith duties in the negotiation of agreements.<sup>180</sup> Yet federal tribunals have stopped short of affording government contractors the full relief to which they are entitled when the government fails to negotiate a contract in good faith.

### A. Common Law Good Faith Duties in Contract Negotiation and Formation

American law imposes no general duty to negotiate a contract in good faith . . . . [American courts] continue to view contract negotiations as, at bottom, an undertaking in which self-interest is the accepted norm. Each party assumes the risk that, despite a heavy investment in the negotiation process, no agreement will be reached.<sup>181</sup>

This American rule of law that good faith duties do not pertain during precontract negotiations is often modified by "preliminary agreements" between the parties.<sup>182</sup> A preliminary agreement is "one made during bargaining on the assumption that further negotiations will take place and result in a later, final contract."<sup>183</sup> Burton and Andersen note that, "in most cases, preliminary agreements include at least an implicit obligation to make efforts to reach that further agreement . . . . [S]uch agreements set out procedural rules for subsequent negotiations, or settle (even if only for purposes of negotiation) some of the substantive terms of the final contract, or both."<sup>184</sup> The parties must, of course, intend to be bound by their preliminary agreement for it to have contractual effect,<sup>185</sup> and even if they intend to be bound, their contract is not enforceable if it is so indefinite that, should the court enforce it, it would lock the parties into "surprise contractual obligations that they never intended."<sup>186</sup> Although Burton and Andersen hold as the "better view . . . that a general duty to negotiate, without more, is too indefinite to be enforced,"<sup>187</sup> the more the parties delineate procedural rules and define specific terms in their preliminary agreement, the more likely the agreement is to be definite and enforceable with attendant good faith duties: "When the parties have agreed to treat some final contract terms as settled, the good faith performance obligation supplies workable boundaries to the general duty to negotiate. It provides a well-developed means of distinguishing performance from breach, satisfying the requirement of definiteness."<sup>188</sup>

In order to calculate the measure of damages for breach of a preliminary agreement, Professor Farnsworth has argued that "expectation" damages (lost profits) are always inappropriate because the parties were foreclosed from entering into the "larger agreement" by the breach of the preliminary agreement.<sup>189</sup> He argues that as there is "no way of knowing what the terms of the ultimate agreement would have been, or even whether the parties would have arrived at an

(...continued)

*Id.* at 580.<REF ID='FN132'>[fm][eb]

<sup>180</sup> See *supra* notes <CITE ID='FN1'>-<CITE ID='FN5'> and accompanying text.<REF ID='FN132A'>[fm][eb]

<sup>181</sup> BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 330-31. Burton and Andersen cite as illustrative the following passage from *Feldman v. Allegheny International, Inc.*, 850 F.2d 1217 (7th Cir. 1988):

In a business transaction both sides presumably try to get the best of the deal. That is the essence of bargaining and the free market. . . . So one cannot characterize self-interest as bad faith. No particular demand in negotiations could be termed dishonest, even if it seemed outrageous to the other party. The proper recourse is to walk away from the bargaining table, not to sue for "bad faith" in negotiations.

BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 331 & n.5 (quoting *Feldman*, 850 F.2d at 1223).<REF ID='FN133'>[fm][eb]

<sup>182</sup> BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 347-48. Burton and Andersen also note that the common law rule that there are no good faith obligations in negotiation is policed by the theories of duress, coercion, fraud, misrepresentation, unjust enrichment, and promissory estoppel. *Id.* at 335-47.<REF ID='FN134'>[fm][eb]

<sup>183</sup> *Id.* at 348-49.<REF ID='FN135'>[fm][eb]

<sup>184</sup> *Id.* at 348.<REF ID='FN136'>[fm][eb]

<sup>185</sup> *Id.* at 353.<REF ID='FN137'>[fm][eb]

<sup>186</sup> *Id.* at 359 (quoting *Teachers Ins. & Annuity Ass'n of Am. v. Tribune Co.*, 670 F.Supp. 491, 497 (S.D.N.Y. 1987)).<REF ID='FN138'>[fm][eb]

<sup>187</sup> *Id.* at 360 (citing *Pinnacle Books, Inc. v. Harlequin Enters. Ltd.*, 519 F. Supp. 118, 122 (S.D.N.Y. 1989)).<REF ID='FN139'>[fm][eb]

<sup>188</sup> *Id.* at 362.<REF ID='FN140'>[fm][eb]

<sup>189</sup> See E. Allan Farnsworth, *Precontractual Liability and Preliminary Agreements: Fair Dealing and Failed Negotiations*, 87 COLUM. L. REV. 217, 263 (1987).<REF ID='FN141'>[fm][eb]

ultimate agreement, . . . there is no possibility of a claim for lost expectation under such an agreement."<sup>190</sup> Thus, under Farnsworth's rationale, only restitutionary, out-of-pocket damages are available for breach of a preliminary agreement.<sup>191</sup>

Burton and Andersen reject Farnsworth's reasoning as an absolute rule, as does the emerging consensus of common law jurisprudence.<sup>192</sup> Although in many cases lost profits cannot be awarded because the terms of the final contract are too indefinite, Burton and Andersen point out that in many cases "it is practical and appropriate to allow expectation damages based on the potential, but unrealized, final contract."<sup>193</sup> They identify the key issue as being whether a court can determine what economic benefit the injured party would have realized had the final contract been executed.<sup>194</sup> "Thus, when the parties have worked out many of the principal economic terms of their final contract in detail, there is no obstacle to allowing expectation damages based on the bargain tentatively agreed to, but not consummated."<sup>195</sup> When expectation interest can be ascertained with certainty, the courts have awarded expectation damages for breach of a preliminary agreement in various settings, including loan agreements,<sup>196</sup> a sale/sale-back of commercial aircraft,<sup>197</sup> a commercial lease,<sup>198</sup> a manufacturing contract,<sup>199</sup> and a subcontract to design and supply radiation detection equipment to the United States Air Force.<sup>200</sup>

### B. Government Contract Formation Law

Unlike common law contracts, federal government contracts are highly regulated in their form, constituent clauses, and procedures for award. With only rare exceptions, a government contractor must accept the contract terms as set out by the agency in the solicitation.<sup>201</sup> Although technical requirements are normally tailored to a particular contract, the large majority of government contracts clauses are specified in the FAR and are uniformly incorporated in government solicitations and contracts.<sup>202</sup> A qualified bidder will be disqualified if it takes exception to any of these material terms or conditions of the solicitation.<sup>203</sup> In "negotiated" solicitations, in which the quality or technical acceptability of the proposal of the offeror is evaluated along with the price,<sup>204</sup> offerors may have more leeway to take exception to the

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<sup>190</sup> *Id.* <REF ID='FN141A'>[fm][eb]

<sup>191</sup> See RESTATEMENT (SECOND) OF CONTRACTS § 344 (1981) (labeling as "reliance" damages what many courts refer to as the "restitutionary" measure); see also *Acme Process Equip. Co. v. United States*, 347 F.2d 509, 530 (Ct. Cl. 1965) (allowing for reliance damages as defined in *Restatement (Second) of Contracts*, *supra*, yet declaring the damages "restitution"), *rev'd on other grounds*, 385 U.S. 138 (1966). <REF ID='FN142'>[fm][eb]

<sup>192</sup> BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 364-66. <REF ID='FN142A'>[fm][eb]

<sup>193</sup> *Id.* at 364. <REF ID='FN143'>[fm][eb]

<sup>194</sup> *Id.* at 365. <REF ID='FN143A'>[fm][eb]

<sup>195</sup> *Id.* <REF ID='FN144'>[fm][eb]

<sup>196</sup> See, e.g., *Teachers Ins. & Annuity Ass'n of Am. v. Coaxial Communications, Inc.*, 799 F. Supp. 16, 18-19 (S.D.N.Y. 1992) (awarding expectation damages for breach of a loan commitment); *Teachers Ins. & Annuity Ass'n of Am. v. Ormesa Geothermal*, 791 F. Supp. 401, 415-18 (S.D.N.Y. 1991) (same); *Teachers Ins. & Annuity Ass'n of Am. v. Butler*, 626 F. Supp. 1229, 1236 (S.D.N.Y. 1986) (same). <REF ID='FN145'>[fm][eb]

<sup>197</sup> See, e.g., *Cauff, Lippman & Co. v. Apogee Fin. Group, Inc.*, 807 F. Supp. 1007, 1024 (S.D.N.Y. 1992) (awarding expectation damages for breach of a preliminary agreement to negotiate the sale/sale-back of a commercial aircraft). <REF ID='FN146'>[fm][eb]

<sup>198</sup> See, e.g., *Evans, Inc. v. Tiffany & Co.*, 416 F. Supp. 224, 240-45 (N.D. Ill. 1976) (awarding expectation damages for breach of a preliminary agreement to enter into a commercial lease). <REF ID='FN147'>[fm][eb]

<sup>199</sup> See, e.g., *Milex Prods., Inc. v. Alra Lab., Inc.*, 603 N.E.2d 1226, 1235-37 (Ill. App. Ct. 1992) (awarding expectation damages for breach of a preliminary agreement to enter into a manufacturing contract). <REF ID='FN148'>[fm][eb]

<sup>200</sup> See, e.g., *Air Tech. Corp. v. General Elec. Co.*, 199 N.E.2d 538, 548 (Mass. 1964) (awarding expectation damages for breach of a preliminary agreement to design and supply radiation detection devices). <REF ID='FN149'>[fm][eb]

<sup>201</sup> See *infra* notes <CITE ID='FN155'>-<CITE ID='FN156'> and accompanying text (discussing "negotiated" solicitations). <REF ID='FN150A'>[fm][eb]

<sup>202</sup> See FAR, 48 C.F.R. pt. 52 (1996). <REF ID='FN151'>[fm][eb]

<sup>203</sup> See FAR, 48 C.F.R. § 14.301(a). To be awarded a government contract, a bidder must be "responsive"[sp2c][sp2c]the bidder must conform in all material respects to the solicitation, not taking exception to any terms and conditions. See *id.* In this way, the government can ensure that all bidders are bidding on an "equal footing." See *id.* <REF ID='FN153'>[fm][eb]

<sup>204</sup> See *id.* § 15.602. <REF ID='FN155'>[fm][eb]

terms and conditions of the contract. Unless the government agrees to amend the solicitation for all offerors, however, award must be made on the solicitation as finalized.<sup>205</sup>

The procedures for awarding a government contract are also highly regulated in order to treat offerors fairly and equally.<sup>206</sup> For instance, a contract is formed only when the government's contracting officer sends the bidder written notice of the award.<sup>207</sup> Further, government representatives are required to communicate the same information to all offerors,<sup>208</sup> and if the contracting officer reopens negotiations with one offeror, she must reopen them with all offerors in the competitive range.<sup>209</sup>

Two judicial forums have jurisdiction over the government contracts award process. Both forums ensure compliance with regulations and fairness to bidders. The Court of Federal Claims, following long-standing precedent, will enforce as an implied contract between an offeror and the government the idea that the offeror's offer will be considered fairly and impartially.<sup>210</sup> If the government breaches this contract, the Court of Federal Claims will award the offeror its bid and proposal costs--restitutionary damages.<sup>211</sup> Moreover, in the Federal Courts Improvement Act of 1982,<sup>212</sup> Congress granted the Court of Federal Claims<sup>213</sup> jurisdiction to grant injunctive relief in "bid protest" actions--when an offeror claims that it was improperly denied a contract or an opportunity to compete for an award.<sup>214</sup> The Federal Circuit has found that the jurisdictional basis for granting this relief still lies under the Tucker Act<sup>215</sup> as an asserted breach of the implied covenant to treat a bidder fairly and impartially.<sup>216</sup> The Federal Circuit had also held that the authority of the Court of

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<sup>205</sup> See *id.* §§ 15.611(d), 15.612(d).<REF ID='FN156'>[fm][eb]

<sup>206</sup> See *id.* § 15.603(c). The purpose of government contracts award procedures is to treat offerors fairly and equally. See *Airco, Inc. v. Energy Research & Dev. Admin.*, 528 F.2d 1294, 1297-99 (7th Cir. 1975) (per curiam); *Elcon Enters., Inc. v. Washington Metro. Area Transit Auth.*, 770 F. Supp. 667, 677 (D.D.C. 1991), *aff'd in part and rev'd in part*, 977 F.2d 1472 (D.C. Cir. 1992); *Howard Cooper Corp. v. United States*, 763 F. Supp. 829, 837 (E.D. Va. 1991); *Dynallectron Corp. v. United States*, 659 F. Supp. 64, 68-70 (D.D.C. 1987); *Grumman Data Sys. Corp. v. United States*, 28 Fed. Cl. 803, 805-06 (1993); *Thomas Creek Lumber & Log Co. v. United States*, 22 Cl. Ct. 559, 566 (1991); *Cassidy Cleaning, Inc. v. United States*, 10 Cl. Ct. 317, 319 (1986).<REF ID='FN157'>[fm][eb]

<sup>207</sup> See 48 C.F.R. § 14.408-1; *Professional Bldg. Concepts, Inc. v. Central Falls*, 974 F.2d 1, 3-4 (1st Cir. 1992) (per curiam); *Coco Bros. v. Pierce*, 741 F.2d 675, 677 (3d Cir. 1984).<REF ID='FN154'>[fm][eb]

<sup>208</sup> See 48 C.F.R. § 15.611(c); *Prudential-Maryland Joint Venture Co. v. Lehman*, 590 F. Supp. 1390, 1408 (D.D.C. 1984); *General Elec. Co. v. Seamans*, 340 F. Supp. 636, 640 (D.D.C. 1972); *Planning Research Corp. v. United States*, 4 Cl. Ct. 283, 298-99 (1983).<REF ID='FN158'>[fm][eb]

<sup>209</sup> See 48 C.F.R. § 15.611(c); *SACO Defense Sys. Div. v. Weinberger*, 806 F.2d 308, 312-13 (1st Cir. 1986); *Blue Cross & Blue Shield of Md., Inc. v. United States Dep't of Health & Human Servs.*, 718 F. Supp. 80, 87 (D.D.C. 1989); *Logicon, Inc. v. United States*, 22 Cl. Ct. 776, 791-93 (1991); see also *Airco*, 528 F.2d at 1298 (stating that when discussions amounted to negotiations and took place after the negotiations "cut off date," the regulations were violated).<REF ID='FN159'>[fm][eb]

<sup>210</sup> See *Grumman*, 28 Fed. Cl. 807-10; *Tonya, Inc. v. United States*, 28 Fed. Cl. 727, 730-32 (1993); *TRW, Inc. v. United States*, 28 Fed. Cl. 155, 157-62 (1993); *Crux Computer Corp. v. United States*, 24 Cl. Ct. 223, 225 (1991); *Contract Custom Drapery Serv., Inc. v. United States*, 6 Cl. Ct. 811, 817-18 (1984); *Keco Indus., Inc. v. United States*, 428 F.2d 1233, 1237-40 (Ct. Cl. 1970); see also *Delta Data Sys. Corp. v. Webster*, 755 F.2d 938, 940 (D.C. Cir. 1985) (per curiam) (finding bid preparation costs after lifting a preliminary injunction against the continuance of a contract available to an offeror that was unfairly denied contract); *B.K. Instrument, Inc. v. United States*, 715 F.2d 713, 732 (2d Cir. 1983) (ordering bid costs if reselection process is not possible); *M. Steinthal & Co. v. Seamans*, 455 F.2d 1289, 1302 (D.C. Cir. 1971) (stating that the court has discretion to award bid preparation costs or injunction); see *infra* note <CITE ID='FN166'>[fm][eb].<REF ID='FN160'>[fm][eb]

<sup>211</sup> See *Grumman*, 28 Fed. Cl. at 807-10; *Keco*, 428 F.2d at 1240.<REF ID='FN161'>[fm][eb]

<sup>212</sup> Pub. L. No. 97-164, 96 Stat. 25 (codified as amended in scattered sections of 28 U.S.C. and other titles).<REF ID='FN162'>[fm][eb]

<sup>213</sup> As originally enacted, the name of the Court of Federal Claims was the Claims Court. See 28 U.S.C. § 1491 (1994). The name was changed in 1992 by the Court of Federal Claims Technical and Procedural Improvements Act of 1992, Pub. L. No. 102-572, § 902, 106 Stat. 4516 (codified as amended in scattered sections of 28 and 41 U.S.C.).<REF ID='FN163'>[fm][eb]

<sup>214</sup> See 28 U.S.C. § 1491(a)(3). This provision provided as follows:

To afford complete relief on any contract claim brought before the contract is awarded, the court shall have exclusive jurisdiction to grant declaratory judgments and such equitable and extraordinary relief as it deems proper, including but not limited to injunctive relief. In exercising this jurisdiction, the court shall give due regard to the interests of national defense and national security.

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*Id.*<REF ID='FN164'>[fm][eb]

<sup>215</sup> 28 U.S.C. § 1491. In particular, bid protest jurisdiction in the Court of Federal Claims has been held to stem from section 1491(a). See *United States v. John C. Grimberg Co.*, 702 F.2d 1362, 1374-77 (Fed. Cir. 1983) (en banc).<REF ID='FN1215A'>[fm][eb]

<sup>216</sup> See *Grimberg*, 702 F.2d at 1367.<REF ID='FN1215B'>[fm][eb]

Federal Claims to grant injunctive relief was limited to decisions brought *prior* to the award of a contract to any offeror under the challenged procurement.<sup>217</sup>

Congress recently amended the Tucker Act in the Administrative Dispute Resolution Act of 1996<sup>218</sup> to clarify that the Court of Federal Claims has jurisdiction to hear bid protest actions whether or not a contract has been awarded under the challenged procurement.<sup>219</sup> Congress did not alter the operative language in section 1491 of the Judicial Code, which states that the Court of Federal Claims "shall have jurisdiction" in bid protest actions,<sup>220</sup> so it seems likely that the Federal Circuit will continue to hold, as it did in *United States v. John C. Grimberg Co.*,<sup>221</sup> that the jurisdiction of the Court of Federal Claims to hear bid protest cases is found in section 1491(a), which gives that court jurisdiction to hear contract breach cases.<sup>222</sup> Whatever its source of jurisdiction, however, the Court of Federal Claims has consistently defined its task in bid protest cases as to determine if the bidder was treated fairly and equally.<sup>223</sup>

The federal district courts also monitor the federal contracts award process. Although, as a general rule, they may not grant contract breach damages,<sup>224</sup> they, too, will grant injunctive relief in appropriate situations<sup>225</sup> and now have authority to grant the monetary relief of bid preparation and proposal costs.<sup>226</sup> These cases, often called "Scanwell" actions--after the lead case of *Scanwell Laboratories, Inc. v. Shaffer*<sup>227</sup>--grant standing under the Administrative

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<sup>217</sup> See *id.* at 1377; see also *F. Alderete Gen. Contractors, Inc. v. United States*, 715 F.2d 1476, 1479 (Fed. Cir. 1983) (holding that the court had jurisdiction to hear the case filed before a contract under the challenged procurement was awarded); *Golden Eagle Ref. Co. v. United States*, 4 Cl. Ct. 613, 618-20 (1984) (same). The Federal Circuit's interpretations in *Grimberg* of the Federal Courts Improvement Act of 1982 were widely criticized. See Frederick W. Claybrook, Jr., *The Federal Courts Improvement Act Needs Improvement: A Renewed Call for Its Amendment*, 21 PUB. CONT. L.J. 1, 2 n.3 (1991) (citing articles).<REF ID="FN165">[fm][eb]

<sup>218</sup> Pub. L. No. 104-320, 110 Stat. 3870.<REF ID="FN801">[fm][eb]

<sup>219</sup> *Id.* § 12(a), 110 Stat. at 3874-75. Section 12(a) of the Administrative Dispute Resolution Act of 1996 strikes previous subsection 1491(a)(3) of the Judicial Code, redesignates previous subsection 1491(b) as 1491(c), and adds the following new subsection 1491(b):

(b)(1) Both the United States Court of Federal Claims and the district courts of the United States shall have jurisdiction to 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. Both the United States Court of Federal Claims and the district courts of the United States shall have jurisdiction to entertain such an action without regard to whether suit is instituted before or after the contract is awarded.

(2) To afford relief in such an action, the courts may award any relief that the court considers proper, including declaratory and injunctive relief except that any monetary relief shall be limited to bid preparation and proposal costs.

(3) In exercising jurisdiction under this subsection, the courts shall give due regard to the interests of national defense and national security and the need for expeditious resolution of the action.

(4) In any action under this subsection, the courts shall review the agency's decision pursuant to the standards set forth in section 706 of title 5.

*Id.* § 12(a).<REF ID="FN802">[fm][eb]

<sup>220</sup> Compare 28 U.S.C. § 1491(a)(3) (1994) ("shall have exclusive jurisdiction"), with 28 U.S.C.A. § 1491(b)(1) (Supp. 1997) ("shall have jurisdiction").<REF ID="FN803">[fm][eb]

<sup>221</sup> 702 F.2d 1362, 1377 (Fed. Cir. 1983) (en banc).<REF ID="FN804">[fm][eb]

<sup>222</sup> The reasoning of the Federal Circuit in *Grimberg* that section 1491(a)(3) (now (b)(1)) is not jurisdictional is questionable. See Claybrook, *supra* note <CITE ID="FN165">, at 16-19. Whether the Federal Circuit will abandon this reading of the section if district and other circuit courts find new section 1491(b)(1) to be jurisdictional, which seems entirely likely, remains to be seen.<REF ID="FN805">[fm][eb]

<sup>223</sup> See *supra* note <CITE ID="FN160"> and accompanying text.<REF ID="FN806">[fm][eb]

<sup>224</sup> Congress has placed exclusive jurisdiction in the Court of Federal Claims and the boards of contract appeals to grant damages for a breach of contract. See 28 U.S.C. § 1491; 41 U.S.C. § 607 (1994). The only exception until recently was that, under the "Little Tucker Act," federal district courts have concurrent original jurisdiction with the United States Court of Federal Claims and the boards to grant contract breach damages under \$10,000. See 28 U.S.C. § 1346(a)(2). Under section 12 of the Administrative Dispute Resolution Act of 1996, Congress also granted the district courts authority to award bid preparation and proposal costs. Pub. L. No. 104-320, § 12(a)(3), 110 Stat. 3870, 3874 (to be codified at 28 U.S.C. § 1491(b)(2)). No monetary limit is stated, so, presumably, district courts may award such monetary relief in excess of \$10,000.<REF ID="FN166">[fm][eb]

<sup>225</sup> See, e.g., *In re Smith & Wesson*, 757 F.2d 431, 433-35 (1st Cir. 1985) (stating that by conferring jurisdiction upon the Claims Court to award injunctive relief in the pre-award stage of the procurement process, Congress left intact the current substantive law in this area, known as the *Scanwell* Doctrine).<REF ID="FN166A">[fm][eb]

<sup>226</sup> See *supra* note <CITE ID="FN166">.<REF ID="FN1218A">[fm][eb]

<sup>227</sup> 424 F.2d 859 (D.C. Cir. 1970).<REF ID="FN167">[fm][eb]



Procedure Act (APA)<sup>228</sup> to a "disappointed bidder" to challenge the propriety of the award process.<sup>229</sup> The well-known review standard of section 10 of the APA<sup>230</sup> is often summarized in *Scanwell* actions as follows:

[T]hose adversely affected by the award of government contracts . . . bear a heavy burden of showing either that (1) the procurement official's decisions on matters committed primarily to his own discretion had no rational basis, or (2) the procurement procedure involved a clear and prejudicial violation of applicable statutes or regulations.<sup>231</sup>

Since 1982, the Court of Federal Claims, while asserting a different jurisdictional basis,<sup>232</sup> has applied practically the identical standard when assessing whether to grant relief in a *Scanwell* action, both with respect to the merits of the complaint<sup>233</sup>--as is now required by statute<sup>234</sup>--and with respect to the standards for granting a preliminary injunction.<sup>235</sup>

<sup>228</sup> 5 U.S.C. §§ 551-559, 701-706 (1994).<REF ID='FN168'>[fm][eb]

<sup>229</sup> See, e.g., *B.K. Instrument, Inc. v. United States*, 715 F.2d 713, 717-23 (2d Cir. 1983) (holding that a disappointed bidder has standing to sue for declaratory and injunctive relief); *William F. Wilke, Inc. v. Department of Army*, 485 F.2d 180, 182-83 (4th Cir. 1973) (same); *Merriam v. Kunzig*, 476 F.2d 1233, 1240-43 (3d Cir. 1973) (same); *Scanwell*, 424 F.2d at 861-73 (same). Jurisdiction in the federal district courts is federal question jurisdiction under section 1331 of the Judicial Code. See 28 U.S.C. § 1331; see also *Chem Serv., Inc. v. Environmental Monitoring Sys. Lab.*, 12 F.3d 1256, 1261 (3d Cir. 1993) (stating that the court has jurisdiction under 28 U.S.C. § 1331 to hear the case); *Choctaw Mfg. Co. v. United States*, 761 F.2d 609, 615 (11th Cir. 1985) (same); *Action Serv. Corp. v. Garrett*, 790 F. Supp. 1188, 1189 (D.P.R. 1992) (same); *Fordice Constr. Co. v. Marsh*, 773 F. Supp. 867, 869 (S.D. Miss. 1990) (same).<REF ID='FN169'>[fm][eb]

<sup>230</sup> Section 10 of the APA reads:

To the extent necessary to decision and when presented, the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of an agency action. The reviewing court shall

- (1) compel agency action unlawfully withheld or unreasonably delayed; and
- (2) hold unlawful and set aside agency action, findings, and conclusions found to be
  - (A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law;
  - (B) contrary to constitutional right, power, privilege, or immunity;
  - (C) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right;
  - (D) without observance of procedure required by law;
  - (E) unsupported by substantial evidence in a case subject to sections 556 and 557 of this title or otherwise reviewed on the record of an agency hearing provided by statute; or
  - (F) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court.

In making the foregoing determinations, the court shall review the whole record or those parts of it cited by a party, and due account shall be taken of the rule of prejudicial error.

5 U.S.C. § 706.<REF ID='FN170'>[fm][eb]

<sup>231</sup> *Kentron Hawaii, Ltd. v. Warner*, 480 F.2d 1166, 1169 (D.C. Cir. 1973) (citations omitted); see also *Chemung County v. Dole*, 781 F.2d 963, 971 (2d Cir. 1986) (adopting basically the same standard of review for the award of a government contract as stated in *Kentron*); *Choctaw*, 761 F.2d at 616 (same); *Sea-Land Serv., Inc. v. Brown*, 600 F.2d 429, 430, 434-35 (3d Cir. 1979) (same); *Airco, Inc. v. Energy Research & Dev. Admin.*, 528 F.2d 1294, 1296 (7th Cir. 1975) (per curiam) (same).<REF ID='FN171'>[fm][eb]

<sup>232</sup> The district courts have uniformly found federal question jurisdiction, see 28 U.S.C. § 1331, in *Scanwell* cases. See, e.g., *Chem Serv.*, 12 F.3d at 1261 (determining that a private laboratory has standing to sue to enjoin the government from carrying out an agreement with a competitor); *Mark Dunning Indus., Inc. v. Perry*, 877 F. Supp. 1541, 1541-42 (M.D. Ala. 1995) (ordering a stay of execution and extension of the unsuccessful bidder's contract); *Action Serv. Corp.*, 790 F. Supp. at 1189 (holding that the United States Navy's failure to conduct a responsibility determination before awarding the contract was clear error prejudicial to the unsuccessful bidder). Whether the district courts in the future will treat new section 1491(b) as their exclusive jurisdictional basis; or as an additive source of jurisdiction to federal question jurisdiction; or will follow the lead of the Federal Circuit in *Grimberg* and find new section 1491(b) not to be jurisdictional (but only a remedy-granting provision), see *supra* note <CITE ID='FN805'>, remains to be seen.<REF ID='FN1223A'>[fm][eb]

<sup>233</sup> See, e.g., *VMS Hotel Partners v. United States*, 30 Fed. Cl. 512, 513 (1994) (stating that the court will overturn an award of a contract only if there is no rational basis for the decision); *Shields Enters., Inc. v. United States*, 28 Fed. Cl. 615, 622-23, 632 (1993) (same); *Magnavox Elec. Sys. Co. v. United States*, 26 Cl. Ct. 1373, 1380-81 (1992) (same); *Baird Corp. v. United States*, 1 Cl. Ct. 662, 664 (1983) (same). A few Court of Federal Claims cases had articulated the standard of review for the merits to require "clear and convincing evidence" of a breach of the implied contract to treat a bidder fairly and impartially. The better reasoned decisions rejected that standard and applied the preponderance standard used by the district courts in APA cases. Compare *Durable Metals Prods., Inc. v. United States*, 27 Fed. Cl. 472, 477-79 (requiring clear and convincing evidence), *aff'd*, 11 F.3d 1071 (Fed. Cir. 1993), with *Isratex, Inc. v. United States*, 25 Cl. Ct. 223, 227 (1992) (rejecting clear and convincing evidence test), and *Arthur Forman Enters., Inc. v. United States*, 22 Cl. Ct. 816, 830 (1991) (same), and *Logicon, Inc. v. United States*, 22 Cl. Ct. 776, 782-83 (1991) (same). Presumably, the Court of Federal Claims will conform to the preponderance standard with the statutory requirement to apply APA standards. See *infra* note <CITE ID='FN173'>.<REF ID='FN172'>[fm][eb]

Both courts commonly state that they lack authority to award a contract,<sup>236</sup> but at the same time, they acknowledge their authority to direct an award when the contracting officer has no discretion under the law to do anything but award the contract to the particular bidder.<sup>237</sup>

When assessing whether to issue an injunction, both the district courts and the Court of Federal Claims frequently state that a disappointed bidder suffers irreparable injury because, if an improper award is allowed to go forward to another bidder, the disappointed bidder will not be able to recover lost profits on the contract the bidder did not receive.<sup>238</sup> The "public interest" prong of the four-pronged test for a preliminary injunction<sup>239</sup> comes into play much more often in government contracts, however, than in other commercial settings. Not uncommonly, the public interest in not disrupting the government's procurement process and in allowing the government to receive its goods or services in a timely fashion will override other considerations that favor granting relief to an aggrieved bidder.<sup>240</sup> The recent

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(...continued)

<sup>234</sup>The Administrative Dispute Resolution Act of 1996 added new subsection 1491(b)(4), which provides in part, "the courts shall review the agency's decision pursuant to the standards set forth in section 706 of title 5." Pub. L. No. 104-320, § 12(a)(3), 110 Stat. 3870, 3875 (to be codified at 28 U.S.C. § 1491(b)(4)).<REF ID=FN1224A>[fm][eb]

<sup>235</sup>Both the Court of Federal Claims and the district courts apply the traditional four-pronged standard when assessing whether to grant a preliminary injunction, considering (1) the likelihood of success on the merits, (2) irreparable injury to the movant, (3) injury to third parties, and (4) the public interest. Compare *Randolph-Sheppard Vendors of Am. v. Weinberger*, 795 F.2d 90, 110 (D.C. Cir. 1986) (using the four-pronged standard to determine if a preliminary injunction should be ordered), and *Princeton Combustion Research Lab., Inc. v. McCarthy*, 674 F.2d 1016, 1019, 1022 (3d Cir. 1982) (same), and *Fort Sumter Tours, Inc. v. Andrus*, 564 F.2d 1119, 1124-25 (4th Cir. 1977) (same), and *DTH Management Group v. Kelso*, 844 F. Supp. 251, 254 (E.D.N.C. 1993) (same), and *Geo-Con, Inc. v. United States*, 783 F. Supp. 1, 2 (D.D.C. 1992) (same), and *Allis-Chalmers Corp. v. Friedkin*, 481 F. Supp. 1256, 1263-64 (M.D. Pa.) (same), *aff'd*, 635 F.2d 248 (3d Cir. 1980), with *Magellan Corp. v. United States*, 27 Fed. Cl. 446, 447, 451 (1993) (rejecting the clear and convincing evidence test for a showing of likelihood of success on the merits, but using the four factors to determine if a preliminary injunction should be ordered), and *Reel-O-Matic Sys., Inc. v. United States*, 16 Cl. Ct. 93, 99 (1989) (using the four factors to determine if a preliminary injunction should be ordered), and *Sterlingwear of Boston, Inc. v. United States*, 10 Cl. Ct. 644, 649-50 (1986) (same), and *Isometrics, Inc. v. United States*, 5 Cl. Ct. 420, 422-23 (1984) (same), and *MWK Int'l, Ltd. v. United States*, 2 Cl. Ct. 206, 208 (1983) (same).<REF ID=FN173>[fm][eb]

<sup>236</sup>See, e.g., *Ulstein Maritime, Ltd. v. United States*, 833 F.2d 1052, 1058-59 (1st Cir. 1987) (affirming the decision of the district court to order review of the bids by the agency and highlighting that the lower court did not direct award of the contract to the plaintiff); *Simmons v. Block*, 782 F.2d 1545, 1550 (11th Cir. 1986) (stating that the plaintiff did not have a right to have the contract awarded to him); *Chemung County*, 781 F.2d at 970-71 (same); *Sea-Land Serv.*, 600 F.2d at 432-33 (same); *Scanwell*, 424 F.2d at 864, 869 (same); *Durable Metals*, 27 Fed. Cl. at 476-77 (same); *Unified Indus., Inc. v. United States*, 24 Cl. Ct. 570, 575-76 (1991) (same); *Arrowhead Metals, Ltd. v. United States*, 8 Cl. Ct. 703, 711 (1985) (same); *International Graphics, Div. of Moore Bus. Forms, Inc. v. United States*, 4 Cl. Ct. 186, 193-94 (1983) (same).<REF ID=FN174>[fm][eb]

<sup>237</sup>See, e.g., *Choctaw Mfg. Co. v. United States*, 761 F.2d 609, 617 n.14, 619-21 (11th Cir. 1985) (instructing lower court to award contract to plaintiff after rejecting government's argument that it had discretion to award contract to another bidder); *Delta Data Sys. Corp. v. Webster*, 744 F.2d 197, 204 (D.C. Cir. 1984) ("[A] court may not order the award of a contract unless it is clear that, but for the illegal behavior of the agency, the contract would have been awarded to the party asking the court to order the award." (footnote omitted)); *Ace-Federal Reporters, Inc. v. Federal Energy Regulatory Comm'n*, 734 F. Supp. 20, 26 (D.D.C. 1990) (same).<REF ID=FN175>[fm][eb]

<sup>238</sup>See, e.g., *Alamo Aircraft Supply v. Carlucci*, 698 F. Supp. 8, 9 (D.D.C. 1988) (stating that plaintiff will suffer harm of the loss of earnings); *Minnesota Mining & Mfg. Co. v. Shultz*, 583 F. Supp. 184, 191 (D.D.C. 1984) (finding that loss of expected profits can constitute irreparable harm); *Ainslie Corp. v. Middendorf*, 381 F. Supp. 305, 307 (D. Mass. 1974) (same); *Magellan*, 27 Fed. Cl. at 447 (same); *Magnavox*, 26 Cl. Ct. at 1379 (same); *Essex Electro Eng'rs, Inc. v. United States*, 3 Cl. Ct. 277, 287 (1983) (same); see also *O'Donnell Constr. Co. v. District of Columbia*, 963 F.2d 420, 428 (D.C. Cir. 1992) (stating that the difficulty of proving possible profits and recouping losses supports the grant of an injunction); *Delta Data Sys. Corp. v. Webster*, 755 F.2d 938, 940 (D.C. Cir. 1985) (per curiam) (stating that because the amount of profit that could be lost has been reduced, the injunction should be lifted); *M. Steinthal & Co. v. Seaman's*, 455 F.2d 1289, 1302, 1306 (D.C. Cir. 1971) (stating that an injunction should not be ordered simply because damages would not make the plaintiff whole); *Funderburg Builders, Inc. v. Abbeville County Mem'l Hosp.*, 467 F. Supp. 821, 825 (D.S.C. 1979) (stating that because lost profits are not recoverable, an injunction should be ordered); *Keco Indus., Inc. v. United States*, 428 F.2d 1233, 1240 (Ct. Cl. 1970) (holding that the plaintiff may not recover lost profits because the contract never came into existence).<REF ID=FN176>[fm][eb]

<sup>239</sup>See *supra* note <CITE ID=FN173>.<REF ID=FN176A>[fm][eb]

<sup>240</sup>See *Diebold v. United States*, 947 F.2d 787, 804 (6th Cir. 1991); *B.K. Instrument, Inc. v. United States*, 715 F.2d 713, 730 (2d Cir. 1983); *M. Steinthal & Co.*, 455 F.2d at 1301-04; *Pace Co., Div. of Ambac Indus. v. Resor*, 453 F.2d 890, 891 (6th Cir. 1971) (per curiam); *Aero Corp. v. Department of Navy*, 549 F. Supp. 39, 46 (D.D.C. 1982); *Arrowhead Metals*, 8 Cl. Ct. at 717; *Northern Va. Van Co. v. United States*, 3 Cl. Ct. 237, 242 (1983).<REF ID=FN177>[fm][eb]

congressional action has clarified that both the Court of Federal Claims and the district courts have jurisdiction over all types of bid protests, or *Scanwell* actions,<sup>241</sup> at least for now.<sup>242</sup>

### C. Application of the Common Law to Government Contract Formation Law

In one sense, government contracts law is in step with, and was even at the forefront of, good faith duties being applied to the negotiation and formation of contracts. Since 1956, government contracts law has consistently recognized an implied contractual duty to treat bidders fairly, honestly, and impartially.<sup>243</sup> Although in 1956 it might have been difficult

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<sup>241</sup>Prior to amendment of section 1491 in the Administrative Dispute Resolution Act of 1996, the circuit courts were broadly split on whether district courts had concurrent jurisdiction with the Court of Federal Claims to grant injunctive relief in cases filed prior to an award under the challenged procurement or whether the jurisdiction of the Court of Federal Claims was exclusive in such situations. The First and Third Circuits held that district courts had concurrent jurisdiction with the Court of Federal Claims to consider bid protest actions brought before an award is made under the challenged solicitation. See *In re Smith & Wesson*, 757 F.2d 431, 433-35 (1st Cir. 1985); *Coco Bros. v. Pierce*, 741 F.2d 675, 677-79 (3d Cir. 1984). The Sixth and Federal Circuits agreed with that view in dicta. See *Diebold*, 947 F.2d at 805-06; *United States v. John C. Grimberg Co.*, 702 F.2d 1362, 1376 (Fed. Cir. 1983) (in banc). The Fourth and Ninth Circuits found that the Court of Federal Claims had exclusive jurisdiction in such situations. See *Rex Sys., Inc. v. Holiday*, 814 F.2d 994, 997-98 (4th Cir. 1987); *J.P. Francis & Assocs., Inc. v. United States*, 902 F.2d 740, 741-42 (9th Cir. 1990). The Second Circuit aligned itself with that view in dicta. See *B.K. Instrument*, 715 F.2d at 721 & n.4; see also *North Shore Strapping Co. v. United States*, 788 F. Supp. 344, 345-47 (N.D. Ohio 1992) (finding concurrent jurisdiction); *Commercial Energies, Inc. v. Cheney*, 737 F. Supp. 78, 79-80 (D. Colo. 1990) (finding no concurrent jurisdiction); *Metric Sys. Corp. v. United States Dep't of Air Force*, 673 F. Supp. 439, 440-41 (N.D. Fla. 1987) (same); *Arrow Air, Inc. v. United States*, 649 F. Supp. 993, 998 & n.8 (D.D.C. 1986) (same); *Caddell Constr. Co. v. Lehman*, 599 F. Supp. 1542, 1545-48 (S.D. Ga. 1985) (same); *Opal Mfg. Co., Ltd. v. UMC Indus., Inc.*, 553 F. Supp. 131, 132-33 (D.D.C. 1982) (same).

The difference in interpretation was based on whether the "exclusive jurisdiction" given to the Court of Federal Claims in former section 1491(a)(3) of the Judicial Code, see 28 U.S.C. § 1491(a)(3) (1994), meant exclusive of only the boards of contract appeals or exclusive of the district courts as well. Those courts that found concurrent jurisdiction relied on the legislative history of the statute. Those that did not considered the provision unambiguous on its face and, thus, did not permit resort to the legislative history. See Claybrook, *supra* note <CITE ID=FN165>, at 11-16 (discussing cases and legislative history and arguing that Congress had originally intended that the Court of Federal Claims and the district courts have concurrent jurisdiction).

In contrast, it was established early that district courts had exclusive jurisdiction over cases brought *after* the award of the challenged procurement. See *Grimberg*, 702 F.2d at 1374. But see Claybrook, *supra* note <CITE ID=FN165>, at 6-11 (arguing that the Court of Federal Claims had jurisdiction of all such actions because the court's original enabling statute, 28 U.S.C. § 1491(a)(3) (1994), properly construed, applied to actions prior to the award of the contract to the plaintiff, whether or not a contract had been awarded to a competitor). Congress has altered this in the amendment of section 1491, which now grants the two courts concurrent jurisdiction "without regard to whether suit is instituted before or after the contract is awarded." 28 U.S.C.A. § 1491(b)(1) (West Supp. 1997).<REF ID=FN178>[fm][eb]

<sup>242</sup>Congress provided in section 12(c) of the Administrative Dispute Resolution Act of 1996 for the General Accounting Office to undertake a study to determine whether concurrent jurisdiction is necessary. Pub. L. No. 104-320, § 12(c), 110 Stat. 3870, 3875 (to be codified at 28 U.S.C. § 1491(b)(4)). In section 12(d), Congress provided that district court jurisdiction will terminate on January 1, 2001, unless extended by Congress. *Id.* § 12(d).

The recent amendment of section 1491 also raises the issue of whether the boards of contract appeals now have jurisdiction over bid protest cases. Former section 1491(a)(3), 28 U.S.C. § 1491(a)(3) (1994), stated that the Court of Federal Claims had "exclusive jurisdiction" over pre-award cases, and the legislative history makes clear that this was meant to prevent the boards from handling such cases, because otherwise they would have had the same powers as the Court of Federal Claims, as provided in section 8(d) of the Contract Disputes Act of 1978, 41 U.S.C. § 607(d) (1994). See *Coco Bros.*, 741 F.2d at 677-79 ("[T]he House Report endeavored to make it clear that the word 'exclusive' in the statute meant the exclusion of the boards of contract appeals . . ."). Section 1491 as revised, however, does not provide that the jurisdiction of the Court of Federal Claims and the district courts is "exclusive." Although undoubtedly not intended by Congress, reading the two statutes in conjunction potentially vests jurisdiction of bid protests in the boards of contract appeals. But see Contract Disputes Act of 1978, §§ 8(d), 10, 41 U.S.C. §§ 607(d), 609 (1994) (providing that (a) boards only have jurisdiction of an appeal from a contracting officer's decision as defined in the act and (b) the jurisdiction of the Court of Federal Claims is coextensive with the boards, but not vice versa).<REF ID=FN1229A>[fm][eb]

<sup>243</sup>See *Heyer Prods. Co. v. United States*, 140 F. Supp. 409, 412-14 (Ct. Cl. 1956). In the recent decision of *Dakota Tribal Industries v. United States*, 34 Fed. Cl. 295 (1995), the Court of Federal Claims may or may not have been correct to foreclose the plaintiff from asserting a breach of procurement regulations because of the late pleading of that cause of action. See *id.* at 298 n.2. The court was certainly incorrect, however, to cite and apply the general rule, as reflected in the *Restatement (Second) of Contracts*, that good faith duties do not adhere in contract negotiations. *Id.* at 298 (citing RESTATEMENT (SECOND) OF CONTRACTS § 205 cmt. c (1981)). The government's "preliminary agreement" in the contract negotiation phase to treat all bidders fairly and equally is a firmly rooted exception to the general rule. See *Heyer*, 140 F. Supp. at 412-14. Thus, the court's conclusion in *Dakota* that alleged misrepresentations by a government agent made in the bidding process are actionable only in tort because no contractual relation exists in the negotiations phase is highly questionable, and the court's attempts to distinguish analogous cases finding breach of contract in such situations are unpersuasive. See *Dakota*, 34 Fed. Cl. at 298-99.<REF ID=FN180>[fm][eb]



to articulate a contractual basis for this obligation, the present law of contractual good faith provides an ample basis. For example, a bidder entering into precontract arrangements with the government does not, like most parties in the commercial marketplace, begin on a blank slate. Instead, the multiple statutes, rules, and regulations controlling government contracts negotiation, competition, and award inform the parties to a potential government contract how they must structure their precontractual arrangements and when and how a contract must be awarded. This regulatory framework provides the "meat" of the justified expectations of the parties and the substance of their preliminary agreement with respect to the procurement.<sup>244</sup>

Considering the solid framework surrounding formation of government contracts, it was unfortunate that the Court of Federal Claims, following the lead of the Federal Circuit, deviated from a proper application of these contractual good faith duties when considering violations of law that affect all offerors equally. If construed properly, Congress's recent amendment to the Tucker Act will cure that deviation. Nevertheless, Congress has not cured, but concretized, a second deviation of the courts. Both the Court of Federal Claims and the district courts have failed to keep pace with the development of the common law of contractual good faith in contract formation with respect to the award of lost profits. The following sections address these deviations and Congress's recent actions concerning them.

*1. The Violation of Law That Affects All Offerors Equally.*--Several decisions in the Court of Federal Claims have held that, even though a violation of procurement law and regulation has been alleged, the disappointed bidder has no cause of action.<sup>245</sup> The court has reasoned that when the violation of law or regulation affects all bidders equally--for example, when the government overspecifies its legitimate needs and, consequently, potentially lessens competition<sup>246</sup>--there can be no breach of the implied contract to treat all bidders fairly and impartially because they are all being treated equally, even if illegally.<sup>247</sup> Similarly, these courts opine that the solicitation itself forms the sole substance of the implied contract, and, thus, by definition, a challenge to the legality of the solicitation itself cannot be countenanced.<sup>248</sup>

The above rationale deviates from a proper understanding of the agency's good faith duties. The government's implied contract requires that it treat offerors fairly *and* impartially, not fairly *or* impartially.<sup>249</sup> In federal procurements, the concept of "fairness" is not ephemeral or subject to reasonable doubt. Its parameters are specified extensively in the procurement laws and regulations, as well as in the solicitation document itself.<sup>250</sup> As the Supreme Court has observed, the government, through procurement laws

is given the benefit of the competition of the market and each bidder is given the chance for a bargain. [The procurement laws are], therefore, in the interest of both Government and bidder, necessarily giving rights to both and placing obligations on both. And it is not out of place to say that the Government should be animated by a justice as anxious to consider the rights of the bidder as to insist upon its own.<sup>251</sup>

Put in common law terms, part of the justified expectations of every bidder is that the government will comply with all applicable procurement laws and regulations. When it does not, the agency not only acts illegally, it also acts contrary to the bidder's justified expectations (and the terms on which it agreed to invest in the bidding process) and violates the covenant of good faith and fair dealing.

Thus, any violation of procurement law or regulation states a cause of action, not just under the APA<sup>252</sup> but as a breach of the implied contract to treat bidders fairly and impartially.<sup>253</sup> Treating bidders "equally unfairly" does not excuse

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<sup>244</sup> Cf. BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 347-49 (stating that preliminary agreements may "either set out procedural rules for subsequent negotiations, or settle . . . some of the substantive terms of the final contract, or both").<REF ID='FN181'>[fm][eb]

<sup>245</sup> See, e.g., *Alabama Metal Prods., Inc. v. United States*, 4 Cl. Ct. 530, 533-35 (1984) (holding that no legitimate contractual expectation was allegedly denied, and, therefore, plaintiff was not entitled to a remedy); *Planning Research Corp. v. United States*, 4 Cl. Ct. 283, 290-92 (1983) (same); *Hero, Inc. v. United States*, 3 Cl. Ct. 413, 415-17 (1983) (holding that plaintiff which had not yet submitted a bid did not have any contractual rights, regardless of whether procurement laws had been broken).<REF ID='FN182'>[fm][eb]

<sup>246</sup> See *New York Tel. Co. v. Secretary of the Army*, 657 F. Supp. 18, 21-25 (D.D.C. 1986); *BSP Div. of Envirotech Corp. v. United States EPA*, 471 F. Supp. 958, 961-62 (D.N.J. 1979).<REF ID='FN183'>[fm][eb]

<sup>247</sup> See *Alabama Metal*, 4 Cl. Ct. at 533-35; *Planning Research Corp.*, 4 Cl. Ct. at 290-92; *Hero*, 3 Cl. Ct. at 415-17; *Claybrook*, *supra* note <CITE ID='FN165'>, at 16-19.<REF ID='FN184'>[fm][eb]

<sup>248</sup> See *Alabama Metal*, 4 Cl. Ct. at 534.<REF ID='FN185'>[fm][eb]

<sup>249</sup> See *supra* note <CITE ID='FN160'> and accompanying text.<REF ID='FN185A'>[fm][eb]

<sup>250</sup> See 5 U.S.C. § 706 (1994).<REF ID='FN185B'>[fm][eb]

<sup>251</sup> *United States v. Purcell Envelope Co.*, 249 U.S. 313, 318 (1919).<REF ID='FN186'>[fm][eb]

<sup>252</sup> In applying the APA standards in *Scanwell* cases, district courts have not developed a similar theory that they cannot redress violations of law that affect all bidders equally. See, e.g., *Single Screw Compressor, Inc. v. United States Dep't of Navy*, 791 F. Supp. 7, 9-11 (D.D.C. 1992) (entertaining, under APA, challenges to the legality of the solicitation).<REF ID='FN187'>[fm][eb]



a good faith breach, and in any event, for both practical and policy reasons, the presumption should be that a violation of law is prejudicial to the aggrieved bidder.<sup>254</sup> Disappointed bidders further a substantial public policy when they prevent statutory or regulatory violations of the procurement process,<sup>255</sup> and lack of prejudice should not lightly be presumed.

Congress, in amending section 1491 in the Administrative Dispute Resolution Act of 1996, addressed this issue in two ways. First, it expressly granted the Court of Federal Claims and the district courts authority to hear objections to solicitations or "alleged violation of statute or regulation in connection with a procurement or a proposed procurement,"<sup>256</sup> thus effectively overruling those Court of Federal Claims decisions that had refused jurisdiction over alleged violations of law that affected all bidders equally. Second, Congress specified that the Court of Federal Claims "shall review the agency's decision pursuant to [the APA]."<sup>257</sup> Under the APA, courts are to set aside prejudicial violations of law<sup>258</sup> and compel agency action unlawfully withheld.<sup>259</sup> It is unlikely, therefore, that the Court of Federal Claims will continue to deviate from the common law in this regard. Under the amended section 1491, the Court of Federal Claims should redress all prejudicial violations of law and other procurement improprieties, even if they affect all bidders equally.

2. *The "No Lost Profits" Rule.*--As alluded to above, both the federal district courts and the Court of Federal Claims have stated repeatedly that the disappointed bidder may not be granted lost profits under the ultimate (or "larger") contract improperly denied.<sup>260</sup> For example, in *Keco Industries, Inc. v. United States*,<sup>261</sup> the Court of Claims stated that "it would be improper for this court to award plaintiff lost profits since the contract under which plaintiff would have made such profits never actually came into existence."<sup>262</sup> The holding of *Keco*, however, no longer reflects the prevailing law of

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(...continued)

<sup>253</sup>Even under the pre-amended section 1491, one well-reasoned decision of the Court of Federal Claims found that the court had jurisdiction to address any violation of law as a breach of the implied contract to treat all bidders fairly and equally. See *McMaster Constr., Inc. v. United States*, 23 Cl. Ct. 679 (1991). Although that decision was not broadly adopted by the judges of the Court of Federal Claims or embraced by the Federal Circuit, *cf. Central Ark. Maintenance, Inc. v. United States*, 68 F.3d 1338, 1342 (Fed. Cir. 1995) (endorsing a restrictive reading of the jurisdiction of the Court of Federal Claims), it had ample support in more longstanding precedent. Many cases have recited that the government breaches its implied duty to treat a bidder fairly when it violates applicable laws or regulations. See, e.g., *Burroughs Corp. v. United States*, 617 F.2d 590, 597-98 (Ct. Cl. 1980) (stating that a violation of procurement laws may be grounds for recovery because it tends to show that the government treated the bid arbitrarily and capriciously); *Keco Indus., Inc. v. United States*, 492 F.2d 1200, 1204 (Ct. Cl. 1974) (same). See also *Heyer Prods. Co. v. United States*, 140 F. Supp. 409, 412-13 (Ct. Cl. 1956) (equating action in conformity with procurement laws with honest consideration).<REF ID=FN188>[fm][eb]

<sup>254</sup>Even if a violation of law is established, prejudice must be shown for a disappointed bidder to prevail. See 5 U.S.C. § 706; *Grumman Data Sys. Corp. v. Widnall*, 15 F.3d 1044, 1048 (Fed. Cir. 1994); *Elcon Enters., Inc. v. Washington Metro. Area Transit Auth.*, 977 F.2d 1472, 1478-79 (D.C. Cir. 1992); *Smith & Wesson, Div. of Bangor Punta Corp. v. United States*, 782 F.2d 1074, 1080 (1st Cir. 1986); *Kentron Hawaii Ltd. v. Warner*, 480 F.2d 1166, 1180-81 (D.C. Cir. 1973). Nevertheless, those decisions which assume that a violation of law that *applies* equally to all bidders also *affects* all bidders equally are often wrong as a matter of fact. For instance, an overly restrictive specification that applies to all bidders will not prejudice a bidder that can meet the overly restrictive specification but will prejudice a potential bidder that cannot.<REF ID=FN189>[fm][eb]

<sup>255</sup>See *O'Donnell Constr. Co. v. District of Columbia*, 963 F.2d 420, 429 (D.C. Cir. 1992); *Hayes Int'l Corp. v. McLucas*, 509 F.2d 247, 258 (5th Cir. 1975); *Keco*, 428 F.2d at 1237-38; *Magnavox Elec. Sys. Co. v. United States*, 26 Cl. Ct. 1373, 1384-85 (1992).<REF ID=FN190>[fm][eb]

<sup>256</sup>Pub. L. No. 104-320, § 12(a)(3), 110 Stat. 3870, 3874 (to be codified at 28 U.S.C. § 1491(b)(1)).<REF ID=FN807>[fm][eb]

<sup>257</sup>*Id.* § 12(a)(3), 110 Stat. at 3875 (to be codified at 28 U.S.C. § 1491(b)(4)). This amendment, making the APA applicable in both courts, was previously suggested by the author. See Claybrook, *supra* note <CITE ID=FN165>, at 19-21.<REF ID=FN808>[fm][eb]

<sup>258</sup>5 U.S.C. § 706(2) (1994).<REF ID=FN809>[fm][eb]

<sup>259</sup>*Id.* § 706(1). Congress retained its admonition in section 1491, not expressly stated in the APA, that "the courts shall give due regard to the interests of national defense and national security and the need for expeditious resolution of the action." Pub. L. No. 104-320, § 12(a)(3), 110 Stat. at 3874 (to be codified at 28 U.S.C. § 1491(b)(3)).<REF ID=FN810>[fm][eb]

<sup>260</sup>See *Keco*, 428 F.2d at 1240.<REF ID=FN190A>[fm][eb]

<sup>261</sup>428 F.2d 1233 (Ct. Cl. 1970).<REF ID=FN191>[fm][eb]

<sup>262</sup>*Id.* at 1240 (citing *Heyer Prods. Co. v. United States*, 140 F. Supp. 409, 412 (Ct. Cl. 1956)). *Compubahn, Inc. v. United States*, 33 Fed. Cl. 677 (1995), provides a recent application of this precedent. In *Compubahn*, the Court of Federal Claims summarily dismissed the disappointed bidder's request for lost profits, ruling that "[c]ontract law . . . does not permit such a genre of recovery." *Id.* at 681.<REF ID=FN192>[fm][eb]

contractual good faith.<sup>263</sup> Rather, when the terms of an improperly prevented contract are reasonably certain, the court may award lost profits based on that improperly prevented contract.<sup>264</sup>

It is hard to imagine a more appropriate situation for applying this principle, now accepted in the common law, than in the highly regulated field of government contracts. As a general matter in federal procurements, contract terms and conditions are not subject to negotiation, but are fixed ahead of time by the government, often in conformity with federal regulatory requirements or other prescribed optional contract clauses.<sup>265</sup> In solicitations in which the only open-bidding term is the price, or the quality of the proposal is evaluated in addition to price, the contract terms and conditions are certain. In these situations, indefiniteness should not prevent the contractor from suing in the Court of Federal Claims for lost profits on the ultimate contract.<sup>266</sup>

This does not mean that a successful disappointed bidder should always be able to recover lost profits or that injunctive relief should always be denied a disappointed bidder because it has a legal remedy and thus will not be irreparably harmed. Many violations of procurement law do not result in the conclusion that the disappointed bidder would have won the competition, but rather, that the bidder should be afforded an opportunity to compete for another chance to improve its competitive position.<sup>267</sup> For example, if the agency's contracting officer conducts negotiations with one or more of the offerors, but not with the aggrieved offeror after "best and final offers" have been submitted,<sup>268</sup> the aggrieved offeror's remedy is normally to have another opportunity to improve its offer, rather than the right to be awarded the contract.<sup>269</sup> Furthermore, many important interests in addition to lost profits are often at stake in a procurement action and have been recognized by the courts in considering the irreparable injury prong of the test for preliminary injunction.<sup>270</sup> Even when recovering lost profits is a potential remedy, these other interests might well dictate the grant of injunctive relief. Lost profits relief would be especially appropriate in these situations, such as when award should have been made to the disappointed bidder but is denied because of the overriding public interest mandating that the illegal procurement of the goods and services continue.<sup>271</sup>

*Robert E. Derecktor of Rhode Island, Inc. v. Goldschmidt*<sup>272</sup> and *Pace Co., Division of Ambac Industries, Inc. v. Department of Army*<sup>273</sup> illustrate these considerations. In *Derecktor* and *Pace*, the government contracting officers made

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<sup>263</sup>BURTON & ANDERSEN, *supra* note <CITE ID='FN6'>, at 362-65.<REF ID='FN193'>[fm][eb]

<sup>264</sup>*Id.* at 364-65.<REF ID='FN194'>[fm][eb]

<sup>265</sup>See *supra* notes <CITE ID='FN150A'>-<CITE ID='FN153'> and accompanying text.<REF ID='FN195'>[fm][eb]

<sup>266</sup>As discussed earlier, any action seeking contract breach damages of greater than \$10,000 must be brought in the Court of Federal Claims, rather than in the district courts. See *supra* note <CITE ID='FN166'>.<REF ID='FN196'>[fm][eb]

<sup>267</sup>See *Dynalelectron Corp. v. United States*, 659 F. Supp. 64, 69-70 (D.D.C. 1987).<REF ID='FN196A'>[fm][eb]

<sup>268</sup>The FAR requires negotiations to be reopened with *all* offerors. See FAR, 48 C.F.R. § 15.611(a) (1996).<REF ID='FN197'>[fm][eb]

<sup>269</sup>See *Airco, Inc. v. Energy Research & Dev. Admin.*, 528 F.2d 1294, 1299-1300 (7th Cir. 1975) (per curiam); *Blue Cross & Blue Shield of Md., Inc. v. United States Dep't of Health & Human Servs.*, 718 F. Supp. 80, 87 (D.D.C. 1989); *Dynalelectron*, 659 F. Supp. at 69; see also *Keco Indus., Inc. v. United States*, 492 F.2d 1200, 1205 (Ct. Cl. 1974) (appeal after decision on remand) (finding that bidder may be rejected even if all the requirements are satisfied); *Burroughs Corp. v. United States*, 617 F.2d 590, 598 (Ct. Cl. 1980) (holding that contracting officer was not required to award the contract to the plaintiff despite irregularities in the bidding process); *Pace Co., Div. of Ambac Indus., Inc. v. Department of Army*, 344 F. Supp. 787, 790 (W.D. Tenn.) (ordering a preliminary injunction after finding violations of the regulations, but not awarding contract), *rev'd per curiam sub nom. Pace Co. v. Resor*, 453 F.2d 890 (6th Cir. 1971).<REF ID='FN198'>[fm][eb]

<sup>270</sup>See, e.g., *O'Donnell Constr. Co. v. District of Columbia*, 963 F.2d 420, 428-29 (D.C. Cir. 1992) (constitutional violation); *Fort Sumter Tours, Inc. v. Andrus*, 564 F.2d 1119, 1124-25 (4th Cir. 1977) (overall effect on business); *DTH Management Group v. Kelso*, 844 F. Supp. 251, 254-55 (E.D.N.C. 1993) (effect on employees); *Abel Converting, Inc. v. United States*, 679 F. Supp. 1133, 1142 (D.D.C. 1988) (enhancement of competition); *Sterlingwear of Boston, Inc. v. United States*, 10 Cl. Ct. 644, 650 (1986) (cost savings to government); *John Carlo, Inc. v. Corps of Eng'rs of the United States Army, Fort Worth Div.*, 539 F. Supp. 1075, 1088 (N.D. Tex. 1982) (impairment of new business opportunities); *Goldhaber v. Foley*, 519 F. Supp. 466, 475 (E.D. Pa. 1981) (loss of public employment); *Robert E. Derecktor of R.I., Inc. v. Goldschmidt*, 506 F. Supp. 1059, 1066 (D.R.I. 1980) (cost savings to government); *Allis-Chalmers Corp. v. Friedkin*, 481 F. Supp. 1256, 1264 (M.D. Pa.) (increased electric rates to consumers; plant shutdown), *aff'd*, 635 F.2d 248 (3d Cir. 1980); *Art-Metal-USA, Inc. v. Solomon*, 473 F. Supp. 1, 4 (D.D.C. 1978) (overall effect on business); *Pan Am. World Airways, Inc. v. Marshall*, 439 F. Supp. 487, 497 (S.D.N.Y. 1977) (loss of follow-on contract).<REF ID='FN199'>[fm][eb]

<sup>271</sup>See *Pace*, 453 F.2d at 891; *Aero Corp. v. Department of Navy*, 549 F. Supp. 39, 44-45 (D.D.C. 1982); see also *Delta Data Sys. Corp. v. Webster*, 755 F.2d 938, 940 (D.C. Cir. 1985) (per curiam) (finding that the public interest requires setting aside a preliminary injunction and leaving plaintiff with only remedy of bid preparation costs). The burden of proof in such an action should be on the private contractor to prove that, if the breach had not occurred, it would have received the contract.<REF ID='FN200'>[fm][eb]

<sup>272</sup>506 F. Supp. 1059 (D.R.I. 1980).<REF ID='FN202'>[fm][eb]

improper responsiveness determinations--in *Derektor*, the Coast Guard's contracting officer improperly disqualified Derektor, the low bidder,<sup>274</sup> and in *Pace*, the Army's contracting officer unlawfully failed to disqualify the low bidder when Pace was next in line for award.<sup>275</sup> The district courts granted relief in both cases.<sup>276</sup> The contracting officer in *Derektor* then found the aggrieved company to be "responsible"--capable of building the Coast Guard cutters--and awarded the contract to the company.<sup>277</sup> Injunctive relief was the appropriate remedy in *Derektor*, even if lost profits had been recognized as an available remedy, because it allowed the Coast Guard to correct its error, to act consistently with the procurement laws, and to save money in two ways--by accepting Derektor's lower price and by avoiding lost profits liability to Derektor.

A different result was obtained in *Pace*. After issuance of the preliminary injunction, the Secretary of the Army represented that the Vietnam War effort would be materially affected by continuation of the injunction of the procurement of artillery shells.<sup>278</sup> The United States Court of Appeals for the Sixth Circuit ordered the injunction vacated on national defense grounds.<sup>279</sup> Although lifting the injunction was obviously correct in that situation, Pace should not have automatically been foreclosed from any remedy. The Army still had breached its good faith covenant to make an award consistent with the procurement laws,<sup>280</sup> and Pace should have been allowed to recover lost profits on the contract it was improperly denied (assuming it could show it was capable of supplying the shells). The terms of the improperly denied contract were fixed by the Army's solicitation and by Pace's bid prices and, thus, were not subject to any debilitating indefiniteness.<sup>281</sup>

Finally, the fact that the improperly withheld government contract would have contained a termination-for-convenience clause should not foreclose the disappointed bidder's recovery of lost profits. It should not be assumed that the government would arbitrarily exercise the termination-for-convenience clause to extricate itself from a contract it should have made. Rather, it should be understood that the government could properly exercise the termination-for-convenience clause only if there were changed conditions. Existence of changed conditions should be considered as a question of fact in each case. If, as was the case in *Pace*, the contract that was improperly awarded to another bidder is still in force and has not been terminated in whole or in part, then presumably there would be no reason to assume that the disappointed bidder's contract would have been terminated. On the other hand, if the improperly awarded contract has been terminated for legitimate reasons (and not as a ruse to attempt to avoid the payment of lost profits), then it could normally be assumed that the disappointed bidder's contract would have been terminated for convenience as well.<sup>282</sup> Whether lost profits from a "follow-on" procurement should additionally be awarded should also be a fact-specific inquiry. For instance, if there were renewed competition for the follow-on contract, it would be speculative as to who would win that competition. If, however, the improperly awarded contract has put the winning bidder in a sole-source position, it presumably would have put the aggrieved bidder in a sole-source position, too. If future requirements are projected, then lost profits could be awarded for the follow-on procurement as well.<sup>283</sup>

Congress, in its recent amendment of section 1491, had the (probably unintended<sup>284</sup>) consequence of stifling the ability of the courts to apply the common law with respect to lost profits. In expanding the scope of section 1491 to include

(...continued)

<sup>273</sup>344 F. Supp. 787 (W.D. Tenn.), *rev'd per curiam sub nom. Pace Co. v. Resor*, 453 F.2d 890 (6th Cir. 1971).<REF ID='FN203'>[fm][eb]

<sup>274</sup>*Derektor*, 506 F. Supp. at 1060-61, 1064-66.<REF ID='FN204'>[fm][eb]

<sup>275</sup>*Pace*, 344 F. Supp. at 788-90.<REF ID='FN205'>[fm][eb]

<sup>276</sup>*Derektor*, 506 F. Supp. at 1067 (declaring the initial award invalid); *Pace*, 344 F. Supp. at 790 (granting a preliminary injunction).<REF ID='FN206'>[fm][eb]

<sup>277</sup>*Robert E. Derektor of R.I., Inc. v. Goldschmidt*, 516 F. Supp. 1085, 1090 (D.R.I. 1981).<REF ID='FN207'>[fm][eb]

<sup>278</sup>*Pace*, 453 F.2d at 891.<REF ID='FN565A'>[fm][eb]

<sup>279</sup>*Id.*<REF ID='FN208'>[fm][eb]

<sup>280</sup>*Pace*, 344 F. Supp. at 790.<REF ID='FN208A'>[fm][eb]

<sup>281</sup>*Id.* at 788.<REF ID='FN208B'>[fm][eb]

<sup>282</sup>If the government determined that it had illegally awarded the contract, it would, of course, be appropriate for the government to terminate for convenience and then to either reprocure or award to the proper bidder. See *John Reiner & Co. v. United States*, 325 F.2d 438, 443-44 (Ct. Cl. 1963). In taking such action, the government could limit its potential lost profits damages to the contractor initially improperly denied the contract.<REF ID='FN209'>[fm][eb]

<sup>283</sup>See *Rogerson Aircraft Corp. v. Fairchild Indus., Inc.*, 632 F. Supp. 1494, 1503 (C.D. Cal. 1986) (holding that spare parts sales were reasonably contemplated if the base contract had not been breached and, thus, lost profits on those later expected sales are recoverable).<REF ID='FN210'>[fm][eb]

<sup>284</sup>See *infra* note <CITE ID='FN817'> and accompanying text.<REF ID='FN811'>[fm][eb]

district courts, Congress also extended to district courts the power to "award any relief that the court considers proper."<sup>285</sup> District courts generally do not have authority to grant monetary relief in contract actions,<sup>286</sup> and Congress restricted the ability of both the district courts and the Court of Federal Claims as follows: "[A]ny monetary relief shall be limited to bid preparation and proposal costs."<sup>287</sup> It seems likely that this language will stifle any award of lost profits, even in situations in which they would be granted under the common law.<sup>288</sup>

That conceded, at the same time, nothing in the legislative history indicates a congressional desire to put the government in a position superior to private parties in the marketplace.<sup>289</sup> Rather, the most obvious intent from the face of the revised statute is that Congress did not want to permit an overbroad exception to the generally exclusive jurisdiction of the Court of Federal Claims to award monetary damages for breach of contract.<sup>290</sup> When Congress reconsiders section 1491, it should amend it once again to serve both of these interests.<sup>291</sup> Congress should amend new section 1491(b)(2) to read as follows:

To afford relief in such an action, the courts may award any relief that the court considers proper, including declaratory and injunctive relief, except that any monetary relief in such an action shall not be available in the district courts unless under \$10,000 in amount.

This language would maintain the traditional division of authority between the district courts and the Court of Federal Claims<sup>292</sup> and, at the same time, would allow aggrieved parties to recover lost profits in circumstances in which it would be appropriate under the common law, once again placing the federal government on an equal footing in the marketplace with the citizens with whom it contracts.

#### IV. CONCLUSION

When the government enters the marketplace, it should be subject to the same contractual good faith duties as is a private party. Although this principle is adhered to in theory and also in practice with respect to many government contracting performance situations, it has not been uniformly followed in termination and formation situations. Government contracts tribunals should recognize openly that termination-for-convenience clauses, while giving the government a significant amount of discretion, must nevertheless be exercised in good faith—that is, in a manner consistent with the justified expectations of the parties and not to recapture opportunities foreclosed at the time of contracting. This open recognition by government contracts tribunals would vindicate the Supreme Court's proclamation

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<sup>285</sup> Pub. L. No. 104-320, § 12(a)(3), 110 Stat. 3870, 3874 (1996) (to be codified at 28 U.S.C. § 1491(b)(2)).<REF ID=FN812>[fm][eb]

<sup>286</sup> See *supra* note <CITE ID=FN166>.<REF ID=FN813>[fm][eb]

<sup>287</sup> § 12(a)(3), 110 Stat. at 3874 (to be codified at 28 U.S.C. § 1491(b)(2)).<REF ID=FN814>[fm][eb]

<sup>288</sup> Arguably, a separate action could be brought in the Court of Federal Claims, not seeking equitable relief, but seeking lost profits in lieu of bid and proposal costs. Such a suit would be analogous to suits litigants now bring for bid and proposal costs under section 1491(a). See, e.g., *Finley v. United States*, 31 Fed. Cl. 704, 708 (1994) (seeking bid and proposal costs); *TRW, Inc. v. United States*, 28 Fed. Cl. 155, 162 (1993) (same).<REF ID=FN815>[fm][eb]

<sup>289</sup> See 142 CONG. REC. S6156-57, S6161-63 (daily ed. June 12, 1996); H.R. REP. NO. 104-841, *reprinted in id.* at H11108-11 (daily ed. Sept. 25, 1996); *id.* at H11448 (daily ed. Sept. 27, 1996); *id.* at S11848 (daily ed. Sept. 30, 1996); *id.* at H12276 (daily ed. Oct. 4, 1996).<REF ID=FN816>[fm][eb]

<sup>290</sup> See *supra* note <CITE ID=FN166>. Congress might also have been reacting to the decision in a Court of Federal Claims case that awarded the costs of litigation, as "bid protest" costs. See *Grumman Data Sys. Corp. v. United States*, 28 Fed. Cl. 803, 807-10 (1993). The original Senate bill, S.1224, which was incorporated in H.R. 2977 as an amendment, divested the district courts of jurisdiction entirely and did not contain any language limiting the monetary relief that the Court of Federal Claims could grant. See 142 CONG. REC. S6161-63 (daily ed. June 12, 1996). The limiting language was inserted without discussion of its purpose in the legislative history. Its absence in the bill when the district courts were divested of jurisdiction and its presence when they were not suggests the language was intended to limit the district courts from granting relief traditionally reserved to the Court of Federal Claims.<REF ID=FN817>[fm][eb]

<sup>291</sup> Congress will be reconsidering its amended section 1491 soon in conjunction with the study it has ordered the General Accounting Office to undertake. See § 12(c), 110 Stat. at 3875. Such was the compromise struck between the House, which passed a bill with concurrent jurisdiction of the Court of Federal Claims and the district courts, and the Senate, which passed a bill divesting the district courts of *Scanwell* jurisdiction. See 142 CONG. REC. S6156-57, S6161-63 (daily ed. June 12, 1996); H.R. REP. NO. 104-841, *reprinted in id.* at H11108-11 (daily ed. Sept. 25, 1996); *id.* at H11448 (daily ed. Sept. 27, 1996); *id.* at S18848 (daily ed. Sept. 30, 1996); *id.* at H12276 (daily ed. Oct. 4, 1996).<REF ID=FN818>[fm][eb]

<sup>292</sup> Under the Little Tucker Act, the district courts have concurrent jurisdiction with the Court of Federal Claims of contract actions under \$10,000. 28 U.S.C. § 1346(a)(2) (1994). Under new section 1491(b)(2), the \$10,000 limit would apparently not apply for district court awards of "bid preparation and proposal costs." § 12(a)(3), 110 Stat. at 3874 (to be codified at 28 U.S.C. § 1491(b)(2)).<REF ID=FN819>[fm][eb]



that the government cannot abort its contractual obligations simply because it made a bad bargain.<sup>293</sup> Likewise, those decisions holding that the government cannot use a termination-for-convenience clause simply to avail itself of a better bargain would be given a firmer conceptual foundation. Although subjective bad faith in appropriate cases would be a strong indication of a breach of good faith duties, it should not be necessary to prove subjective bad faith to find that the government has abused its discretion to terminate for convenience.

Government contracts tribunals and Congress should also bring contract formation law in line with common law good faith precedent. They should uniformly recognize that the framework of laws and regulations concerning government procurement form the substance of the justified expectations of the parties which, if violated, also violate the government's good faith duties incorporated in its implied contract to treat bidders fairly, honestly, and impartially. Moreover, in appropriate circumstances, a disappointed bidder in a government contract should be able to recover lost profits on the contract that the bidder was unlawfully denied, similar to disappointed contracting parties under the common law.

When the government enters the marketplace, it "contracts as does a private person, under the broad dictates of the common law."<sup>294</sup> This should be as true with respect to the covenant of good faith as it is with respect to any other contractual duties. It should be as true with respect to the termination and formation of government contracts as it is with respect to their performance.

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<sup>293</sup> See *United States v. Mississippi Valley Generating Co.*, 364 U.S. 520, 565-66 (1961) ("Of course, the Government could not avoid the contract merely because it turned out to be a bad bargain."); see also *Lynch v. United States*, 292 U.S. 571, 580 (1934) ("The United States are as much bound by their contracts as are individuals. If they repudiate their obligations, it is as much repudiation, with all the wrong and reproach that term implies, as it would be if the repudiator had been a State or a municipality or a citizen." (quoting *Sinking Fund Cases*, 99 U.S. 700, 719 (1879))).<REF ID="FN211">[fm][eb]

<sup>294</sup> *Tornello v. United States*, 681 F.2d 756, 762 (Ct. Cl. 1982) (en banc).<REF ID="FN212">[fm][eb]