ARMED SERVICES BOARD OF CONTRACT APPEALS

Appeal of --	)	
	)	
Blue Cross and Blue Shield Association	)	ASBCA No. 53632
	)	
Under Contract No. CS 1039	)	

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OPINION BY ADMINISTRATIVE JUDGE PEACOCK
ON MOTIONS FOR SUMMARY JUDGMENT

The parties dispute the allowability of state franchise taxes paid by appellant during 1991 through 1995 and have filed cross motions for summary judgment.[1] Neither party supported its motion with affidavits and appellant contends it needs discovery on some points. We grant appellant's motion in part concluding that the government is contractually time-barred from asserting the present claim with respect to years 1991 though 1993. The motions are denied with respect to 1994 and 1995.

FINDINGS OF FACT FOR PURPOSES OF THE MOTIONS

1. The Office of Personnel Management (OPM or the government) administers the federal employee health benefit program established by the Federal Employees Health Benefit Act (FEHBA) (5 U.S.C. Chapter 89) and contracts with health benefit carriers to offer health benefit plans to federal employees, their families and retirees. The referenced contract for the government-wide Service Benefit Plan was entered into between OPM

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[1] "OPM's Motion for Summary Judgment" (OPM mot.) is dated 6 November 2002. Appellant filed its "Opposition to OPM's Motion for Summary Judgment and . . . Cross Motion For Summary Judgment" (app. cross mot.) on 9 December 2002. OPM filed a "Reply" (OPM reply) to app.'s cross mot. on 23 January 2003. Appellant submitted a "Reply" (app. reply) to the OPM reply on 23 February 2003. OPM filed a "Surreply" (OPM surreply) to app.'s reply on 17 March 2003.

and Blue Cross and Blue Shield Association (BCBS or appellant) which acts on behalf of local participating BCBS plans in various geographic service areas in the United States. Anthem Blue Cross and Blue Shield (Anthem) (sometimes referred to as Blue Cross and Blue Shield of Cincinnati) is one of those local participating plans providing coverage in Ohio. Anthem authorizes BCBS to enter into the Service Benefit Plan through a Plan Participation Agreement, under the terms of which BCBS acts as Anthem's agent and issues uniform practices and procedures to its participating plans, including Anthem. The Service Benefit Plan is funded by contributions from enrollees and the government and placed into a Fund in the U.S. Treasury administered by OPM from which BCBS was, during the period relevant to this dispute, reimbursed for benefit payments, administrative expenses and other allowable retentions. (5 U.S.C. § 8909(a); 48 C.F.R. §§ 1602.170-6, 1632.170(b) (1991-1995); R4, tabs 1, 9)

2. Section 1.15 of the contract, which became effective on 1 January 1960, states that it "renews automatically for a term of one (1) year each January first, unless written notice of non-renewal" is given by either party. The contract has been renewed annually and the years 1991 through 1995 are in issue in this appeal. (R4, tabs 9-13)

3. The FEHBA was amended in 1990 by Pub. L. No. 101-508 § 7002(c), 5 U.S.C. § 8909(f), to provide in pertinent part as follows:

> (1) No tax, fee, or other monetary payment may be imposed, directly or indirectly, on a carrier or an underwriting or plan administration subcontractor of an approved health benefits plan by any State, the District of Columbia, or the Commonwealth of Puerto Rico, or by any political subdivision or other governmental authority thereof, with respect to any payment made from the Fund.
>
> (2) Paragraph (1) shall not be construed to exempt any carrier or underwriting or plan administration subcontractor of an approved health benefits plan from the imposition, payment, or collection of a tax, fee or other monetary payment on the net income or profit accruing to or realized by such carrier or underwriting plan administration subcontractor from business conducted under this chapter if that tax, fee or payment is applicable to a broad range of business activity.

4. The FEHBA authorizes OPM to promulgate implementing regulations. 5 U.S.C. § 8913(a). Pursuant to this authority, OPM has promulgated two pertinent Federal Employees Health Benefits Acquisition Regulation (FEHBAR) provisions:

FEHBAR 1631.205-41 and FEHBAR 1652.216-71. FEHBAR 1631.205-41, effective 12 December 1991, states:

> 5 U.S.C. § 8909(f)(1) prohibits the imposition of taxes, fees, or other monetary payment, directly or indirectly, *on FEHB premiums* by any State, the District of Columbia, or the Commonwealth of Puerto Rico, or by any political subdivision or other governmental authority of those entities. Therefore, FAR 31.205-41 is modified to include those taxes as unallowable costs. The prohibited payments, referred to elsewhere in these regulations as *"premium taxes,"* applies to all payments directed by States or municipalities, regardless of how they may be titled, to whom they must be paid, or the purpose for which they are collected, and it applies to all forms of direct and indirect measurements on *FEHBP premiums*, however modified, to include cost per contract or enrollee, with the sole exception of a tax on net income or profit, if that tax, fee, or payment is applicable to a broad range of business activity.

(Emphasis supplied)

5. FEHBAR 1652.216-71(b)(2)(ii) provides, "Unless otherwise stated in the contract, administrative expenses include, in part: all taxes (excluding premium taxes, as provided in section 1631.205-41). . . ." FEHBAR 1652.216-71(b)(2)(iv)(B) defines "premium taxes" as "a tax, fee, or other monetary payment directly or indirectly imposed on FEHB premiums by any State, ... with the sole exception of a tax on net income or profit, if that tax, fee, or payment is applicable to a broad range of business activity."

6. The contract incorporated by reference "applicable provisions" of the FEHBA, Federal Acquisition Regulation (FAR) (*see* 48 C.F.R. Chapter 1) and the FEHBAR. The above amendment to the FEHBA, sometimes referred to by the parties as the preemption provision, was incorporated into the contract by reference effective with respect to contract years beginning on or after 1 January 1991 (R4, tab 9 at § 1.4). The verbatim text of the FEHBA amendment was also set forth in Part IV – Special Provisions of the 1991 contract as an amendment to § 3.2(b)(ii) (R4, tab 9 at IV-2). The contract further stated that, "If the Regulations are changed in a manner which would increase the Carrier's Liability under this contract, the change will be made effective for the contract period subsequent to the period in which the amendment to the Regulations is enacted or promulgated. . . ." (R4, tab 9 at § 1.4(b))

7. For contract years 1991 through 1994, contract § 3.2, ACCOUNTING AND ALLOWABLE COST (JAN 1991) stated in relevant part (R4, tab 9 at III-1):

> (a) Annual Accounting Statement.
>
> (1) The Carrier, not later than the date specified by the contract, shall furnish to OPM for that contract period an accounting of its operations under the contract. The accounting shall be in the form prescribed by OPM and shall include, among other things, a Balance Sheet and a Summary Statement of FEHBP Financial Operations. The Summary Statement of FEHBP Financial Operations shall include the following items for each option provided by the contract:
>
> (i) Subscription income received and accrued (including amounts received from the Contingency Reserve);
>
> (ii) Health Benefits charges paid and accrued;
>
> (iii) Administrative expenses and other charges paid and accrued;
>
> (iv) Income on investments;
>
> (v) Other adjustments;
>
> (vi) Sum of items (i) minus (ii) minus (iii) plus (iv) plus or minus (v).
>
> . . . .
>
> (b) Definition of costs.
>
> (1) The allowable costs chargeable to the contract for a contract period shall be the actual, necessary and reasonable amounts incurred with proper justification and accounting support, determined in accordance with the terms of this contract, Subpart 31.2 of the Federal Acquisition Regulation (FAR) and Subpart 1631.2 of the Federal Employees Health Benefits Acquisition Regulation (FEHBAR) applicable on the first day of the contract period.
>
> (2) In the absence of specific contract terms to the contrary, contract costs shall be classified in accordance with the following criteria:
>
> (i) Benefits. Benefit costs consist of payments made and liabilities incurred for covered health care

services on behalf of FEHBP subscribers less any refunds, rebates, allowances or other credits received.

(ii) Administrative expenses. Administrative expenses consist of all allocable, allowable and reasonable expenses incurred in the adjudication of subscriber benefit claims or incurred in the Carrier's overall operation of the business. Unless otherwise stated in the contract, administrative expenses include, in part: all taxes (except that premium taxes are considered "other charges"[1]). . . .

(iii) Investment income. The Carrier is required to invest and reinvest all funds on hand, including any in the Special Reserve or any attributable to the reserve for incurred but unpaid claims, which are in excess of the funds needed to discharge promptly the obligations incurred under the contract.

(iv) Other charges. (A) Mandatory statutory reserve. Charges for mandatory statutory reserve are not allowable unless specifically provided for in the contract. . . . (B) Premium taxes. When the term "premium taxes" is used in the contract without further definition or explanation, it means a tax imposed by State or local statutes upon the Carrier's gross or net premiums received.[1]

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1 As amended in Article IV.

8. Footnote 1 referenced in § 3.2(b)(2)(ii) and (iv) above states, "As amended in Article IV" referring to the verbatim text of the FEHBA amendment quoted in Part IV – Special Provisions (*see* finding 6, *supra)* (R4, tab 9 at III-2, IV-2).

9. The second sentence of § 3.2(b)(2)(ii), "Administrative expenses," was amended in 1995 to state, "Unless otherwise stated in the Contract, administrative expenses include, in part: all taxes (excluding taxes, as provided in section 1631.205-41). . . ." (R4, tab 13 at 2)

10. Section 3.3(a) SPECIAL RESERVE (JAN 1991) stated in part, "The cumulative gain or loss on operations under this contract [item (a)(1)(vi) in Section 3.2, Accounting and Allowable Cost] constitutes the Special Reserve held by or on behalf of the Carrier to be used only for payment of charges against this contract." Section 3.7 SERVICE CHARGE

(JAN 1991) states in part, "Any service charge negotiated . . . shall be the total profit that can be charged to the contract." (R4, tab 9)

11. Section 3.4 INVESTMENT INCOME (JAN 1991) (FEHBAR), requires BCBS to invest all excess FEHB funds with investment income credited to the Special Reserve. To the extent that BCBS receives payment, *inter alia*, for unallowable costs, it is obligated to reimburse the Fund not only the principal amount of the unallowable costs, but also associated "lost investment income" that would have been earned by the principal amount, had BCBS not received the payment. (R4, tab 9 at § 3.4) As relevant to this appeal, the contract requires BCBS to pay interest on amounts due the government from the date of the Contracting Officer's (CO) final decision asserting a government claim for reimbursement (R4, tab 9 at § 5.34(b)(2)).

12. BCBS is required to file its Annual Accounting Statement (AAS) within 120 days after the close of each calendar year (R4, tab 9 at § 4.1(g)). Although the calendar date varies, the parties have used 30 April of each year as the required filing date for convenience and we adopt that practice herein. The contract's AUDIT DISPUTES (JAN 1991) clause set forth a contractual statute of limitations requiring, as relevant here, that government claims must be asserted in a contracting officer's final decision no later than 5 years following the due date for the AAS (R4, tab 9 at ¶¶ 4.7-4.8, ex. B, Letter of Agreement of 17 Dec. 1980). For example, for contract year 1991, the CO's final decision must be issued no than later 30 April 1997, five years following the due date for the 1991 contract year AAS of 30 April 1992.

13. During the period relevant to this appeal, the State of Ohio levied an "Annual Franchise Tax for Domestic Insurance Companies" (hereinafter the Ohio Franchise Tax). The statutory provision imposing the tax stated, at Ohio Rev. Code Ann. § 5725.18 (1991-1995):

> An annual franchise tax on the privilege of being an insurance company is hereby levied on each domestic insurance company. In the month of May, annually, the treasurer of state shall charge for collection from each domestic insurance company a franchise tax in the amount computed in accordance with division (A) or (B) of this section, whichever is less:
>
> (A) Six-tenths of one per cent of the value of the capital and surplus of a domestic insurance company having capital divided into shares, or the value of the surplus of a domestic insurance company not having capital divided into shares, as reported by the company in its annual statement for the

preceding year filed with and approved by the superintendent of insurance setting forth the admitted and nonadmitted assets and the liabilities of the company, including in such liabilities:
(1) The reserve and unearned premium liabilities computed as provided by law, which is the amount of debts of an insurance company because of its outstanding policies in gross;
(2) Amounts set apart for the payment of dividends to policyholders, and all actual liabilities set forth in the annual statement.

(B) Two and one-half per cent of the gross amount of premiums received by any such domestic insurance company from policies covering risks within this state during the preceding calendar year, after making the deductions prescribed by section 5729.03 of the Revised Code for foreign insurance companies. The objects of such tax are those declared in section 5725.24 of the Revised Code, to which only such tax shall be applied.

(C) In no case shall such tax be less than twenty-five dollars.

14. The above Ohio Franchise Tax requires insurance companies to use the calculation method resulting in the lowest tax liability. Anthem used the capital/surplus method to calculate the lowest tax liability for 1991 though 1995 (R4, tab 1 at 23).

15. The Ohio Franchise Tax is imposed on all domestic insurance companies, not solely health insurance companies, operating within Ohio in lieu of a state corporate income tax. Ohio Rev. Code Ann. § 5733.09. In Ohio, the corporate income tax (from which insurance companies are exempt) is measured by the net income or net worth of the corporation, whichever produces the greater tax (Ohio Rev. Code Ann. §§ 5733.05, 5733.06). It is also referred to as a franchise tax that is levied on a corporation "for the privilege of exercising its franchise during the calendar year in which the amount is payable." Ohio Rev. Code Ann. § 5733.01 (1991-1995).

16. The contract requires the carrier to retain records applicable to a contract term for five years after the end of the term and make them available for examination and audit (R4, tab 9 at §§ 3.8, 5.7). Thus OPM had until 31 December 1996 to audit records for 1991. The audit of Anthem for the years in dispute (1991 through 1995) began on 28 October 1996 (R4, tab 1).

17. On 27 January 1997, OPM issued Informal Audit Inquiry Number 14. The audit inquiry questioned only Anthem's method of allocating Ohio Franchise Taxes for Calendar Year 1991 but did not otherwise question any other aspect of the allowability of Ohio Franchise Taxes paid (app. cross mot. at ex. 1).

18. As noted above, the contract required the contracting officer to issue any final decision, *inter alia*, disallowing costs pertaining to calendar year 1991, no later than 30 April 1997 unless a waiver of the contractual time limitation was approved. On 30 April 1997, the parties entered into a 240 day waiver and extension of the time period, through 31 December 1997, for "All Costs Incurred" for Anthem's 1991 calendar year (OPM reply at attach. B-1, item 7; app. cross mot. at ex. 3).

19. A second waiver of the time limitation was granted by appellant on 18 December 1997, extending the waiver period through 30 April 1998, identifying "Excess Franchise Taxes" as one of the issues to which the waiver applied (OPM reply at attach. B-2, item 5).

20. On 9 April 1998, OPM issued its "Draft of A Proposed Report" (hereinafter the Draft Audit Report) covering, *inter alia,* Anthem's administrative expenses for contract years 1991 through 1995 (OPM reply, attach. A at i). With respect to "Franchise Taxes," the Draft Audit Report questioned solely the allocation method used by Anthem to allocate franchise taxes incurred for the years in dispute to cost objectives. Specifically, the Draft Audit Report determined that OPM had been overcharged $203,255 because the "prior year revenue" allocation base used by Anthem to allocate franchise taxes to the Plan failed to include certain lines of business. As a result, the report recommended that the contracting officer disallow that amount of "excess franchise taxes" and further recommended that the Plan be directed "to implement a cost allocation method that equitably allocates franchise taxes to all benefiting cost objectives." (*Id.* at 18) There is no indication in the Draft Audit Report that OPM otherwise questioned the allowability of the franchise taxes.

21. On 29 April 1998, appellant entered a third extension of the limitations period for issuance of final decisions (third waiver) with respect to calendar year 1991 and 1992 costs, authorizing an extension through 30 April 1999. The third waiver referenced the Draft Audit Report and identified in particular the "Excess Franchise Tax" issue. The third waiver tracked the categories of questioned costs set forth in the Draft Audit Report as relevant for years 1991 and 1992. There is no evidence that the scope of the waiver exceeded the scope of the Draft Audit Report. (OPM reply, attach. B-3 at 3, 5)

22. By letter dated 3 August 1998, appellant responded to the Draft Audit Report disputing, *inter alia,* the audit finding that the $203,255 amount of questioned franchise taxes was not properly allocable (R4, tab 1 at appendix).

23. In March 1999, the parties entered into an agreement entitled "Settlement of Lost Investment Income" (SLII Agreement) regarding all BCBS FEHB Plans, including the Anthem Plan. The purpose of the SLII Agreement was to resolve general issues related to the payment of LII on audit findings and set forth "principles to calculate actual amounts due the FEHB Program by the BCBS Association (BCBSA)." (R4, tab 14) Paragraphs 1-2 and 7 of the SLII Agreement stated in pertinent part:

> 1. This settlement applies to all pending audit appeals and all pending audits as of the date of this Agreement. . . .
>
> 2. If a contractual limitation precludes the pursuit of an audit finding, it also precludes the pursuit of LII. If OPM and BCBS waived the time limitation with respect to any principal amount, the waiver also applies to the LII associated with that amount.
>
> . . . .
>
> 7. For unallowable administrative costs, the calculation of the LII will be according to the provisions in the FEHBAR . . . applicable on the date the cost was incurred.

(*Id* at 1-2)

24. The fourth waiver, executed by appellant on 30 April 1999, extended the limitations period for issuing final decisions through 30 April 2000 with respect to disputes concerning calendar year 1991, 1992 and 1993 costs. The fourth waiver also referenced the Draft Audit Report and identified in particular the "Franchise Tax" issue. The fourth waiver again substantially tracked the categories of questioned costs set forth in the Draft Audit Report and there is no evidence that the fourth waiver exceeded the scope of that report for 1991 through 1993. (OPM reply, attach. B-4 at 3, 6, 8, 15)

25. No waivers of the limitations period were executed by the parties relative to franchise taxes incurred in calendar years 1994 and 1995.

26. On 2 June 1999, OPM issued its Final Audit Report covering administrative expenses for the years 1991 through 1995 (R4, tab 1). For the first time, the Final Audit Report "revised our original franchise tax finding to question the total amount of franchise taxes [*i.e.*, $498,647] claimed by the Plan during the audited years" (*id.* at 22). Citing the statutory amendment (finding 3) and its implementation in FEHBAR 1631.205-41 (finding 4), the Final Audit Report stated in part:

> The Ohio State tax law allows the Plan to base its franchise tax calculation on either capital/surplus or premiums.
>
> State taxes on FEHBP premiums are unallowable FEHBP expenses. Had the Plan used premiums as its base to calculate the franchise tax, FEHBP would not have been charged any tax amount. The Plan has instead opted to base its calculation of the franchise tax on capital/surplus during the audit period.
>
> Capital/surplus is not "net income or profit" as required in the regulations. The surplus of a corporation is the excess of its assets over its liabilities plus stated capital, if any, as of a certain date. Net income or profit is the excess of its revenues over expenses from operations for the year. Therefore, the franchise tax calculated based on capital/surplus is also an unallowable expense in accordance with FEHBAR. For example, in 1994, the Plan had reported in its audited financial statements surplus and net income of $447.4 million and $49.5 million, respectively. The Plan used the surplus of $447.4 million in the franchise tax calculation.
>
> Alternatively, if the tax is found to be allowable, the Plan did not fairly allocate the franchise tax to the FEHBP during the audited period. The Plan excluded certain lines of business from the allocation base for the franchise tax in violation of the requirements of 48 CFR 31.201-4. FEHBAR, Section 1631.205-41 states that net income or profit tax must be applicable to a broad range of business activity. Since the Plan did not take into consideration all lines of business in its allocation process, the tax amount was not equitably allocated to the FEHBP.

(*Id.* at 22-23)

27. The AUDIT DISPUTES clause was modified beginning with contract year 2000, effective 1 January 2000. Section 4.4(c) of the modified clause is identical to the clause in the earlier contracts setting forth the five year time limit for issuance of final decisions (*see* finding 12, above). In addition, the revised clause contains two new paragraphs at § 4.4(a) and (b). (App. cross mot. at tab 6) Section 4.4(a) is relevant to this dispute, stating:

> a) Any questioned costs or issues documented by or on behalf of OPM's Office of the Inspector General (OIG) in draft or final audit reports examining the Carrier's and Participating Plans' performance under this contract, that are provided to the Carrier and that were initially raised [within five years], remain open until resolved. Audit issues related to monetary findings for which extensions of the waiver period for issuance of final decisions . . . were obtained in previous contract terms also remain open until resolved.

28. By letters dated 31 March and 25 July 2000, OPM reasserted the position taken in the Final Audit Report that the all franchise taxes for the years in dispute were unallowable (R4, tabs 4-5). In a letter dated 12 September 2000, appellant agreed with the audit conclusions concerning how the taxes should be allocated but otherwise disputed OPM's questioning of their allowability (R4, tab 6).

29. By final decision dated 17 September 2001, the contracting officer adopted the conclusions of the Final Audit Report that all franchise taxes paid during the years in dispute were unallowable. The CO determined that the BCBS owed the FEHB Program $498,647 in franchise taxes, $229,979 in lost investment income on the taxes, and any additional accrued LII and interest from 30 September 2001. (R4, tab 8)

DECISION

Summary judgment is properly granted where no genuine issue of material fact is present and the movant is entitled to judgment as a matter of law. *Mingus Constructors, Inc. v. United States,* 812 F.2d 1387, 1390 (Fed. Cir. 1987). Inferences must be drawn in favor of the party opposing summary judgment. *Hughes Aircraft Co.,* ASBCA No. 30144, 90-2 BCA ¶ 22,847. The Board's task is not to resolve factual disputes but to ascertain whether material disputes of fact exist. *General Dynamics Corp.,* ASBCA Nos. 32660, 32661, 89-2 BCA ¶ 21,851. Summary judgment may be denied if "there is reason to believe that the better course would be to proceed to a full trial." *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 255 (1986).

The government argues that franchise tax costs paid by Anthem to the state of Ohio are not allowable and seeks to recover the amount of the taxes paid during 1991 through 1995 along with associated Lost Investment Income (LII). Appellant alleges that the contracting officer's decision was not timely issued within the limitations period prescribed in the AUDIT DISPUTES clause and, accordingly, the claim is time-barred. Alternatively, appellant maintains that the Ohio Franchise Tax was not imposed directly or indirectly on premiums and, to the extent, if any, the tax was imposed on premiums received by appellant, the tax fell within the "net income or profit" exception. Appellant

further contends that the preemption of the Ohio Franchise Tax would constitute a prejudicially retroactive disallowance.

We conclude that the government claim is contractually time-barred with respect to 1991 through 1993 and that the presence of genuine issues of material fact precludes disposition of this appeal by summary judgment for 1994 and 1995 costs.

A. Contractual Limitations Period for Assertion of Claims

The contract's AUDIT DISPUTES clause set forth a limitations period within which the contracting officer was required to issue a final decision. That clause required issuance of a final decision no later than five years following the last date for filing the Annual Accounting Statement for each contract year. The AAS was due no later than 30 April following the end of each year of performance. Thus, for example, the final decision was required to be issued by 30 April 1999 for contract year 1993 and by 30 April 2001 for contract year 1995, the last year involved in this dispute. In this case, the final decision was issued on 17 September 2001. Consequently, the government claim (pertaining to contract years 1991 through 1995) contained in that decision is time-barred unless the limitations period was waived or rendered timely by the parties' modification of the AUDIT DISPUTES clause beginning with contract year 2000. Contract years 1991 through 1993 require us to address both the import of the final, fourth waiver as well as the modified clause. Because no waivers were issued pertaining to contract years 1994 and 1995, only interpretation of the modified clause is required as to those years.

1. Contract Years 1991 through 1993

a. The Waivers

The parties entered into a series of waivers (eventually covering 1991 through 1993) bilaterally extending the specified limitations period. These waivers ultimately, however, did not preserve the government's claim for the reasons discussed below.

On 9 April 1998, OPM issued its Draft Audit Report which, as relevant here, questioned solely the method used to allocate the total franchise tax cost. No other factor relating to the allowability of that cost was raised in the Draft Audit Report. Because only allocability was challenged, that report questioned only $203,255 of the total taxes paid ($498,647).

Thereafter, the parties executed the third and fourth waivers extending the limitations period for issuance of a final decision. The fourth and final waiver of 30 April 1999 encompassed 1991, 1992 and 1993 and extended the period through 30 April 2000.

Both the third and fourth waiver referenced the Draft Audit Report and issues raised therein. Although both the Draft and Final Audit Reports group and treat all years (1991 through 1995) collectively, the scope of the waivers is of critical importance because we consider that scope to control whether the government's claim was timely asserted to the extent it disallows 1991 through 1993 costs.

The period for assertion of claims pertaining to years 1994 and 1995 was not addressed in the waivers because contractually that period already extended to 30 April 2000 and 30 April 2001, respectively. Thus, no waivers were required for the latter two years at the time the fourth waiver was signed.

The government's Final Audit Report was issued in June 1999. For the first time, the auditors asserted that the entire amount of appellant's franchise tax costs were unallowable under FEHBAR 1631.205-41.[2] We consider that this was a new government claim that was not covered by the unexpired fourth waiver. The fourth waiver (as well as the third waiver) merely tracked the categories of questioned costs set forth in the Draft Audit Report. There is no evidence that the scope of the fourth waiver exceeded the scope of the Draft Audit Report.

The government argues that the Draft Audit Report identification and waiver coverage of the allocability issue was sufficient to preserve any issue relating to franchise tax cost allowability. This argument ignores fundamental, well established concepts and distinctions routinely applied in government contract accounting. Allocability is not synonymous with allowability; it is merely one factor to be considered in determining allowability. *E.g.,* FAR 31.201-2. Other allowability factors for consideration include whether the costs are "reasonable," compliant with Generally Accepted Accounting Principles (if applicable) and, most importantly for purposes of this case, whether the costs are subject to express limitations or exclusions set forth in the contract and/or applicable cost principles and regulations. *Id.* Here, if the authors of the Draft Audit Report considered Ohio Franchise Tax costs to be wholly unallowable by virtue of the FEHBAR provisions implementing the amended FEHBA, it made little sense to question only a portion of the tax cost and address only the more narrow issue of whether the questioned portion was properly allocated to the contract. Unlike the Final Audit Report that raised both the broad FEHBAR limitation and more narrow allocability issues, the draft report identified only the question of allocability.

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[2] Alternatively, the report maintained that a portion of the costs were not properly allocated for the reasons set forth in the Draft Audit Report. Appellant has since concurred with the government's position on how the tax costs should be allocated and that issue is not before us.

We conclude that the waivers did not address and preserve the present government claim. Accordingly that claim is time-barred unless it was preserved under the contract year 2000 modification of the AUDIT DISPUTES clause.

b. Modification of Contract - AUDIT DISPUTES Clause

No additional waivers were executed following issuance of the Final Audit Report. However, the AUDIT DISPUTES clause was modified commencing with contract year 2000 (finding 27). The government argues that the modified clause preserved its right to assert government claims for all years in dispute, including 1991 through 1993. We agree with OPM that the present government claim disallowing all franchise costs for 1994 and 1995 is timely by virtue of the modification of the clause as discussed below. However, the clause does not permit the government to assert a new claim for years 1991 through 1993 first conceived in the Final Audit Report.

The pertinent revisions of the clause are set forth in its two initial sentences. The first sentence requires that, for the "questioned costs or issues" identified in audit reports to remain open, they must be "initially raised" and "documented" within the five year contractual time limitation. With respect to years 1991 through 1993, the contractual time limitation for 1993 costs expired on 30 April 1999. As of that date only the Draft Audit Report had been issued. Only the issue of the allocability of the costs was identified in the Draft Audit Report and only $203,255 of the total franchise tax cost was questioned. Appellant no longer disputes the issue of allocability and that issue is not involved in this appeal. As of the critical date of 30 April 1999, no issue had been raised concerning the allowability of all franchise tax costs under the FEHBAR and no costs had been questioned on that basis. Accordingly, the present government claim is not preserved by the first sentence of the modified clause.

The second sentence of the revised clause also does not permit assertion of the present government claim.[3] That sentence encompasses only the "audit issues" identified by a current waiver. The sole relevant audit issue identified (in the Draft Audit Report) that was the subject of the waivers in this case pertained to the method of allocating the franchise costs. No other issues pertaining to allowability of taxes were raised. As emphasized above there are critical, fundamental differences between allocability and allowability. Accordingly, the government claim for 1991 through 1993 is also not

[3] Because neither the first nor the second sentence of the revised clause permits assertion of the present government claim based on unallowability of the entire franchise tax cost under the FEHBAR for years 1991 through 1993, we need not address whether the second sentence controls the parties' rights to the exclusion of the first given that waivers existed with respect to those years.

preserved under the second sentence of ¶ (a) of the clause as revised commencing with contract year 2000.

We conclude that the present government claim is time-barred with respect to contract years 1991 through 1993. Because the claim is time-barred for 1991 through 1993, the pursuit of associated LII is also time-barred per the parties' settlement agreement (finding 23).

2. Contract Years 1994 and 1995

Nevertheless, the government claim was timely with respect to 1994 and 1995. The first sentence of the modified AUDIT DISPUTES clause authorizes the claim. For contract year 1994 costs, ¶ (c) of the clause would ordinarily require assertion of any government disallowance claim (CO final decision) no later than 30 April 2000. However, the FEHBAR unallowability issue was raised in the Final Audit Report in June 1999 making the first sentence of ¶ (a) of the revised clause dispositive. Because all franchise costs were "questioned" and because the unallowability issue was "documented" and "initially raised" prior to 30 April 2000 the government claim as to 1994 and 1995 remains "open until resolved." The clause was primarily a substitute for the tedious waiver process that previously had preserved audit issues.

B. Retroactive Disallowances

Appellant's contention that the government claim represents a "retroactive disallowance" is without merit. The contract itself expressly authorizes delayed assertion of the claim covering issues that "were" raised in previous audits. Nothing precludes the parties from bilaterally addressing open audit issues by contract clause.

None of the cases cited by BCBS, primarily involving changes to well established accounting practices that had previously been accepted by the government, are apposite. *E.g., Litton Systems, Inc. v. United States,* 449 F.2d 392 (Ct. Cl. 1971). A critical prerequisite to application of the retroactive disallowance doctrine is an "established practice of Government approval" upon which the contractor could reasonably rely. *FMC Corp. v. United States,* 853 F.2d 882, 886-87 (Fed. Cir. 1988). The Government must have "consistently accepted and allowed" the cost in question and failed to provide the contractor with proper notice that the cost will be disallowed in the future. *Lockheed Martin Western Development Laboratories,* ASBCA No. 51452, 02-1 BCA ¶ 31,803 at 157,103-04.

Prior to issuance of the Final Audit Report, OPM had not taken definitive action on the Ohio Franchise Tax that reasonably could be relied upon. The franchise tax had not been "consistently accepted and allowed." Any implication concerning allowability

of the tax arising from the questioning solely of its allocability in the Informal Audit Inquiry and the Draft Audit Report cannot be construed as an "established practice" of OPM approval. Both the Informal Audit Inquiry and the Draft Audit Report were inconclusive in both substance and form and cannot provide a basis for the requisite reasonable reliance by appellant.[4]

C. Factual Issues-1994 and 1995

Although we have concluded that the government claim was timely with regard to contract years 1994 and 1995, the appeal may not be resolved by summary judgment because of the presence of genuine issues of material fact on the merits.

The primary issue controlling resolution of the merits of this appeal is whether the franchise tax costs are allowable under the pertinent FEHBAR provisions. Accordingly, we must determine whether the tax is: (i) "directly or indirectly" imposed "on premiums" and, (ii) classifiable as a "tax on net income or profit" that is "applicable to a broad range of business activity" (FEHBAR 1652.216-71(b)(2)(ii), (iv)(B)). We are unable to resolve these issues without further development of the record.

Although the Ohio Franchise Tax is imposed on capital/surplus, the parties dispute whether the tax is "indirectly" assessed on premiums. In this regard, they apparently agree that Anthem's capital/surplus may be equated with "net worth" but disagree concerning the contribution, if any, made by FEHB premium payments to "net worth" (*see* OPM mot. at 13, 15-17). Among other things,[5] the causal relationship between the taxes assessed and FEHB premiums received is disputed. Appellant argues that there are important differences among financial, government contract and tax accounting treatments, in particular unallowable costs rules applicable to government contract accounting. As a consequence of these differences appellant maintains that FEHBP premium payments actually received by Anthem (as opposed to deposited in an FEHBP trust fund or retained by BCBS) made little, if any, contribution to Anthem's capital/surplus. (App. cross mot. at 19-21) Similarly, appellant alternatively asserts that to the extent, if any, that FEHBP premiums did contribute to Anthem's capital/surplus, it is because the premiums contributed to net income (and, thus, "net worth") over

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[4] A substantial basis for appellant's claimed detrimental reliance is that it was allegedly unable to seek a timely refund of the taxes paid. It is uncertain and we need not determine whether the period for seeking a refund under applicable Ohio statutes had expired with respect, in particular, to years 1994 and 1995 at the time of issuance of the Final Audit Report in June 1999.

[5] The Board does not attempt to detail every possible genuine issue of material fact in deciding these motions.

accounting periods, bringing the franchise tax (in substance) within the "net income or profit" exception. Facts bearing on appellant's "net worth" (capital/surplus) accounting computations may be relevant to the latter issue as well. In short, we are unable, *inter alia*, to resolve the factual issues of whether the taxes are "indirectly" imposed "on premiums" and whether the taxes are more properly classified as falling within the "net income" exception in appellant's particular circumstances. To some degree, these factual issues may involve closely-related or inter-mixed "legal" issues. We decline to decide any such closely-associated, intertwined "legal" issues pending full development and consideration of a complete factual record.

CONCLUSION

Appellant's cross motion for summary judgment is granted with respect to years 1991 through 1993. The motions are otherwise denied. The appeal is sustained to the extent indicated.

Dated: 28 October 2003

ROBERT T. PEACOCK
Administrative Judge
Armed Services Board
of Contract Appeals

I concur

MARK N. STEMPLER
Administrative Judge
Acting Chairman
Armed Services Board
of Contract Appeals

I concur

EUNICE W. THOMAS
Administrative Judge
Vice Chairman
Armed Services Board
of Contract Appeals

I certify that the foregoing is a true copy of the Opinion and Decision of the Armed Services Board of Contract Appeals in ASBCA No. 53632, Appeal of Blue Cross and Blue Shield Association, rendered in conformance with the Board's Charter.

Dated: OCT 2 9 2003

EDWARD S. ADAMKEWICZ
Recorder, Armed Services
Board of Contract Appeals