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¶ 338

FEATURE COMMENT: Government's Defective Pricing Claim In The Great Engine War Flames Out At The Federal Circuit

Wynne v. United Technologies Corp., No. 05-1393, 2006 WL 2466286 (Fed. Cir. Aug. 28, 2006), affirming United Technologies Corp., ASBCA Nos. 51410, 53089, 53349, 04-1 BCA ¶ 32,556, modified on recon., 05-1 BCA ¶ 32,860

In the largest defective pricing action ever litigated under the Truth in Negotiations Act, the Government launched its $299 million offensive with 32 audit reports spanning more than a decade, three final decisions escalating the claimed damages each time and three years of pretrial skirmishing, followed by a 33-day trial introducing over 40 witnesses. In combination with this extraordinary deployment of resources, the Government unsheathed an arsenal of novel, often unprecedented, legal arguments seeking to bend TINA into a contractor's warranty certifying the perfection of its proposal and estimates, without regard for whether Government personnel relied on the allegedly defective data. Thrice the Government lost, once before the Armed Services Board of Contract Appeals, again on ASBCA reconsideration and finally at the U.S. Court of Appeals for the Federal Circuit. More than 22 years after United Technologies Corp.'s Pratt & Whitney (Pratt) submitted its TINA certificate to the Air Force, the Federal Circuit's decision in *Wynne v. United Technologies Corp.* hopefully closes the last chapter on the Government's defective pricing claim in the Great Engine War.

This FEATURE COMMENT describes (1) the historic procurement—the Fighter Engine Competition—birthing this defective pricing action, (2) the ASBCA's initial and reconsideration decisions sustaining the contractor's appeal, and (3) the Federal Circuit's decision reaffirming reliance as an essential element of proof in defective pricing actions and rebuffing the Government's efforts to transform TINA into an ex post facto repricing exercise.

The Great Engine War—In the 1980s, the Air Force pitted Pratt against General Electric (GE) in a $10 billion competition for F15 and F16 fighter jet engines required during 1985–90. See Bodenheimer, Feature Comment, "Competition Trumps Defective Pricing Claim in the Great Engine War," 47 GC ¶ 86 (2005). Although officially called the Fighter Engine Competition, this procurement earned the moniker "The Great Engine War" because of the competitive and political firestorm ignited on Capitol Hill, in the Pentagon and within industry. Id.; see Robert W. Drewes, The Air Force and the Great Engine War (1987).

After Air Force Secretary Verne Orr's award decision in February 1984, the Air Force touted the Great Engine War as a huge success, reaping $2 billion in competitive savings, "classical benefits of competition" and "competitive leverage to drive the prices down as we have." Defense Department Authorization and Oversight Hearings on H.R. 5167 Before the House Armed Services Comm., Part 2, 98th Cong., 2nd Sess. 224-225, 255 (1984) (statement of Air Force Assistant Secretary Cooper). Not only did Secretary Orr tell Congress that it was "a great competition, probably the finest that I've experienced in the 3 years in the Air Force" (id., Part 1 at 760), but Defense Secretary Caspar Weinberger testified that he used it as "ammunition" for competitive recommendations for other contracts.

In 1984–85, the Air Force resisted the initial efforts by the Defense Contract Audit Agency to conduct postaward audits, telling DCAA that the contracts to Pratt and GE "were awarded solely on a competitive basis consistent with the decision made by the Source Selection Authority" and "a defective pricing audit was inappropriate." 04-1 BCA ¶ 32,556

at 161,013, 161,017. By 1989 when the Fighter Engine Competition had fully yielded its multi-billion dollar competitive savings, the Air Force switched positions, supporting 32 DCAA audit reports between 1989 and 2001, issuing three final decisions from 1998 to 2001, and steadily upping the ante from $95 million in 1998 until finally peaking at $299 million.

The ASBCA Decisions—In its initial decision, the ASBCA sustained the contractor's appeal, finding some Air Force claims to be without merit and recognizing offsets exceeding the remaining claims. 04-1 BCA ¶ 32,556 at 161,029. In doing so, the ASBCA reaffirmed fundamental TINA principles on disclosure, judgments, availability of data, certification and offsets.

- Disclosure: "TINA is a disclosure statute" that "does not obligate a contractor to use any particular cost or pricing data to put together its proposal." Id. at 161,024.
- Judgments: An "escalation factor was in essence a judgment as to the future movement of material costs" and thus "not cost or pricing data." Id. at 161,019.
- Availability of Data: A contractor is not liable for errors in cost data created after the certification date. Id. at 161,018.
- Proposals Not Certified: Proposals are not certified, as "[w]e are aware of no statute, regulation, or contract provision that obliges a contractor to certify its BAFO proposal." Id. at 161,025.
- Conceded Offsets: The ASBCA refused to "strike or ignore" offsets "memorialized in DCAA audit reports and CO decisions." Id. at 161,027.
- Two-Way Errors: For a two-way error resulting from deletion of the wrong part, the Air Force could not cherry-pick the part of the error to its benefit and ignore the "countervailing effects" of the rest of the error. Id. at 161,028.

When the Air Force moved for reconsideration, the contractor filed a cross-motion, stating that the lack of reliance and causation undercut all Air Force defective pricing claims. In its 2005 reconsideration, the ASBCA agreed, holding that the Air Force failed to prove either reliance or causation for any of its TINA claims. 05-1 BCA ¶ 32,860 at 162,824. The ASBCA divided its findings into two parts, addressing (a) the initial 1983 competition covering engines for delivery in 1985, and (b) the subsequent rounds of competition (the "outyear awards") covering engines for 1986–90.

For the initial competition (1985), the ASBCA found no reliance or causation because (1) the contractor provided evidence that neither DCAA nor the Air Force "reviewed the BAFO cost or pricing data prior to award"; (2) although Air Force rules required documentation of any "cost/price information relied upon" by the Government, the Air Force did not identify any cost data on which it relied; and (3) Air Force testimony regarding reliance "was lacking in specificity and was unpersuasive." Id. at 162,823. Accordingly, the ASBCA was "hard pressed to understand how the AF could have relied on BAFO cost or pricing data—defective or otherwise—that no one reviewed." Id. Given that the Air Force source selection record validated the reasonableness of BAFO prices based upon the Air Force independent estimate and the "impact of competition" (04-1 BCA ¶ 32,556 at 161,012), the Air Force had good reason to disregard the BAFO cost data.

For the subsequent rounds of competition (1986–90), the Air Force sought and received new offers, performed fresh evaluations and made separate award decisions—all without reviewing the 1983 BAFO cost data or obtaining new cost or pricing data for the revised offers. 04-1 BCA ¶ 32,556 at 161,013-16; 05-1 BCA ¶ 32,860 at 162,824. During the postaward audit, an Air Force CO aptly summed up this process in a letter to DCAA:

> [T]his contract is very unique in that it is basically a perpetual competition using a split award technique decided by the [Air Force Secretary] annually. In this process, *the Contractor's originally submitted certified Cost or Pricing Data has been subjected to an annual Call for Improvements letter requesting improvements in prices as well as terms and conditions.* Over the years, dramatic improvements have been experienced in almost all areas.

05-1 BCA ¶ 32,860 at 162,824 (emphasis in decision). Considering this record, the ASBCA found that the Air Force relied on "competitive forces" and "market test[s] between the competitors," rather than the allegedly defective cost data, in making these subsequent awards. Id. Accordingly, the ASBCA held that the Air Force failed to prove either reliance or causation for these outyear awards for 1986–90.

The Government's Federal Circuit Appeal—On appeal, the Government did not challenge the ASBCA's factual findings, presumably because

they rested on the Air Force's own contemporaneous records and trial admissions. *Wynne v. United Technologies Corp.,* No. 05-1393, 2006 WL 2466286 at 4 (Fed. Cir. Aug. 28, 2006). Instead, the Government opened a bold frontal assault on TINA and its long-standing interpretations by arguing that reliance is not an element of TINA, disclosure does not discharge a contractor's TINA obligations, and judgmental estimates must be certified. The Federal Circuit bought none of these radical notions, instead affirming the ASBCA's decision that the Air Force's defective pricing claim collapsed because of a lack of reliance on the allegedly defective cost or pricing data.

Reliance as an Element of TINA: On appeal, the Government audaciously asserted that defective pricing liability exists regardless of whether anyone relies on the cost or pricing data at issue. For example, one heading in the Government's brief proclaimed that "Reliance Is Not An Element of a TINA Cause of Action." Appellant's Reply Brief at 21. As purported support, the Government employed creative interpretations of Court of Claims decisions from the 1970s. In addition, the Government cited TINA's legislative history, yet even the General Accounting Office (a chief proponent of TINA in 1962) stated that the Act "should apply to all negotiated procurements in which *the Government has relied upon cost and pricing data furnished by the contractor* ...." S. Rep. No. 1884 (1962), reprinted in 1962 USCCAN 2476, 2494 (emphasis added).

In its decision, the Federal Circuit systematically dismantled the Government's attempt to rewrite TINA. The Court first turned to the text of the statute, which authorized a price adjustment only if "such price was *increased because*" the contractor furnished defective cost or pricing data. 10 USCA § 2306(f) (1982) (emphasis added). Citing the long-standing interpretation of the Court of Claims in *Singer Co. v. U.S.,* 576 F.2d 905, 914 (Ct. Cl. 1978) ("whether the Government relied on the overstated costs to its detriment"), the Federal Circuit concluded that "a contract price has been increased by defective cost or pricing data when the government relied on the defective data to its detriment in agreeing to the contract price." *Wynne* at 4.

Next, the Federal Circuit turned to its own precedent "[t]hat reliance on defective data is a necessary element of a TINA claim was reinforced by this court's decision in *Universal Restoration, Inc. v. United States,* in which we found that the Government could not recover on its TINA claim, even though the contract price was calculated using defective data. 798 F.2d 1400, 1402, 1406 (Fed. Cir. 1986)." *Wynne* at 4. Just as the agency in *Universal Restoration* unsuccessfully relied solely on the presumption of reliance, the Federal Circuit explained that the Air Force's TINA claim likewise failed because the Air Force offered no proof of reliance after the contractor rebutted the presumption. Id. at 4–5.

Finally, the Federal Circuit turned to the legislative history of the 1986 TINA amendments. In 1986, the Air Force lobbied Congress to eliminate reliance as a required element of proof. Complaining that lack of proven reliance had shot down a number of TINA claims, the Air Force backed H.R. 4548 to amend TINA to make the presumption of reliance "conclusive." Acquisition Reform—1986: Hearings Before the House Acquisition and Procurement Policy Panel of the Armed Services Comm., 99th Cong. 517-36 (1986) (statement of Mr. Kinlin, Air Force Senior Trial Attorney). The legislative history of the 1986 TINA amendments expressly confirmed well-settled law that reliance long had been an element of proof in defective pricing cases:

> Existing law has been interpreted to require that, in order to recover under TINA, the contractors' failure to disclose must have resulted in the government's being misled into agreeing to a price greater than it would have agreed to had the correct information been provided. Accordingly, if a contractor proves that the government did not rely on the cost and pricing data submitted by the contractor or that, even if it had known the correct information, the government would not have been able to negotiate a better price, the government could not recover.

H.R. Rep. No. 99-718 at 260 (1986).

In its decision, the Federal Circuit not only quoted this legislative history, but added that 1986 TINA amendments reaffirmed this existing law: "Congress rejected the proposed amendment; rather than altering TINA to create a conclusive presumption of reliance, Congress codified the reliance requirement as a defense to a TINA claim." *Wynne* at 5, citing P.L. 99-661, § 952, 100 Stat. 3816, 3945–49 (codified at 10 USCA § 2306a(d)(2) (1986)).

The Federal Circuit ended its thorough analysis without discussing the Department of Defense's own regulations implementing TINA. In particular, the Defense Acquisition Regulation (DAR) in effect

during the Fighter Engine Competition foreclosed defective pricing liability if the data "were not relied upon." DAR § 3-807.10(a)(2); see *Sylvania Elec. Prods., Inc. v. U.S.,* 479 F.2d 1342, 1349 (Ct. Cl. 1972) (citing this part of the regulation regarding reliance). In addition, DAR § 3-807.6(g) made it clear that such reliance required "examination and analysis of the contractor's proposal." These regulations established yet another reason why both the Federal Circuit and the ASBCA correctly held that the Air Force's defective pricing claim failed because no one relied upon the cost data at issue.

Disclosure versus Use of Cost Data: At both the ASBCA and the Federal Circuit, the Government contended that a contractor cannot discharge its duty under TINA simply by disclosing data, but instead must actually *use* such data in its proposal. For example, its appellate brief stated that "[a] bidder who certifies summaries of its current, accurate and complete cost or pricing data is *required to use* its current, accurate and complete cost or pricing data to compile those summaries." Appellant's Brief at 21 (emphasis in original). As the Federal Circuit framed the issue, the Government argued that "it is sufficient to establish that the contract price offered by [the contractor] was calculated using the defective cost or pricing data." *Wynne* at 4.

With this argument, the Government sought to rewrite TINA, transforming it from a disclosure statute into a "use" law. Nowhere does the term "use" appear in TINA; it requires only that cost or pricing data "be submitted." 10 USCA § 2306(f) (1982). Likewise, the DAR did not provide that cost or pricing data "shall be used," but specified instead that it be "submitted or identified in writing." DAR § 3-807.3(c). The case law confirms that contractors only need disclose, not use, the cost data. See, e.g., *U.S. ex rel. Williams v. Martin-Baker Aircraft Co.,* 389 F.3d 1251, 1257 (D.C. Cir. 2004) (no case or regulation "requiring use of such data during negotiations"); *Hughes Aircraft Co.,* ASBCA No. 30144, 90-2 BCA ¶ 22,847 at 114,761 ("contractor does not have to either itself use the cost information or analyze it for the Government"). Finally, even DCAA's own Contract Audit Manual (DCAM) recognized that TINA "does not require a contractor to use such data in preparing its proposals ...." DCAM § 14-104.7 (January 2001).

The Federal Circuit readily disposed of the Government's argument, explaining that it cannot be squared with *Universal Restoration*:

> Rather, the Air Force argues that the presumption cannot be rebutted in an instance in which the allegedly defective data was used in calculating the contract price. That argument is foreclosed by *Universal Restoration*, where we found the presumption of causation rebutted even though the defective data was used in calculating the contract price. 798 F.2d at 1402, 1406.

Wynne at 5–6. Accordingly, the Federal Circuit had no use for the Government's "use" argument under TINA.

Certification of Judgmental Estimates: In yet another twist on TINA, the Government argued that contractors must certify judgmental estimates: "Estimates are Routinely Certified" and "contractor estimates were the principal focus of TINA." Appellant's Reply Brief at 2, 9. Again, the Government took liberties with TINA. The statute requires only certification of "cost or pricing data," not "estimates." 10 USCA § 2306(f) (1982). Consistent with TINA, DOD's implementing regulation expressly stated that the TINA certificate "does not make representations as to the accuracy of the contractor's judgment on the estimated portion of future costs or projections." DAR § 3.807.6(b). Even the DCAA's audit rules acknowledge that "[e]rrors in estimates generally would not result in defective pricing." DCAM § 14-104.7 (Jan. 2001). By definition, an estimate is "an opinion or a judgment" (Webster's New World Dictionary 479) and, therefore, not suitable for certification. See Bodenheimer, " 'False' or 'Inaccurate' Estimates," Briefing Papers No. 05-13 (December 2005) (addressing why estimates are not subject to TINA certification).

Given its already ample basis to affirm the ASBCA's decision on reliance and causation, the Federal Circuit did not expressly confront this additional Government attempt to reconfigure TINA and vastly expand potential defective pricing liability for contractors. Accordingly, the ASBCA has the last word on this issue—at least until the next defective pricing battle. 04-1 BCA ¶ 32,556 at 161,019.

Conclusion—By "exploiting the competitive environment" to extract multi-billion dollar savings, the Air Force's Fighter Engine Competition achieved what Secretary Orr called the "finest competition" of his tenure. In this context, the Air Force's subsequent action to launch the biggest defective pricing litigation in TINA history is, at best, puzzling, especially when the contemporaneous source selection record

and the Government trial admissions demonstrated beyond dispute on appeal that no one relied on—or even looked at—the cost data at issue. Even more inexplicable is the Government's pursuit of an appeal in which the central argument—reliance is not an element of TINA—is crosswise with the Air Force's position 20 years ago before Congress. Nonetheless, the two ASBCA decisions and the recent Federal Circuit decision now offer a comprehensive disposition of virtually every element of a defective pricing case, from disclosure, definition and availability of cost or pricing data to offsets, reliance and causation. Now that more than two decades have passed since the beginning of the Great Engine War, perhaps the Federal Circuit's decision will bring peace to this historic competition.

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