

By
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For more than three decades, the Truth in Negotiations Act (TINA) has bedeviled contractors, but hardly ever in the context of competitive procurements. Recently, however, the battles over defective pricing have spilled from the well-trodden fields of sole-source contracts into the relatively virgin territory of competitive actions. Two recent cases, discussed below, reflect the government's willingness to test the boundaries of TINA and the exemption for adequate price competition.

Whether these recent forays into competitive—yet defective—pricing represent a trend or just a coincidence of anomalous claims, they present some perplexing questions about how far TINA can, or even should, be stretched, including:

- Did Congress intend for TINA to cover competitive procurements?
- When does a competitive procurement not constitute adequate price competition?
- Why would an agency rely upon cost or pricing data – rather than price competition – in a competitive procurement?
- How would the price adjustment for defective pricing be determined in a competitive procurement?

The Great Engine War – Round II

In the 1980s, the Air Force decided that it wanted competition for the fighter engines for the F-15 and F-16 aircraft and proceeded with a formal source selection

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headed by Secretary Verne Orr as the selection authority. The competition became so heated that it was known on Capitol Hill, in the Pentagon, and throughout industry as “The Great Engine War.”¹ The competition proved to be so successful that the Air Force trumpeted competitive savings of more than \$2 billion from the Fighter Engine Competition and Secretary Orr proclaimed it “a great competition, probably the finest that I’ve experienced in the 3 years in the Air Force.”²

Years after these public statements touting the competitive success of the procurement, the Air Force claimed \$95 million in defective pricing against one of the competitors, Pratt & Whitney. When Pratt

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responded with an appeal that raised the issue of adequate price competition, the Air Force sought dismissal of that part of the appeal, arguing the government had “absolute discretion to require certified cost or pricing data and to include a price adjustment clause in the contract where the price was negotiated based upon adequate price competition.”³

The Armed Services Board of Contract Appeals (ASBCA) rejected this notion of unfettered discretion, writing that it found “no suggestion that this discretion is to be exercised without regard to the relevant circumstances, or that this discretion is otherwise absolute or unreviewable.”⁴ Instead, the ASBCA concluded that if a contracting officer demanded

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Dec. 14 Accounting, Cost & Pricing Committee Meeting. American Bar Association, Public Contract Law Section. Members only. Washington, DC. Registration/Information: (202) 626-5993.

Jan. 22-26 National Defense Industrial Association, Procurement Committee Annual Education Seminar. Tradewinds Hotel, St. Petersburg Beach, FL. Registration/Information: (703) 522-1820.

Jan. 11 Accounting, Cost & Pricing Committee Meeting. American Bar Association, Public Contract Law Section. Members only. Washington, DC. Registration/Information: (202) 626-5993.

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Critical Thinking

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certified cost or pricing data contrary to the requirements governing adequate price competition, "this action may constitute an abuse of the government discretion under the statute and regulations."⁵ The ASBCA denied the Air Force motion to dismiss and allowed the case to proceed on all of the issues, including adequate price competition.

The Great Hummer War Revisited

When the Army decided to replace the venerable Jeep in the 1980s, it issued a request for proposals for the High Mobility Multipurpose Wheeled Vehicles (HMMWV), sometimes known as "Humvees" or "Hummers." The Army limited the competition to three offerors – AM General Corporation, General Dynamics Land Systems, Inc., and Teledyne Continental Motors – that had participated in the prototype development phase of the program.⁶ The procurement proceeded with the usual hallmarks of a competitive source selection, including three able competitors, competitive discussions, and Best and Final Offers from the offerors.⁷ As reflected in its proposal, AM General developed its pricing strategy and took price risks consistent with the competitive nature of the procurement:

The costing for this proposal was developed on the basis of a competitive procurement.

Certain changes therefore were required from our normal costing and pricing procedure which resulted in deviations from AM General's Disclosure Statement dated October 26, 1981.⁸

Long after AM General won the competition, the Army initiated a defective pricing claim for \$7,998,073 against the company. Although the first issue to be litigated in this appeal involved the contractor's offsets,⁹ the issue of adequate price competition cannot be far behind.

TINA's History and Competitive Contracts

At the time that it enacted TINA, Congress did not like the fact that many defense contracts had been awarded without obtaining certified cost or pricing data, noting that:

While the Armed Services Procurement Regulation now contains requirements for certification of cost and pricing data, the General Accounting Office informed the committee that its examination of major military procurement activities in the past disclosed many noncompetitive procurements were being accomplished without

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obtaining certifications from Defense contractors and subcontractors.¹⁰

In fact, General Accounting Office testimony during the legislative hearings focused solely on noncompetitive contracts and subcontracts.¹¹ Thus, the legislative history does not suggest any need to extend the scope of TINA to competitive procurements.

TINA's central purpose is to equalize the bargaining power between the parties where the government does not have the leverage of competition:

The classic situation concerning the advocates of the act was where the Government and a large firm negotiated target costs on a one-to-one basis, with the firm knowing its true costs and the government having no such knowledge. [citation omitted] In such cases, where the pressures of competition were not present to ensure fair and reasonable prices, the Government needed protection.¹²

Where competition is driving the prices, certified cost or pricing data is not only unnecessary, it gives the government unfair bargaining power. The contracting agency can reduce the price once through competition and again through a defective pricing claim that further reduces a price already squeezed by competition.

TINA's Exemption for Adequate Price Competition

TINA has always included an exemption for "adequate price competition," but the statute did not offer any definition of this term.¹³ Instead, the task of defining adequate price competition has fallen to the regulations, with some help from the General Accounting Office.¹⁴ For example, the Defense Acquisition Regulation (DAR) in effect at the time of both the Fighter Engine Competition and Hummer procurement stated:

Price competition exists if offers are solicited and (i) at least two responsible offerors, (ii) who can satisfy the requirements, (iii) independently contend for a contract to be awarded to the responsive and responsible offeror submitting the lowest evaluated price, (iv) by submitting priced offers responsive to the expressed requirements of the solicitation.¹⁴

The definition proved relatively workable except for the reference to "lowest evaluated price." Did this provision mean that adequate price competition could not exist unless the agency resorted to sealed bidding? Such a construction would have resulted in the nonsensical interpretation that every "best value" competitive source selection would be subject to TINA simply because the agency reserved the right to award to other than the offeror with the lowest price. Blessedly, common sense prevailed as the Comptroller General interpreted this provision:

"[T]he language 'lowest *evaluated price*' [emphasis in original] should be defined to include all of the factors in the award evaluation." Generally, then, adequate price competition exists and certified cost or pricing data need not be submitted where more than one offeror is considered to be within the competitive range, and price is a substantial, though not necessarily determining, factor in the prescribed evaluation criteria.¹⁶

The Federal Acquisition Regulation (FAR) expressly recognizes that adequate price competition exists when two offerors compete for an award "where price is a substantial factor in source selection."¹⁷ In addition, adequate price competition arises where a reasonable expectation of price competition exists or a price comparison with competitive prices establishes the reasonableness of the prices.¹⁸

Despite the fact that this exemption has been part of TINA since the beginning, adequate price competition has barely been tested in the context of a defective pricing claim. In a case involving urgent requirements for bomb bodies during the Vietnam war, the Navy abandoned its normal competitive procedures and proceeded to allocate the requirements among several individual suppliers.¹⁹ In responding to the Navy's defective pricing claim, Norris Industries contended that adequate price competition existed even though the contract was not competitive because "the contractor's price is reasonably close to recently-obtained competitive prices."²⁰ In addressing the issue of adequate price competition, the ASBCA applied the following standard:

But in our view the regulatory language cited by appellant in support of its position requires reliance upon several competitive

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procurements of comparable quantities within the same relative time frame as a basis for price comparison if the price for an individual noncompetitive procurement is to be regarded as based on adequate price competition.²¹

The ASBCA declined to find adequate price competition because the prior competitive procurements involved differing quantities and occurred too long before the noncompetitive contract at issue.

What does the *Norris Industries* decision mean for the two pending appeals involving the Fighter Engine Competition and the Hummer procurement? Unlike *Norris Industries*, these two appeals represent actual competitive source selections, rather than non-competitive procurements that are merely being compared to competitive prices from other acquisitions. As a result, the ASBCA will soon take a fresh look at whether an agency can sustain a claim of defective pricing in the face of adequate price competition arising out of a competitive source selection.

Reliance Upon Cost or Pricing Data in a Competitive Procurement

To recover for defective pricing, the agency must rely upon the allegedly defective cost or pricing data.²² While a contracting officer may sensibly rely upon cost or pricing data in sole source negotiations, what sense does reliance on cost or pricing data make when the agency has used the competitive process to extract competitively-driven prices? The FAR establishes an express preference for price analysis, rather than cost or pricing data, as a basis for determining prices to be fair and reasonable.²³ Similarly, the regulation in effect at the time of the Fighter Engine Competition and the Hummer procurement placed a premium upon price analysis over cost and profit analysis:

Government procurement is concerned primarily with the reasonableness of the price which the Government ultimately pays, and only secondarily with the eventual cost and profit to the contractor.²⁴

Thus, if the competitive process generates attractive prices that allow the agency to perform a meaningful price comparison, the regulations indicate that reliance upon the cost or pricing data may not only be unnecessary, but may even be unreasonable.

Given the dearth of defective pricing cases involving competitive contracts, the courts and administrative boards have not had many opportunities to address the issue of reliance on cost or pricing data when competitive prices are available. Nonetheless, the ASBCA has found a lack of reliance in cases where the government found prices to be reasonable based upon comparison to competitive prices.

In one case, the Navy entered into separate negotiations with three different contractors and then awarded contracts to each company, with the largest share of the work going to the firm with the lowest price, Sparton Corporation.²⁵ The Navy's Business Clearance Memorandum stated that the contracting officer performed a "quick review" of the contractor's cost breakdowns and accepted the proposed price "in view of the competition present and the fact that these prices compared favorably with prices previously submitted and/or paid."²⁶ The ASBCA characterized the Navy's analysis as a price analysis, rather than a cost analysis, and concluded that reliance upon the cost data had not been proven.²⁷

In another case, no reliance existed where the contracting officer found the proposed price to be reasonable, based upon a comparison to competitive market prices:

Considering that the contracting officer "testified" that he was able independently to determine that Luzon's offer was competitive from other sources, we are not at all certain that this procurement might not have come within one of the exceptions to the requirement for furnishing cost and price data, even though it was determined for other reasons to effect a sole source procurement here. The complete disinterest in checking any cost other than insurance before contract award, indicates that the procurement was made on the basis of an independent price analysis based on market conditions for the rental.²⁸

As these cases show, a competitive procurement may well present a double hurdle for the government in defective pricing cases, first with adequate price competition and second with reliance upon competitive pricing rather than cost or pricing data.

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Defective Pricing and Competitive Source Selections

Price reductions under TINA rest upon the premise that if the government had only known of the defective cost data, a lower price would have been negotiated. In short, the government would have named a lower price and stuck to it.

In a competitive source selection, the process differs considerably from sole-source negotiations. For example, the regulations governing the Fighter Engine Competition and the Hummer procurement strictly prohibited auctions, barring an agency from “indicating to an offeror a price which must be met to obtain further consideration.”²⁹ Even with the FAR Part 15 rewrite that removed the provisions regarding auctions, an agency would be skipping through a protest minefield if it insisted upon a specific price reduction from one offeror, but not the other. What if the offeror became the winner due to the requested price reduction? The loser would protest, complaining that the agency treated the offerors unequally.

As another example, sole-source negotiations continue until the parties reach agreement upon price, while competitive discussions conclude with the request for Best and Final Offers. If the allegedly defective data surfaces in the Best and Final Offer, the government cannot simply open negotiations with one offeror to secure further price reductions. Instead, the government has to reopen discussions with everyone, at which point all bets are off. Technical proposals may change, prices may vary, and the relative standing of the offerors may shift. How can anyone reconstruct the effect of the defective cost data upon the price when the competitive kaleidoscope begins to turn, altering the prices, technical approaches, and perhaps even the eventual winner? TINA offers no guidance on how to untangle these knots, presumably because no one ever contemplated defective pricing claims in competitive procurements.

Conclusion

More than 35 years have passed since TINA became law. While virtually every other crevice and nook of defective pricing has been explored by the courts and boards, competitive procurements have remained untouched until recently. With the Fighter Engine Competition and the Hummer procurement, the government has commenced battle on new and unfamiliar territory. While it is too soon to predict the outcome, the government appears to have gone too far if the history

of TINA, the requirements of the regulations, and the cases involving competitive pricing are to be given their due weight.

Endnotes:

1. Robert W. Drewes, *The Air Force and the Great Engine War* (1987).
2. *Defense Department Authorization and Oversight: Hearings on H.R. 5167 for Department of Defense Authorization of Appropriations for Fiscal Year 1985 Before the House Armed Services Committee, 98th Cong., 2nd Sess.* 225 (statement of Dr. Cooper) and 760 (statement of Sec. Orr) (1984).
3. *United Technologies Corp., Pratt & Whitney*, ASBCA No. 51410, June 23, 1999, 99-2 BCA ¶ 30,444 at 150,425.
4. *Id.* at 150,427.
5. *Id.*
6. *AM General Corp.*, ASBCA Nos. 48476, 51107, Nov. 10, 1998, 99-1 BCA ¶ 30,130 at 149,043.
7. *Id.* at 149,043-45.
8. *Id.* at 149,044.
9. *Id.* at 149,046.
10. S. Rep. No. 1884 (1962), reprinted in 1962 U.S.C.C.A.N. 2476, 2478.
11. *Id.* at 2476, 2495.
12. *Serv-Air, Inc. – Reconsideration*, B-189884, 79-1 CPD ¶ 212 at 7.
13. TINA is currently codified at 10 U.S.C. § 2306a and 41 U.S.C. § 254b. The version in effect at the time of the Fighter Engine Competition appeared at 10 U.S.C. § 2306(f) (1982).
14. Compare Federal Acquisition Regulation (FAR) § 15.403-1(c) (1999) with Defense Acquisition Regulation (DAR) § 3-807.7 (1983).
15. DAR § 3-807.7(a)(1) (1982).
16. *Serv-Air, Inc.*, B-189884, 78-2 CPD ¶ 223 at 13.
17. FAR § 15.403-1(c)(1)(i)(A).
18. FAR § 15.403-1(c)(1)(ii) and (iii).
19. *Norris Indus., Inc.*, ASBCA No. 15442, Feb. 7, 1974, 74-1 BCA ¶ 10,482 at 49,569.
20. *Id.*
21. *Id.*
22. *Universal Restoration, Inc. v. United States*, 798 F.2d 1400, 1405-06 (Fed. Cir. 1986); *Aerojet Ordnance Tennessee*, ASBCA No. 36089, Sept. 7, 1995, 95-2 BCA ¶ 27,922 at 139,445.
23. FAR § 15.402(a).
24. DAR § 3-806(b).
25. *Sparton Corp.*, ASBCA No. 11363, Aug. 25, 1967, 67-2 BCA ¶ 6539 at 30,375-76.
26. *Id.* at 30,376.
27. *Id.* at 30,382.
28. *Luzon Stevedoring Corp.*, ASBCA No. 14851, Feb. 24, 1971, 71-1 BCA ¶ 8745 at 40,607.
29. DAR § 3-805.3(c).