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NEWSLETTER

Your Money's No Good Here: Resolving Contract Disputes Using Other Than Cash

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Many government contract law practitioners were in elementary school when the Navy, McDonnell Douglas (now Boeing), and General Dynamics first squared off, in the last millennium, to resolve a dispute over the cancellation of the A-12 stealth aircraft program. However, on January 23, 2014, after a 23-year litigation death-march involving numerous dueling claims, millions of documents, thousands of pages in pleadings, and multiple trials and appeals, the exhausted parties finally gave up, agreeing to settle the multi-billion dollar dispute not with a bang but a whimper, with a value of about $400 million changing hands in favor of the Navy.

The tortured history of this litigation is a cautionary tale, but the parties' final settlement, involving the use of in-kind transfers of products and services, rather than exclusively a cash payment, is one that also offers lessons for litigators seeking to resolve seemingly intractable contract disputes. In the present and future years of severe fiscal austerity, contractors and government officials will need creativity and flexibility to avoid potentially staggering litigation costs, while forging settlements that parties can live with. Settlement features of the kind highlighted in the A-12 case point the way.

While such decades-long disputes are rare, contract appeals often can linger for years, given the slowness of the contract dispute and appeal process. As reflected by the most recent Armed Services Board of Contract Appeals Quarterly Report discussed elsewhere in this *Update*, the Board's backlog of appeals has increased by 42% from December 2008 to December 2013 (542 cases pending to 934 cases pending). The upward trend in appeals appears to be accelerating, with the most recent quarterly increase clocked at 41 cases (4.5%) in the last three months alone. One logical surmise is that neither the Government nor contractors enjoy the same liquidity to pay or compromise on settlements of contract disputes that they enjoyed in days gone by. This can lead to intransigence and delay (with commensurate elevated cost and risk for both sides) for cases in which, in years past, the parties would have more quickly achieved a deal with cash payments. And even when funds were more plentiful, agencies often faced fiscal law challenges when fashioning cash-based settlements.

Over time, agencies may lose flexibility in accepting cash payments that benefit the programs involved in disputes, with payments being diverted in some cases to the U.S. Department of the Treasury (Treasury) under the provisions of the Miscellaneous Receipts Statute, 31 U.S.C. § 3302(b). For example, a quickly resolved dispute can be paid by the contractor through a cash credit on the company's next invoice for the contract associated with the dispute, but this remedy may not be available if the issue takes years to resolve.

These challenges can affect not only litigation under the Contract Disputes Act, but also cases brought under the False Claims Act (FCA) and related statutes. Simply put, the incentive for the Government to settle a case can be significantly affected if the proceeds of the settlement will be swallowed up by Treasury. But government officials dealing with contract disputes nevertheless feel pressure to obtain substantial consideration in exchange for compromising a claim in order to avoid scrutiny and criticism after a deal is achieved. Thus, the Government dispute partner confronts potentially conflicting influences: the Government's need to resolve disputes in order to focus on current and future requirements, the requirement to obtain at least minimally satisfactory consideration, and the desire to retain the fruits of any settlement within the agency. These countervailing influences can lead to paralysis and delay in contract-related litigation.

By doing nothing (or as little as possible) to advance dispute resolution, the Government minimizes the drain on current resources, and postpones the day of reckoning with respect to the merits of the dispute—the time when congressional, senior agency, or inspector general officials may review the matter to decide who erred, and how badly. And there are many ways by which, with relatively little effort and expense, the Government can slow the pace of dispute resolution, even beyond the inherently slow pace of formal litigation. The incentive to do so is only increased if the original dispute was started years before, and/or by persons no longer associated with the government program, a circumstance especially commonplace in the U.S. Department of Defense (DOD) and in connection with overseas contingency operations, which experience a very high rate of personnel turnover. To break this impasse, the use of in-kind or non-cash settlement elements can be effective, by delivering immediate and tangible value to Government programs.

Such an approach gives program and contracting personnel a good reason to become active in settlement efforts. Instead of achieving, through a settlement, some theoretical or academic finding that the Government's position was correct, and little else because any cash goes elsewhere, the Government customer can realize real benefits in the form of additional products, services, warranty extensions, discounts, and other identifiable benefits that help carry out current operations. The U.S. Government Accountability Office (GAO) fiscal law rulings have, moreover, sanctioned such settlements, at least insofar as they have determined that acceptance of such non-cash elements does not run afoul of the Miscellaneous Receipts Statute and the Antideficiency Act's prohibition against the acceptance of voluntary services. *See, Bureau of Alcohol, Tobacco, and Firearms—Augmentation of Appropriations—Replacement of Autos by Negligent Third Parties*, B-226004, 67 Comp. Gen. 510 (July 12, 1988) (agency could legally accept a replacement vehicle from a negligent third party without transferring an amount equal to the value of the replaced vehicle from agency's current appropriations to the Treasury's miscellaneous receipts fund); *General Services Administration: Real Estate Brokers' Commissions*, B-291947 (Aug. 15, 2003), (GSA's acceptance of real estate brokerage services at no cost also did not constitute voluntary services).

This is not to suggest that such settlements are easy to achieve. Agency settlement officials will still be under pressure to demand the best possible deals (especially in FCA cases), and to ensure that the actual value of the goods or services offered matches the stated values in the settlement agreement. This imperative will typically involve advance scrutiny and audit, and careful negotiations to match what is being offered to the needs of the agency. And, while such concerns would appear to be greatly diminished in this context, there may be review and questions related to the potential impact on competition. For example, if a settlement element includes a three-year extension of services, albeit at a severe discount, the agency's Competition Advocate might object. But while there may be substantial hurdles to overcome, the point of this approach is that agency officials will be motivated to make the deal work. And of course, on the other side of the settlement, the parties will have work to do to ensure that goods and services are delivered in accordance with the bargain struck, just as with any other government contract.

Sequestration, government shutdowns, slow incremental funding, continuing resolutions, budget impasses, and draconian cuts—fiscal austerity is here to stay and may get worse, while agency missions expand. These forces will likely make protracted, seemingly insoluble contract-related disputes more common. On the contractor side, avoidance of such disputes is frequently an equal imperative. To mitigate such risks, contractors and their agency dispute partners should in most cases consider whether the use of non-cash settlement elements can provide a path to dispute resolution that is truly fair to both parties, to the American taxpayers, and to the customers of the programs that will be the recipients of the goods and services delivered as the benefit of the bargain.