Mr. Jeremy Olson  
General Services Administration  
FAR Secretariat (MVRS)  
Room 4037  
18th and F Streets, N.W.  
Washington, D.C. 20405

Ms. Sandra G. Haberlin  
Defense Acquisition Regulations Council  
Crystal Square No. 4  
Suite 200  
1745 Jefferson Davis Highway  
Arlington, Virginia 22202

Re: FAR Case 95-020, Costs Related to Legal and Other Proceedings, 61 Fed. Reg. 31790 (June 20, 1996)

Dear Mr. Olson and Ms. Haberlin:

On behalf of the Section of Public Contract Law of the American Bar Association ("the Section"), I am submitting comments on the above-referenced matter. The Section consists of attorneys and associated professionals in private practice, industry and Government service. The Section’s governing Council and substantive committees contain members representing these three segments to ensure that all points of view are considered. In this manner, the Section seeks to improve the process of public contracting for needed supplies, services and public works.

The Section is authorized to submit comments on acquisition regulations under special authority granted by the Association’s Board of Governors. The views expressed herein have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and, therefore, should not be construed as representing the policy of the American Bar Association.
In June of 1996, proposed changes to FAR 31.205-47, pertaining to the costs of defense of qui tam actions, were published in the Federal Register. 61 Fed. Reg. 31790 (June 20, 1996). The Section did not submit comments on the proposed rule by the August 19, 1996 deadline, but is submitting comments at this time because it has been brought to the Section’s attention that the FAR Council is currently considering whether to apply the proposed changes to the cost principle retroactively. Because retroactive application of these changes is an important issue, we ask that these comments receive consideration in the Council’s deliberations.

The proposed rule purports to "clarify" the allowability of costs incurred to defend qui tam suits in which the Government does not intervene. It does so by amending FAR 31.205-47 to address for the first time, in paragraph (b), "costs incurred in connection with any proceeding brought by a third party in the name of the United States under the False Claims Act, 31 U.S.C. § 3730." The proposed rule also "clarifies" that the maximum reimbursement contractors can receive for legal costs pursuant to agreements settling qui tam actions is 80 percent of otherwise allocable and allowable costs. This is accomplished by amending paragraph (c) to add a new subparagraph (c)(2) providing as follows:

(2) In the event of a settlement of any proceeding brought by a third party under the False Claims Act in which the United States did not intervene, reasonable costs incurred by the contractor in connection with such a proceeding that are not otherwise unallowable by regulation or by separate agreement with the United States, may be allowed if the contracting officer, in consultation with his or her legal advisor, determines that there was very little likelihood that the third party would have been successful on the merits.

In addition, language has been added to subparagraph (e)(3) stating that allowable qui tam defense costs shall be "determined by the cognizant contracting officer, but shall not exceed 80 percent of otherwise allowable legal costs incurred."

### Clarification vs. Substantive Change

In considering whether an amendment to the text of a FAR cost principle is a change, to be given prospective effect, or a clarification, to be given retroactive effect, a board or court will consider the plain language as well as the history of the provision, and may accept the rulemaking body's description of the purpose of the amendment, if supported by the language and the history of the cost principle. Rockwell Internat'l Corp., 96-1 BCA ¶ 28,057 at 140,093, aff'd sub nom. Rockwell Internat'l Corp. v. Secretary of the Air Force, 109 F.3d 1579, 1584 (Fed. Cir. 1997). In Rockwell, the FAR cost principle at 31.205-41 had initially been amended "to clarify that the [Superfund Tax] is allowable," but a correction was later issued to state that retroactive allowability was not intended and the purpose of the amendment was to revise the cost principle to make the tax allowable. Both the Board and the court concluded that the Superfund Tax was unallowable prior to the revision of the cost principle.

In this case, the plain language of FAR 31.205-47 makes it abundantly clear that, regardless of the subjective intent of the regulators, the pending amendments constitute a substantive change. To find that the amendments were a clarification only, a court would have to find that the legal proceedings cost principle has always meant that the costs of qui tam defense, even where the Government does not intervene, are unallowable. The plain language of the current cost principle does not support such a finding. First and foremost, by its very terms, it only covers costs of a proceeding "brought by" the Government. While policy makers may have legitimate reasons for believing that suits brought by third parties on behalf of the Government should be equated with proceedings brought by the Government, this belief merely supports the decision to revise the cost principle to include such proceedings. It does not change the fact that the cost principle currently does not refer to such proceedings; nor does it amount to a supportable interpretation of the current language of the cost principle.

The history of the proposed rule simply underscores that the proposed rule is a substantive change. Neither
the present FAR 31.205-47 nor its predecessors ever applied to actions brought by private parties. The cost principle did not apply to actions by relators when the fraud provisions were first implemented in 1982 in the Defense Acquisition Regulation, and it has never been amended to include such actions. The original fraud provisions stated that, in cases where fraud allegations were settled, "the parties" could negotiate the allowability of the contractor's legal costs. Defense Acquisition Circular #76-39 (October 20, 1982). Since private parties cannot negotiate government contract cost allowability, relators (without Government intervention) were not one of the "parties" contemplated by the cost principle.

In 1994, the Defense Contract Audit Agency (DCAA) issued Audit Guidance on Allowability of Legal Costs Associated with Qui Tam Suits, 94-PAD-100(R) (June 20, 1994). This guidance concluded that costs of defense of qui tam suits are allowable so long as the Government does not intervene. The guidance specifically addressed the question whether a qui tam suit can be considered to be "brought by the Federal Government, under the theory that the qui tam relator 'stands in the shoes' of the Government. . . ." It answered this question in the negative based on the "prevailing view among the circuit courts" that the qui tam provisions constitute a limited assignment of the Government's claim to the relator, and therefore the relator files the suit in his or her own right, even though for the benefit of the Government. The Guidance concluded by stating that FAR 31.205-33, Professional and Consultant Services Costs, not FAR 31.205-47, was the cost principle applicable to evaluating the costs of defending against qui tam lawsuits. This guidance was consistent with the plain meaning and regulatory history of the cost principle, as well as with published court decisions establishing that qui tam actions brought by relators are considered to be brought by private plaintiffs. See, e.g., U.S. ex rel. Kelly v. Boeing Co., 9 F.3d 743, 748-50 (9th Cir. 1993).

As a result of well-publicized objections by the Department of Justice to this audit guidance, revised guidance was issued a little over a year later. See 95-PAD-121(R) (August 24, 1995). This one-page guidance did not refute the reasoning of the prior guidance. It concluded, without any explanation of the reversal in position, that "costs of defending against any qui tam suit are evaluated by the provisions of FAR 31.205-47 as if the Government brought the suit directly." (Emphasis added.) Note that this change was effected not by a clarification, but by means of "new" and "revised" guidance. Furthermore, even though the revised guidance was clearly a result of DOJ's displeasure with the previous guidance, DCAA could not go so far as to state that qui tam suits actually were suits brought by the Government - only that they should be treated the same way. Later audit guidance in the DCAA Contract Audit Manual states that "[a] legal determination has been made that a 'qui tam' proceeding is a 'proceeding brought by the Federal government as that term is used in FAR 31.205-47(b)." Contract Audit Manual, 7-1918.2d. (January 1997). However, the reasoning underlying the cited legal determination has not been revealed.

It would be extremely difficult for the Government to convince a board or court, in light of this history, that the proposed amendments to FAR 31.205-47 do not constitute a substantive change.

Substantive Changes to Cost Principles
Are Implemented Prospectively

The cost principles incorporated into a contract are those that were in effect when the contract was entered into. See FAR 52.216-7, providing that the Government shall make payments in accordance with Subpart 31.2 of the FAR in effect on the date of the contract. A substantive revision to a cost principle therefore is normally not applied to contracts already in existence at the time the change is made. There is a powerful presumption against retroactive changes in substantive rights, which has been specifically applied in the context of cost principle changes. See, e.g., Cotton & Co., 90-2 BCA 22,828 at 114,625 (costs for alcoholic beverages were allowable despite changes in regulation, after award of the contract, disallowing such costs). Moreover, where the Government considers and allows a cost, and the contractor detrimentally relies on the approval, the Government may not withdraw its approval or disallow the cost retroactively. See, e.g., Bell-Boeing Joint Venture, ASBCA No. 39681, 93-2 BCA 25,791 (Government moved for summary judgment on the theory it could not be estopped by a prior Contracting Officer's determination of CAS compliance because that determination was erroneous. The Board said that even if the prior practice did not comply with CAS, Bell-Boeing could still prevail if it could demonstrate that it reasonably relied to its detriment on the prior determination). See also Gould Defense Systems, Inc., ASBCA No. 24881, 83-2 BCA 16,676, aff'd on reconsideration 84-3 BCA 17,666 (Government estopped from
challenging inclusion of good will in facilities capital cost of money because it did not object to this practice during a forward pricing audit, and the contractor relied on the methodology in pricing contracts) and Litton Systems, Inc. v. U.S., 449 F.2d 392, 401-402 (Ct. Cl. 1971) (contractor could continue to use disapproved accounting method for all contracts entered into before method was authoritatively disapproved by the Government).

The Section submits that there is abundant evidence, including the plain language of the cost principle, its regulatory history, DCAA's original audit guidance, and the Government’s failure to disallow such costs consistently in the field, that the Government has allowed the costs of qui tam defense under the very same cost principle language that it now proposes to "clarify." Where contractors have relied to their detriment on the Government’s approval of these costs, the costs will continue to be allowable on all contracts entered into prior to "authoritative" disapproval - an event that may not be held to occur until the cost principle is revised.

**Conclusion**

The Section is concerned that any attempt to give the proposed changes to FAR 31.205-47 retroactive effect is not well based in law or in fact, and would undoubtedly result in substantial, widespread litigation raising retroactive disallowance issues. While we understand that some may hold the view that the cost principle should apply equally to qui tam actions as well as to actions brought by the Government, this view by no means establishes that the cost principle, in its current form, actually does apply to qui tam actions. We urge the FAR Council to recognize that serious issues are implicated by giving the changes retroactive effect, and that implementing the changes on a prospective basis would avoid substantial administrative and litigation costs.

The Section appreciates the opportunity to provide these comments and is available to provide additional information or assistance as you may require.

Sincerely,

Marcia G. Madsen
Chair
Section of Public Contract Law

cc: David A. Churchill
    Rand L. Allen
    Gregory A. Smith
    Patricia A. Meagher
    Marshall J. Doke, Jr.
    John T. Kuelbs
    Michael K. Love
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