No. 09-3

IN THE

Supreme Court of the United States

DAEWOO ENGINEERING & CONSTRUCTION CO., LTD,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

On Petition for a Writ of Certiorari To the United States Court of Appeals For the Federal Circuit

BRIEF OF WASHINGTON LEGAL FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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BRIEF OF WASHINGTON LEGAL FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

INTERESTS OF *AMICUS CURIAE*

The Washington Legal Foundation (WLF) is a non-profit public interest law and policy center with supporters in all 50 States.[1] WLF devotes a substantial portion of its resources to defending free-enterprise, individual rights, and a limited and accountable government.

To that end, WLF has appeared before this and other federal courts in numerous cases raising issues relating to the proper interpretation of government contracting law, with an eye to ensuring that entities that contract with the federal government are afforded legal rights commensurate with those afforded to contracting parties generally. *See, e.g., Rumsfeld v. United Technologies Corp.*, 315 F.3d 1361 (Fed. Cir.), *cert. denied,* 540 U.S. 1012 (2003); *Allegheny Teledyne Inc. v. United States*, 316 F.3d 1366 (Fed. Cir.), *cert. denied, sub nom., General Motors Corp. v. United States*, 540 U.S. 1068 (2003).

WLF is concerned that the Federal Circuit's decision, if allowed to stand, will expose companies that

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[1] Pursuant to Supreme Court Rule 37.6, WLF states that no counsel for a party authored this brief in whole or in part; and that no person or entity, other than WLF and its counsel, made a monetary contribution intended to fund the preparation and submission of this brief. More than ten days prior to the due date, counsel for WLF provided counsel for Respondent with notice of its intent to file this brief. All parties have consented to the filing; letters of consent have been lodged with the clerk.

contract with the government to huge, unwarranted penalties if a reviewing court later determines that claims they submitted were even partially inaccurate. WLF is concerned that the fear of such penalties will discourage companies from contracting with the federal government. WLF is also concerned that such fears will deter contractors from submitting meritorious claims for post-award equitable adjustments – and the results of any such reluctance include increased opportunity for federal agency abuse of the procurement process and windfalls for the government. WLF does not believe that Congress intended to create the specter of such crippling penalties when it adopted the Contract Disputes Act.

REASONS FOR GRANTING THE PETITION

The Washington Legal Foundation (WLF) agrees with petitioner that the Federal Circuit committed clear error when it held that under the anti-fraud provision of the Contract Disputes Act of 1978 (Contract Disputes Act or CDA), 41 U.S.C. § 604, the proper measure of damages to be awarded to the government is the entirety of a projected, or estimated, claim, rather than the demonstrably fraudulent individual elements of such a claim. This error has great significance for government contractors.

If the error remains uncorrected, it will potentially affect all of the more than 190,000 businesses that sell the goods and services that the Federal government needs to accomplish its various missions. *See* http://www.usaspending.gov (193,259 companies and individuals received Federal government

contracts in FY2008). The effect on these and future government contractors will be significant because each of them will have to clear a high hurdle to be fairly and adequately compensated when the government changes a contract, as the government does routinely, or when the government breaches a contract. Indeed, the Federal Circuit's error sets a "fraud trap" for contractors that must use estimates to present their legitimate claims for damages consisting of projected future costs to the government.

If the error that is the subject of the petition remains uncorrected, businesses that may consider continuing to provide goods and services, or that may consider entering the federal government procurement arena for the first time, may well choose not to do either. Accordingly, the error will not only undermine Congress's stated policy in enacting the Contract Disputes Act to "insure fair and equitable treatment to contractors," S. Rep. No 95-1118, at 1 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5235, 5235, but it will also undermine the efficient and effective working of the government. For those reasons, the petition for a writ of certiorari to the Federal Circuit should be granted.

I. REVIEW SHOULD BE GRANTED BECAUSE ONLY THIS COURT CAN CORRECT THE FEDERAL CIRCUIT'S MISINTERPRETATION OF 41 U.S.C. § 604, AND UNDO THE DAMAGE IT HAS CAUSED TO THE PROCUREMENT PROCESS

A. The Federal Circuit Misinterpreted 41 U.S.C. § 604 by Including Non-Fraudulent Elements in the Damages Calculation

The Contract Disputes Act's "anti-fraud" provision, codified at 41 U.S.C. § 604, is straightforward:

> If a contractor is unable to support any part of his claim and it is determined that such inability is attributable to misrepresentation of fact or fraud on the part of the contractor, he shall be liable to the Government for an amount equal to such unsupported part of the claim in addition to all costs to the Government attributable to the cost of reviewing said part of his claim. Liability under this subsection shall be determined within six years of the commission of such misrepresentation of fact or fraud.

The plain text of the statute, as well as its legislative history as noted by petitioner, establishes that a contractor that is unable to support *any part* of a claim brought under the Act, when it is determined that the inability to support *that part* of the claim is attributable to misrepresentation of fact or fraud, will be

liable to the government for an amount equal to *such unsupported part* of the claim. The statute does not allow for the Federal Circuit's interpretation that if a claim is tainted by a factual misrepresentation or fraud in *any* of its constituent elements, the *entire claim* is fraudulent, and therefore the entire amount of the claim will be assessed against the contractor as damages, or, in reality, a penalty.

A violation of the Contract Disputes Act must be proved by a preponderance of the evidence. *UMC Electronics Co. v United States*, 249 F.3d 1337, 1339 (Fed. Cir. 2001); *Commercial Contractors, Inc. v. United States*, 154 F.3d. 1357, 1362 (Fed. Cir. 1998). The trial court found only that certain elements of petitioner's claim were overstated, and perhaps fraudulent. *See* Pet. App. 138a-143a (certain equipment acquisition and maintenance costs, production rates, depreciation of scrapped equipment, costs of daily use of some equipment). The trial court also noted that petitioner made rounding errors, and included expressly unallowable costs (alcohol, donations to the Palau government, entertainment, and interest on a letter of credit) in its claim. *See* Pet. App. 147a.

Thus, the actual instances of fraud that were found by the trial court, and affirmed by the Federal Circuit, were discrete and quantifiable. Such isolated examples did not, however, infect petitioner's full $50.6 million claim for projected costs and damages, much less the total claim of $64 million that petitioner put forward.

The Federal Circuit did not make any calculation

or finding that petitioner's *entire* $50.6 million claim for projected costs was based on misrepresentations of fact or was otherwise fraudulent. Likewise, there is no indication in either the trial court's or the Federal Circuit's opinion that the government proved by a preponderance of the evidence that the substance of petitioner's *entire* claim was false or fraudulent.

Accordingly, on a proper construction of Section 604, there was no evidentiary basis for either the trial court or the Federal Circuit to conclude that, under the statute, petitioner should be penalized in the entire amount of its claim for projected costs. Likewise, there is no legal basis in the statute or its legislative history for the Federal Circuit's conclusion that elements of a claim that have not affirmatively been proven to be fraudulent should be included in a penalty that might otherwise be correctly assessed under 41 U.S.C. § 604.

B. The Federal Circuit Misinterpreted What Constitutes a Fraudulent Claim, in Whole or In Part, Under 41 U.S.C. § 604

The Federal Circuit noted that petitioner "apparently used no outside experts to make its certified claim calculation." Pet. App. 13a-14a. This was apparently part of the circuit court's reasoning why petitioner had committed fraud in submitting its claim.

The absence of expert assistance in claim preparation is not fraud, especially considering that Congress's intent in enacting the Contract Disputes Act was to provide an informal and efficient method for the

resolution of claims arising under and relating to government contracts. S. Rep. No 95-1118, at 1 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5235, 5235 ("The act's provisions help to induce resolution of more contract disputes by negotiation prior to litigation; equalize the bargaining power of the parties when a dispute exists; provide alternate forums suitable to handle the different types of disputes; and insure fair and equitable treatment to contractors and Government agencies.") To require contractors – *all* contractors, including small and disadvantaged businesses – to retain experts to help prepare their claims in order to avoid possible assessment of fraud penalties under 41 U.S.C. § 604, as the government can now argue based on the Federal Circuit's opinion, is an erroneous interpretation of the statute and does not comport with Congress's intent in enacting the Contract Disputes Act.

The Federal Circuit also noted with approval that while the trial court did not find that petitioner's reliance on legal theories such as defective specifications, superior knowledge, and impossibility of performance was fraudulent, the trial court was correct in finding that petitioner's "$50.6 million projected cost calculation was fraudulent." Pet. App. 13a. As the Federal Circuit went on to say:

> [Petitioner's] calculation assumed that the government was responsible for each day of additional performance beyond the original 1080-day contract period, without even considering whether there was any contractor-caused delay or delay for which the government was not responsible.

Id. In other words, according to the Federal Circuit, if a contractor does not take pains to separate out all elements of claimed damages for which it may itself ultimately be shown at some unknowable point in the future to be responsible, or for which the government may ultimately be shown not to be responsible, the contractor's entire claim is fraudulent.

This conclusion represents a sea change in the way the lower courts treat government contract claims. The mere claiming of all costs incurred – the use of the "total cost method" of claiming compensation under a contract – is a well-recognized basis for contractor claims in certain circumstances. The specificity required for a contractor's proof of damages is related to the nature of the government's breach. The more fundamental, intrusive, or continuous the government's breach, the less specific a contractor's proof of damages needs to be. *See, e.g., Ralph L. Jones Co. v. United States*, 33 Fed. Cl. 327, 336 (1995) (applying total cost method to determine damages where government agency ordered changes that it knew would be difficult for contractor to prove with definitive evidence of costs incurred, and where agency was responsible for all associated extra costs); *Concrete Placing Co. v. United States*, 25 Cl. Ct. 369, 377-78, *aff'd*, 985 F.2d 585 (Fed. Cir. 1992) (court allowed contractor to change proof at trial from actual cost to total cost method because of difficulty in distinguishing between work caused by defective specifications and work covered by contractor's bid). In the instant case, when petitioner submitted its claim, it believed that the contract

> [C]ontained a misleading weather-delay clause

> and defective road design specifications, that the government breached its duty to disclose its superior knowledge of its weather-delay calculation methods, and that the contract was thus impossible to perform.

Pet. App. 6a. In these circumstances, it is not inappropriate for a contractor to calculate its damages using the total cost method. Moreover, as noted above, the trial court did not find that these theories were "fraudulent"; it merely found them to be without merit. Pet. App. 13a. How, then, could petitioner's method of calculating delay damages, which did not take into account the possibility that either petitioner itself might have been liable for some of the delay or that the government might *not* have been liable for *all* of the delay – a calculation that amounted to the use of the total cost method – be fraudulent? Petitioner's claim for delay damages was merely that: a claim founded on a recognized government contracting method of calculation. It was for the government to argue against the claim on a factual basis, and for the trier of fact to make the ultimate determination as to how much, if any, of the delay was compensable to petitioner. It was error as a matter of law for the trial court to conclude that petitioner's *entire* delay claim was fraudulent in the circumstances, and it was error for the Federal Circuit to affirm the trial court's judgment.

Moreover, the Federal Circuit erred in affirming the trial court's finding that there was fraud in the absence of any false documents, or other false information, or a false certification. Under the False Claims Act, fraud against the government exists, inter

alia, when a person "knowingly presents . . . a false or fraudulent claim for payment or approval," 31 U.S.C. § 3729(a)(1), or "knowingly makes, uses, or causes to be made or used, a false record or statement to get a false or fraudulent claim paid or approved." 31 U.S.C. § 3729(a)(2). "Knowingly" is defined to include situations where a claimant "has actual knowledge of" the falsity of information presented to support a claim, "acts in deliberate ignorance of the truth or falsity" of such information, or "acts in reckless disregard of the truth or falsity" of such information. 31 U.S.C. § 3729(b). Likewise, under the Contract Disputes Act, a "misrepresentation of fact," which is one of the elements required for imposition of the penalties provided for in 41 U.S.C. § 604, is "a false statement of substantive fact, or any conduct which leads to a belief of a substantive fact material to proper understanding of the matter in hand, with intent to deceive or mislead." 41 U.S.C. § 601(9).

Aside from certain conclusory statements ("The certified claim itself was false or fraudulent and [petitioner] knew it was false or fraudulent," Pet. App. 121a-122a; "Witnesses admitted that [petitioner] files a certified claim as a negotiating ploy," Pet. App. 129a; "[Petitioner] did not honestly believe that the Government owed it the various amounts when it certified the claim," Pet. App. 133a), the trial court did not make any specific finding that petitioner filed any false documents or otherwise submitted any false information in support of its claim, or falsely certified its claim as required by 41 U.S.C. § 605(c)(1). Without such findings, there was no fraud, and the Federal Circuit erred in affirming the trial court's judgment.

II. REVIEW SHOULD BE GRANTED BECAUSE THE FEDERAL CIRCUIT'S MISINTERPRETATION OF A KEY CONTRACT DISPUTES ACT PROVISION UNDERMINES FUNDAMENTAL COMPONENTS OF THE FEDERAL PROCUREMENT PROCESS

A. The CDA'S Anti-Fraud Provision Applies to All Executive Branch Contractors

In the decision below, the Federal Circuit held that under the Contract Disputes Act's anti-fraud provision, 41 U.S.C. § 604, the proper measure of damages to be awarded to the government is the entirety of a projected, or estimated, claim, rather than the demonstrably fraudulent individual elements of such a claim. As the petition demonstrates, this holding is wrong and has great significance for government contractors.

The Contract Disputes Act applies to all contracts, express or implied, entered into by an Executive Branch department or agency of the United States government (including some non-appropriated fund activities) for the procurement of property (other than real property), services, and real property construction, alteration, repair or maintenance, as well as for the disposal of personal property. 41 U.S.C. § 602(a). The Act also applies to procurement contracts of the Tennessee Valley Authority. *Id.*, § 602(b). Accordingly, the Federal Circuit's erroneous holding with regard to the measure of damages under 41 U.S.C.

§ 604 will affect all contracts for the acquisition of goods or services by Executive Branch agencies. Thus, based on statistics for FY2008 alone, a significant portion of over 190,000 contractors, with pending contracts totaling in the hundreds of billions of dollars in value, will be affected by the lower court's error. *See* http://www.usaspending.gov. To date in FY2009, over $221B worth of contracts have been awarded to nearly 113,000 contractors. *See id.*

Many current and future contractors will be affected adversely by the Federal Circuit's error, because the Federal Circuit has set a disincentivizing "fraud trap" for contractors that must use estimates in presenting their contract claims to the government, as explained hereinafter. Such a situation must not be allowed to continue.

B. The Federal Circuit's New and Unreasonably Low Standard of Proof for Fraud Places Thousands of Current and Future Government Contractors at Risk

The CDA applies to all contracts awarded by executive agencies and to all non-routine requests for payment under those contracts, which are called "claims." A claim is a demand for payment arising under a contract (pursuant to a remedy-granting clause) or relating to a contract (based on an alleged breach). *See* 41 U.S.C. § 605(a); 48 C.F.R. § 52.233-1(b), -(c) (contractual Disputes clause). *See also United States v. Utah Constr. & Mining Co.*, 384 U.S. 394 (1966).

Amounts claimed by contractors often include estimates that require only minimal support to be asserted. As acknowledged by the Federal Circuit in its decision below, estimates may be appropriate in any claim. *See* Pet App. 8a. *See also Ralph L. Jones Co.*, 33 Fed. Cl. at 336 ("It is enough that the contractor supply the court with a 'reasonable basis for computation, even though the result is only approximate"; that is, "[t]he court needs only enough evidence to make a fair and reasonable estimate'") (citing *Miller Elevator Co. v. United States*, 30 Fed. Cl. 662, 702, *appeal dismissed by* 36 F.3d 1111 (Fed. Cir. 1994)). *See also Story Parchment Co. v. Paterson Parchment Paper Co.*, 282 U.S. 555, 562 (1931) ("The rule which precludes the [recovery] of uncertain damages applies to such as are not the result of the wrong, not to those damages which are definitely attributable to the wrong and are only uncertain in their amount."). The Federal Circuit's conclusion, however, that estimates of future costs are inherently suspect, and are somehow broadly tainted by association with some misrepresentations or fraudulent representations in the same claim, so as to subject the claimant to a penalty in the entire amount of the claim, flies in the face of these established principles of government contract dispute resolution with regard to estimated damages.

The Federal Circuit has thus effectively established a low standard of proof of fraud by imposing elevated requirements for proof of estimates that exist nowhere else in the law. While the government is certainly entitled to protect itself from fraud, estimates of contract damages do not necessarily equate to fraud, especially when those estimates are linked to sound

legal theories. The Federal Circuit has exacerbated this problem, though, by holding that if the government can meet the unjustifiably low level of proof required by the circuit's decision below, contractors will face having to pay penalties and forfeiting even their "untainted" claims.

If the Federal Circuit's holding is not reversed, any claim that involves an estimate in any amount or any percentage of the total will be subject to complete forfeiture. This will permit the government to avoid paying actual costs incurred by contractors as well as "valid" estimates that meet the standards of Rule 11 (of both the Court of Federal Claims and the district courts) and the Contract Disputes Act certification for claims exceeding $100,000, and will accordingly create unjustified financial windfalls for the government. In this era of daunting budget deficits, the incentive for the government to misuse and abuse the Federal Circuit's holding is significant.

Likewise, if the holding below is not reversed, any claim is subject to an argument that the contractor did not do enough to support its estimate; that is, that the contractor did not engage experts to assist in formulating the claim, or engaged the wrong experts, or relied on the wrong numbers, or any number of conceivable arguments. Such arguments could always be made to attack the trustworthiness of damage estimates, certainly, but under the Federal Circuit's holding, those arguments are no longer limited to lessening any damages a contractor may ultimately recover; now they would carry the added threat of converting the contractor's entire claim into a penalty

payable to the government. The Federal Circuit's decision blurs the distinction between legitimate, good faith arguments against the merits of a contractor's claim, and what will in all likelihood become routine allegations of fraud by the government if the decision is allowed to stand.

Moreover, if the Federal Circuit's holding is allowed to stand, then contractors that are confronted with a circumstance in which actual damages are difficult to ascertain except on the basis of estimates will have to decide whether to (a) continue to perform the affected contract and be subjected to government arguments regarding unsupported claims and total forfeiture and penalties, or (b) stop performing in potential breach of their obligation under the Disputes clause to continue performance. *See* 48 C.F.R. § 52.233-1(i) ("The Contractor shall proceed diligently with performance of this contract, pending final resolution of any request for relief, claim, appeal, or action arising under the contract, and comply with any decision of the Contracting Officer.").

C. The Federal Circuit's Holding Thwarts Federal Procurement Policies and Creates Disincentives for Contracting with the Government

The Federal Circuit's holding will lead to contractors not believing that they can get a fair shake in the claims process, and ultimately may lead potential sellers of goods and services to the government to conclude that the risk of doing business with the government – and facing potential multi-million dollar

penalties for bringing legitimate claims based in part on good faith estimates – outweighs any potential reward for accepting government contracts.

As discussed above, the decision will discourage government contractors from pursuing legitimate claims for fear that the government will attempt to penalize them whenever a claim includes an estimate of damages. Besides being contrary to law, such a result is contrary to Congress's expressed intent in enacting the CDA to "insure fair and equitable treatment to contractors," S. Rep. No 95-1118 at 1 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5235, 5235.

The Federal Circuit's holding also creates disincentives to current contractors to continue competing for government contracts, as well as to potential contractors that may contemplate entering the government contracting marketplace for the first time. Such a result could be critical to the government by lessening competition, and thus raising prices and lowering quality, in such areas as construction and public works in an era when the government is attempting to rebuild the nation's infrastructure. *See generally, e.g.,* American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5.

The impact on both existing and potential contractors will be especially hard on certain types of businesses. Small and small disadvantaged businesses, for example, will be unduly burdened because claim preparation and resolution will become too expensive, requiring, if the Federal Circuit's holding stands, expensive experts to assist in claim preparation and

presentation. This is contrary to the Federal government's stated policy of encouraging the participation of small and small disadvantaged businesses to seek and perform government contracts. *See, e.g.*, 10 U.S.C. § 631(a) ("It is the declared policy of the Congress that the Government should aid, counsel, assist, and protect, insofar as is possible, the interests of small-business concerns in order to . . . insure that a fair proportion of the total purchases and contracts or subcontracts for property and services for the Government (including but not limited to contracts or subcontracts for maintenance, repair, and construction) be placed with small-business enterprises . . . ."); 48 C.F.R. § 19.201(a) ("It is the policy of the Government to provide maximum practicable opportunities in its acquisitions to small business, veteran-owned small business, service-disabled veteran-owned small business, HUBZone small business, small disadvantaged business, and women-owned small business concerns.").

The holding will also discourage businesses that primarily sell in the non-governmental, commercial marketplace from doing business with the Federal government. Such "commercial" concerns, like small businesses, will view government contracting as unnecessarily expensive because of the necessity to hire experts to assist in claim preparation and presentation. Moreover, because of the viability of their non-government business, such "commercial" concerns will more readily than others view the rewards of selling to the government as incommensurate with the risk of having any claim turned into a penalty under the Federal Circuit's interpretation of 41 U.S.C. § 604. This is also contrary to the government's stated "preference

for the acquisition of commercial items." *See* 48 C.F.R. § 12.000. *See also* 10 U.S.C. § 2377(b)(1); 41 U.S.C. § 264b(b)(1) (preferences of Department of Defense and other Executive Branch agencies, respectively, for acquisition of commercial items; heads of agencies to ensure that procurement officials, "to the maximum extent practicable – acquire commercial items . . . to meet the needs" of the agency).

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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