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THE "TRUTH-IN-NEGOTIATING" CLAUSE OF P.L. 87-653 AS INTERPRETED BY THE ARMED SERVICES BOARD OF CONTRACT APPEALS

Amidst a storm of controversy there was enacted into law on September 10, 1962, Public Law 87-653, which was intended to increase formal advertising whenever possible and, where justification exists for the use of negotiated procurement, to supply appropriate safeguards for Government protection against inflated cost and pricing estimates. Provisions for the latter purpose were inserted to require "truth-in-negotiating," but the terminology of the bill is so ambiguous that perhaps it has created more problems than it has solved.

I. HISTORY

In 1959, audits of Department of Defense (DOD) negotiated contracts by the General Accounting Office (GAO) revealed that the prices charged by some contractors had resulted in unwarranted profits which would not have occurred had Government negotiators been in possession of the current, complete, and accurate pricing data which was available to the contractors. In support of its findings, GAO's report to Congress enumerated specific examples occurring during the preceding year (1958) in which the Government had obtained millions of dollars in refunds.

Taking cognizance of GAO's report to Congress, DOD decided to revise its policies and procedures relative to its negotiated contracts by requiring the disclosure of current, complete, and accurate data by the contractor. The result of this decision was a substantial revision of Armed Services Procurement Regulations (ASPR) Section III, Part 8, entitled Price Negotiation Policies and Techniques. ASPR 3.807-28 was amended to require the contractor to furnish the Government negotiating team with current, complete, and correct cost or pricing data as it became available throughout the negotiation process. At the same time, an entirely new

5. 1960 Hearings 64-70. Most of the overcharges on the contracts were incurred in the airframe and missile industries, and especially in the "fixed-price incentive" type contract. Id. at 125, 685; H.R. Rep. No. 1797, 86th Cong., 2d Sess. 5-6 (1960).
7. Id. at 145-55. ASPR is issued under the authority of the Armed Services Procurement Act, 10 U.S.C. §§ 2301-14 (1964), and represents the most significant procurement regulations to be considered by defense contractors and subcontractors. See generally J. Paul, United States Government Contracts & Subcontracts 20, 31-32 (1964).
subsection, ASPR 3.807–7,9 was added prescribing the form of the newly required Certificate of Current Cost or Pricing Data.

In 1960 the Senate and House Armed Services Committees, disturbed by the contents of the GAO audit reports, conducted hearings to determine the extent of the deficiencies in DOD negotiation procedures with regard to inaccurate pricing data.10 Representative Vinson, on June 8, 1960, introduced H.R. 12572;11 that resolution passed the House on June 24,12 but was not acted on by the Senate before the adjournment of the 86th Congress. H.R. 12572 was reintroduced in the 87th Congress as H.R. 5532. Again the resolution was passed by the House,13 and on July 19, 1962, Chairman Vinson made a lengthy statement in support of it before the Senate Armed Services Committee. He noted that the requirements of the resolution were already contained in ASPR but, relying on information supplied by the GAO,14 indicated that the certificate of data was not being used to the degree Congress desired.15 H.R. 5532 was enacted into law as Public Law 87–653, approved September 10, 1962.16

10. 1960 Hearings.
13. When presented to the House, Congressman Smith, who did not feel that the bill was a "step in the right direction," stated that it came from the Committee with a minority report of three members, whereas "all previous bills from the great Committee on Armed Services have always been reported unanimously by that committee." 108 Cong. Rec. 9967–68 (1962).
15. Hearings on H.R. 5532 Before the Senate Comm. on Armed Services, 87th Cong., 2d Sess. 18 (1962). "Now listen to these figures: Of 364 prime contracts entered into since the regulations were adopted, 121 of them having a total value of $253 million had no certified-cost-data as the regulations require."

DOD also felt that the bill was unnecessary since ASPR adequately covered the subject matter. Id. at 2484. There has been considerable question, however, as to the binding effect of regulations not specifically incorporated into the contract. At the time that P.L. 87–653 was enacted, judicial decisions indicated that procurement regulations not specifically incorporated into the contract were not contractually binding. Hartford Accident & Indem. Co. v. United States, 127 F. Supp. 565 (Cl. Cl. 1955); Caskel Forge, Inc., ASBCA No. 7638, 1962 BCA ¶ 3318; Morrison-Knudsen Co., Inc., IBCA Nos. 36, 50, 59–1 BCA ¶ 2110; Vevier Loose Leaf Co., Inc., ASBCA No. 1500 (1953). Subsequent to passage of this bill, however, there has been some indication that such regulations are deemed incorporated into the contract and are therefore binding. G.L. Christian & Associates v. United States, 312 F.2d 418 (Cl. Cl. 1963); see J. PAUL, UNITED STATES GOVERNMENT CONTRACTS & SUBCONTRACTS 7, 34 (1964).

Others also opposed the bill as unnecessary. See, e.g., Statement of the Aerospace Industries Ass'n, Hearings on H.R. 5532, supra note 15, at 105–07; Statement of H.M. Horner, Chairman of United Aircraft Corp., id. at 107–10; Statement of Machinery and Allied Products Institute, id. at 113–14; Letter from Nat'l Aeronautics & Space Administration to the Chairman, Senate Armed Services Comm., August 8, 1962, U.S. Code Cong. & Ad. News 2486.

Strong support for P.L. 87–653 came from the Comptroller General, who indicated that ASPR was not accomplishing its desired objectives. Letter from Comptroller General of the United States to the Chairman, Senate Armed Services Comm., July 17, 1962, U.S. Code Cong. & Ad. News 2490, 2495. In a well-written
The law added a new subsection, (f), to 10 U.S.C. § 2306 requiring that a prime contractor or subcontractor submit cost or pricing data under certain circumstances prior to the award of a negotiated contract; such data shall be certified to be "accurate, complete and current."17 The certification requirement applies when the contract, change, or modification to the contract will exceed $100,000; it also applies to a subcontract exceeding $100,000 if the prime contractor is required to submit a certificate. The importance of the certificate lies in its proviso that the price certified to the Government shall be adjusted to exclude significant sums by which the head of the agency determines the price was increased due to deficient data.18

The Act has been implemented by regulations19 which require that a "truth-in-negotiating" certificate be submitted prior to the award of a cost-reimbursable,20 incentive,21 or price determinable22 contract, regard-

and persuasive article, the argument has been advanced that the only thing necessary, both before and after enactment of the bill, is for GAO to discharge its statutory duty to inspect the books and records of contractors and subcontractors under negotiated procurements with limited or no competition. McClelland, Negotiated Procurement and the Rule of Law, The Place of Public Law 87-653, 32 Fordham L. Rev. 411, 412-13, 441 (1964). Many cases indicating a need for the "truth-in-negotiating" provision were cited at the hearings on P.L. 87-653. Hearings on H.R. 5532, supra note 15, at 16-18, 29. However, in the majority of these cases, virtually no attempt was made to verify prices submitted by contractors. Hearings on Weapons Systems Management Before a Subcomm. of the House Comm. on Armed Services, 86th Cong., 1st Sess. 346, 632 (1959); McClelland, supra at 441. DOD itself has implied that its determinations filed with GAO in support of its negotiated procurements are rarely questioned because the latter's audits are so highly selective. S. Rep. No. 4, 87th Cong., 1st Sess. 17 (1961). See also 1960 Hearings 571; Hearings on Weapons Systems Management, supra at 346, 380, 673.


18. The problems actually faced by the contractor have been neatly categorized into five departments: (1) invasion of privacy (cost information is of a proprietary nature and is extremely important to a company's competitive position), (2) administrative burden (additional accounting, administrative and legal personnel are sometimes required, resulting in additional costs), (3) subcontract problems (the prime contractor is exposed to a contingent liability against which he may not be able to protect himself), (4) uncertainty in terms (the meaning of the clause and the standards to be applied are ambiguous), and (5) the problem of obtaining "fair and reasonable prices" (the profit margin is too slight to cover non-allowable costs, such as research and development costs and proprietary rights). Pettit, The Defective Pricing Law and Implementing Regulations - A Year and a Half Later, 29 LAW & CONTEMP. PROB. 552, 557-61 (1964). See also Cuneo & Crowell, Negotiated Contracts - Two-Step Procurement, Cost and Pricing Data Requirements and Protests to the Comptroller General, 5 B.C. IND. & COM. L. REV. 43, 59 (1963).

19. ASPR, 32 C.F.R. § 3.807-3 (1967) (Cost or pricing data).

20. Cost-reimbursement contracts "[provide] for payment to the contractor of allowable costs incurred in the performance of the contract, to the extent prescribed in the contract." ASPR, 32 C.F.R. § 3.405-1 (1967). Estimates of total cost are established for the dual purpose of obligating funds and establishing ceilings which can be exceeded by the contractor without prior approval or later ratification by the contracting officer, only at the contractor's own risk. Cost-reimbursement contracts are employed when the costs cannot be estimated with the degree of accuracy required for the use of fixed-price contracts. ASPR, 32 C.F.R. § 3.405-1(b) (1967).

21. A fixed-price incentive contract "is a fixed-price type contract with provision for adjustment of profit and establishment of the final contract price by a formula based on the relationship which final negotiated total cost bears to total target costs." ASPR, 32 C.F.R. § 3.404-4 (1967) (Fixed-price incentive contracts). This type contract is frequently used in research and development or for items not previously produced, and serves as an aid to the contractor in financing the work.

22. A price determinable contract may be either prospective or retrospective. If
less of dollar amount; prior to the award of any “firm fixed-price or 
fixed-price with escalation negotiated contract” that may be in excess of 
$100,000; prior to any contract modification expected to involve more 
than $100,000, regardless of whether the original contract was negotiated 
or formally advertised; and in situations where the negotiated contract or 
modification is not expected to exceed $100,000, when the contracting 
officer so requires.

Before an examination of the specific problems encountered in the 
implementation of the certification provisions, it should be noted that 
there are six exceptions to the above requirements for the certificate:23

(1) Formally advertised contracts — the necessity for current, com-
plete and accurate data does not exist here;

(2) Negotiated fixed-price contracts under $100,000 — it would be 
too burdensome to obtain data for all contracts of this size;

(3) Negotiated fixed-price contracts over $100,000 “where the price 
negotiated is based on adequate price competition” — this terminology 
is undefined, but “adequate price competition” probably can be established 
to when two or more sources are available;24

(4) Negotiated fixed-price contracts over $100,000 where the price 
negotiated is based on “established catalog or market prices of commercial 
items sold in substantial quantities to the general public”25 — required 
here are substantial commercial sales, not including sales to the Government, 
based on established prices;

(5) Prices set by law or regulation — this exception probably is 
not available to contractors since it applies to such things as public 
utilities;

(6) Exceptional cases where the head of the agency waives the 
requirements.

II. Burden of Proof

American Bosch Arma Corp.26 was the first case to be heard by the 
Armed Services Board of Contract Appeals (ASBCA)27 relative to the
pre-statutory defective pricing clause. The contracting officer ordered a price reduction on the grounds that the overstatement of the target price and a failure to disclose current cost information that was reasonably available during the contract price negotiations on a $15 million fixed-price incentive contract had resulted in an unwarranted profit of $45,529.

On appeal, ASBCA placed the burden on the Government to establish: (1) that the contractor furnished inaccurate, incomplete or noncurrent data in the price negotiation; (2) that because of this defective data, the negotiated price was increased; and (3) the precise dollar amount by which the negotiated price was increased.

The facts were that on March 22, 1960, the Ballistics Systems Division, Air Force Systems Command (BSD) negotiation team requested American to submit a cost quotation on two missile guidance sets containing very complex types of electronic equipment. American's initial proposal was submitted on April 5, but BSD subsequently amended its request for proposals five times. On May 31, American submitted its proposal on 49 units. Air Force auditors reviewed this proposal during the week of June 10, and its subsequently prepared audit report contained no exceptions to any of the figures on the costs of purchased parts reflected in American's May 31 proposal. In August, the contractor was advised by BSD that a new contract would be issued for 60 missile guidance sets in lieu of increasing any existing contract. American furnished all the required "back-up" information, none of which related to the costs of materials. Although no demand was made and no further cost or pricing data was submitted by the contractor, during the period from May 31 to the completion of negotiations all of American's data was available to the Air Force auditors on demand.

The Government clearly met its burden of showing that inaccurate, incomplete, and noncurrent data had been submitted by American. American used the data contained in its May 31 proposal for the September negotiations without reflecting the lower prices which could have


28. As used throughout this Comment, the pre-statutory defective pricing clause refers to the 1959 version of ASPR, 32 C.F.R. § 3.807-4 (Certificate of cost or pricing data). As noted earlier, P.L. 87-653, which made mandatory the defective pricing clause, was not enacted until 1962.

29. In 1960, the House Armed Services Subcommittee was given a detailed analysis by the Director of Procurement and Production, Headquarters, Air Materiel Command, Dayton, Ohio, of the procedures followed by the Air Force in negotiating target costs and prices on fixed-price incentive contracts. The Air Force negotiating team consists of about 15 people on the average, "all of them experts," being "better than the contractor's people by far." Prior to the commencement of negotiations, the team constructs its own price "just as the contractor would construct it himself," having done it "independently." This independently constructed price is so low that the contractor "wouldn't have a prayer of making it unless he did something really drastic." The contractor is then required to submit his cost proposal in detail and negotiations are conducted "across the table" until the negotiators arrive at a mutually acceptable target price. 1960 Hearings 304-05.
been obtained on various parts subsequent to its original proposal and prior to final negotiations. However, the question of causality between the defective data and the increased price posed a more difficult problem.

Prior to the commencement of negotiations, the BSD negotiation team had independently arrived at its own price in much the same manner as a prime contractor might have, considering all available information, including the Air Force audit of American’s May 31 proposal. BSD assumed that the cost of materials to the contractor would be the same as his most recent experiences and did not anticipate the reductions which occurred in the June to August period.\(^\text{30}\) If BSD had relied exclusively on its independently constructed price there could be no price adjustment under the clause, even though the contractor had supplied defective data, since without reliance, that data could not have caused an increase in the negotiated price. Notwithstanding this virtually independently constructed price which BSD used in subsequent negotiations, ASBCA found that at least some reliance must have been placed on data supplied by the contractor and ordered a price reduction.\(^\text{31}\)

The inference that the Government might easily meet its burden under the clause was quickly dispelled, however, in the next two price reduction cases, both of which were decided in favor of the contractors. In one, the Government’s negotiating position had been based on its own data and not founded upon information made available by the contractor.\(^\text{32}\) In the other, full disclosure might have led to a price decrease, but only in the event of future negotiations, and such negotiations were not feasible under the circumstances.\(^\text{33}\) Government negotiators thus may find that if

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30. August 15 was considered as the cut-off date for reasonably available data because, in American’s operation, two weeks to a month constituted the time lag from the receipt of a vendor’s quotation to its recording. Anything received after August 15 was considered not to be reasonably available to the negotiators; the contractor was only liable for data up to that date which was not disclosed.

31. The Board admitted to the difficulty of proving that the information supplied by the contractor caused the price increase. The parties do not bargain over specific items, but only as to total price. Each party draws up its own materials cost breakdown so that if the Government had underestimated some other cost elements, the overestimate by the contractor would be washed out in the total figures. As the Board stated: “All this is speculation, of course, as there is no way of ascertaining what would have happened if appellant had disclosed the additional pricing data.” ASBCA No. 10305, 65–2 BCA ¶ 5280, at 24,852–53.

32. FMC Corp., ASBCA Nos. 10995, 11113, 66–1 BCA ¶ 5483.

33. In Defense Electronics, Inc., ASBCA No. 11127, 66–1 BCA ¶ 5604, the contract was awarded to the contractor for a total price of nearly $6 million for telemetry pre-detection systems for use on the Atlantic Missile Range. The original contract was placed by two-step formal advertising (technical proposals are obtained initially, and then bids are obtained from those who submitted acceptable technical proposals). Since the contract was placed by formal advertising, the contract was not subject to the defective pricing data statute, 10 U.S.C. § 2306(f) (1964), except for changes and modifications in excess of $100,000. See pp. 606–07 supra. The contracting officer found that the negotiated price under a change order was increased by $400,296 due to incomplete, inaccurate, or noncurrent cost and pricing data, and reduced the contract by that amount pursuant to the Price Reduction for Defective Cost or Pricing Data clause in the contract. Defense Electronics’ pricing data was incomplete in that it did not include the costs of certain conversion kits. However, the Government was unable to prove that the non-disclosure
they desire to insure a meeting of their burden of proof in the event a claim under the clause arises, they must choose between relying on the contractor's data and forgoing an independent analysis, and relying on their own independently obtained information and perhaps forfeiting a price reduction even though deficient data had been supplied by the contractor. The choice is hardly clear cut, since the cases illustrate that the Government may use both its own information and that disclosed by the contractor and still be entitled to a reduction. The more that the Government uses its own data, however, the more difficult it will be to sustain its burden.

III. COST AND PRICING DATA

What is meant by cost and pricing data is one of the questions that was left unanswered by both the pre-statutory and the current clauses. Under ASPR 3.807-3(e) cost or pricing data is defined as:

that portion of the contractor's submission which is factual. The requirement for "cost or pricing data" subject to certification is satisfied when all facts reasonably available to the contractor up to the time of agreement on price and which might reasonably be expected to affect the price negotiations are accurately disclosed to the contracting officer or his representative. . . . Cost or pricing data, being factual, is that type of information which can be verified. Because the contractor's certificate pertains to "cost or pricing data," it does not make representations as to the accuracy of the contractor's judgment as to the estimated portion of future costs or projections. It does, however, apply to the data upon which the contractor's judgment is based. This distinction between fact and judgment should be clearly understood.

As might have been safely predicted, the Board adopted this broad definition of cost or pricing data, one which covers virtually any factual information available to the contractor at the time of the negotiations. But it also went further by addressing itself to the relevant question of availability of the data to the contract negotiators. ASBCA determined, in American Bosch Arma Corp., which was decided under a pre-statutory clause requiring "reasonably available" cost or pricing data, that a one month period was needed from the time the contractor received the vendor's quotations to the time the negotiators could use them in arriving at the target price. Hence the contractor was not responsible for any

of such data caused any increase in the negotiated price adjustment. In the circumstances of this case it was apparent that there would not be a price reduction without further price negotiations, and such negotiations were not practicable before the bid opening date.

34. Such a dilemma has been suggested by Braemer, Recent Developments in Government Contract Law, 22 Bus. Law. 1057, 1069 (1967).
35. ASPR 32 C.F.R. § 3.807-3(e) (1967) (Cost or pricing data).
36. ASBCA No. 10368, 63-2 BCA ¶ 5280.
data received within one month of the date that the certificate of current pricing was executed. In FMC Corp., 37 where the Board again made a determination as to the lag period, data not within the normal documentation channels of FMC within two weeks of negotiation was considered not reasonably available. 38

The certificate of current pricing now in use does not contain the words "reasonably available" as did the pre-statutory clause; instead it refers to disclosure of data which is available "as of the date of execution of this certificate." 39 This requirement is unrealistic in that it fails to recognize the necessary interim between the time a contractor obtains information and the time at which he is able to forward it to his negotiator. 40 Based on the Board's recognition of the realities of intra-corporate communication, as evidenced in American Bosch Arma Corp., FMC Corp., and Defense Electronics, Inc., it is probable that ASBCA will read the phrase "reasonably available" into the present certificate. Nevertheless, the regulations presently state that the date of the certificate should be, as a general rule, "the date when the contract price was agreed to." 41

For the abovestated reasons, it would seem advisable to alter the regulation to permit contractors to date the certificate as of the time when the data is really current, complete, and accurate, rather than subject the contractor to the risk of an ad hoc determination as to the availability of information.

The danger of withholding any information that might constitute "facts . . . which might reasonably be expected to affect the price negotiation" was brought to light in Cutler-Hammer, Inc. 42 In that case, each

37. ASBCA Nos. 10095, 11113, 66-1 BCA ¶ 5483.
38. Id. at 25,702.
39. ASPR, 32 C.F.R. § 3.807-4 (1967) (Certificate of current cost or pricing data). When a certificate of cost or pricing data is required in accordance with this regulation, a certificate in the form below should be included in the contract file:

CERTIFICATE OF CURRENT COST OR PRICING DATA
(October 1964)

This is to certify that, to the best of my knowledge and belief, cost or pricing data submitted to the Contracting Officer or his representative in support of ___________________________________ are accurate, complete and current as of the date of execution of this certificate.

Firm ___________________________________
Name ___________________________________
Title ___________________________________

Date of Execution

Id.

40. The enormity of the task of preparing a complicated cost estimate prevents a new price or quotation from being instantaneously reflected on the estimate. Vendors' quotations must be received, examined, compared with others, posted, and ultimately transmitted to negotiators. Checking and rechecking by various people is time consuming but essential for the preparation of an accurate cost estimate.
41. ASPR, 32 C.F.R. § 3.807-4 (1967) (Certificate of current cost or pricing data).
42. ASBCA No. 10990, 67-2 BCA ¶ 6432. The case is presently before the Court
of nine airborne electronic analysis systems which were the subject matter of the procurement required antennas, and the contractor chose a particular model, for acceptable technical reasons, which had a restricted availability of sources. Cutler-Hammer received but one quotation which compared favorably with its own in-house cost estimate. Immediately prior to the commencement of negotiations Cutler-Hammer received another proposal, from Transco Products Co., which it felt was so ridiculously low and inconsistent with actual cost experience that it did not recognize it as a valid proposal, and consequently purposely failed to mention its receipt to the Government negotiators. It was only after the completion of negotiations that Cutler-Hammer received Transco’s technical data and decided to take “a calculated risk” by awarding a contract for one set of antennas to Transco. Transco’s work proved satisfactory, and it was eventually awarded all nine sets. The Government’s argument that it would have delayed execution of the contract until more information was available about Transco was rejected as implausible because of its urgent need for the procurement. However, the Board felt that if the Government had been informed of the proposal the antennas would have been excluded from the contract pricing structure and reserved for future negotiation. The case was remanded for negotiation on the issue since ASBCA felt that it was unable to determine by how much the contract price should be reduced on account of the antennas.

It is clear that Transco’s original price quotation did not constitute data upon which a price reduction of the entire contract could have been negotiated. There was, at the completion of negotiations, no basis for evaluating Transco’s technical competence. Therefore the ruling in Cutler-Hammer, Inc. must be interpreted to mean that any time a contractor has any data which might be significant from the standpoint of overall contract negotiations, he must disclose this data to the Government. There is no choice but to read the decision broadly because on the facts of the case the effect of full disclosure on negotiations was only conjectural. It is entirely possible that the Government, realizing that Transco’s price proposal was received immediately prior to negotiations and before any technical evaluation was conducted, would have disregarded this as unreliable and would therefore have arrived at the same target price. ASBCA assumes that the Government would have excluded the antennas from the contract pricing structure, or at least would have conducted the negotiations otherwise than it did. It seems that the Board fails to realize that Cutler-Hammer may not have been willing, for valid reasons, to separately negotiate the price of parts at later date and, as the Government urgently needed the procurement, it is at least possible that the contract price would have been negotiated just as it actually was. The Board seems to read “reasonably be expected to affect the price negotiation” as “might be expected,” thereby placing an unnecessarily heavy burden on the private contractor.
IV. Availability v. Disclosure

The "truth-in-negotiating" clause of P.L. 87-653 requires a contractor or subcontractor to "submit" cost or pricing data under certain circumstances; but whether the submission requirement necessitates disclosing cost or pricing data to the Government or merely requires making such data available has presented a major problem of interpretation. This question was one of the main issues in *Lockheed Aircraft Corp.*\(^{43}\) That case involved a $10.5 million contract for the furnishing of MADREC (Malfunction Detection and Recording Systems) kits for various models of the B-52 aircraft. Although the letter contract was awarded to Lockheed on May 4, 1962, that concern had anticipated the award and had solicited a proposal from its subcontractor, Midwestern Instruments, Inc.,\(^ {44}\) almost three months before. The MADREC system requires a Model 813LQ oscillograph recorder, which was newly developed by Midwestern for the MADREC program; its design requirements differed considerably from the Model 812L recorder manufactured by Midwestern prior to negotiations for the MADREC program. The subcontractor's proposal was thus based on a bill of materials for the earlier model recorder, Model 812L, plus estimates to cover the anticipated differences between the Model 812L recorder as previously produced and the Model 813LQ which had not yet gone into production.\(^ {45}\) Finding Midwestern's proposal acceptable, Lockheed made a purchase order, effective May 15, and the Air Force Administrative Contracting Officer approved it on June 25. In July, Lockheed submitted its proposal. Subsequent to a preliminary price analysis, the Air Force pricing team, in September of 1962, conducted an additional audit of the proposed purchase order price. The Board found that no information had been withheld from the team, and that all of Midwestern's files and bills of materials for the Model 812L recorder had been made available to it. Although a bill of materials was not yet available for the new Model 813LQ recorder, the subcontractor offered to submit one in a few weeks, if desired, but this offer was declined. Thus neither temporary nor partial bills of materials for the new model were submitted to the Air Force.

43. ASBCA No. 10453, 67-1 BCA ¶ 6356.
44. Midwestern's pricing data is the basis of the dispute and it is the real party in interest in the case, although the appeal is filed in the name of the prime contractor, Lockheed. Although the Government has a substantial interest in subcontracts, including this one between Lockheed and Midwestern, there is no direct contractual relationship between the Government and the subcontractor. The prime contractor is primarily liable to the Government for a price reduction in such situations. Whether the reduction can be shifted to the subcontractor depends upon the contractual relationship between the contractor and subcontractor. See generally J. Paul, *supra* note 7, ch. XIII.
45. The industry considers this practice to be an acceptable method for determining the cost of items never before produced. It was also the method used by the contractor in a case decided earlier by the Board. FMC Corp., ASBCA Nos. 10095, 71113, 68-1 BCA ¶ 5483, at 25,896.

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Lockheed and the Government held final negotiations between February 26 and March 2, 1963, using the total price approach, all subcontracts being considered only in terms of their total figures without breakdown. On April 15, 1963, the letter order contract of the preceding May was definitized. In the fall of 1963 GAO began its audit of the negotiated prices of the purchase order awarded to Midwestern. It determined that the subcontractor's prices were overestimated and that "substantially all or 90 percent of the material cost had already been incurred by Midwestern" and was reasonably available to that concern prior to the completion of its negotiations with Lockheed in June 1962.46 The Board found that Midwestern had failed to inform either the Air Force or Lockheed that it possessed firm prices, as opposed to mere estimates, on these materials, and that its duty to disclose this pertinent information was not fulfilled.

In so deciding this case, the Board seems to be imposing a more stringent standard than was formerly employed or is desirable. Midwestern's method of accounting was to accumulate materials cost data on Kardex cards reflecting the cost history of each component. All of the prices for each component of the Model 812L were indicated on the Kardex and as orders were placed on the Model 813LQ, these prices were also recorded on the Kardex. By the time the Air Force conducted its audit in September 1962 Midwestern had accumulated a considerable amount of historical data, all of which was reflected on the Kardex. The entire Kardex file was made available to, and actually used by, the Air Force; in addition, bills of materials were offered, but the invitation was declined. Hence, all data possessed by Midwestern was made available to the Government.

There is language in each of ASBCA's three preceding cases in this area which indicates that the only requirement imposed upon the contractor is to make pertinent data available to the Government. In American Bosch Arma Corp., the Board stated:

Since appellant made available its . . . records to the AF auditors who examined them during the period 10 to 17 June and reported the results of their examination to the BSD negotiating team, we hold that everything that could be found from examination of appellant's records up to 17 June was disclosed to the Government.47

In Defense Electronics, Inc., ASBCA said:

When the contractor made data available to the Government auditor for his use in auditing the contractor's change order price proposal, that was a sufficient furnishing of such data for the purposes of the Price Reduction clause, and the contractor was under no obligation to furnish to the contracting officer personally data not requested by the contracting officer which the contractor had already made available to the Government auditor and which the auditor had used

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46. Lockheed Aircraft Corp., ASBCA No. 10453, 67-1 BCA p 6356, at 29,444.
47. American Bosch Arma Corp., ASBCA No. 15255, 65-2 BCA p 5280, at 24,851
and referred to in the audit report which was furnished to the contracting officer.\footnote{48} FMC Corp. contains similar language. The contractor fulfilled the requirements of the clause on the basis of a stipulation between the parties that

\[\text{[a]ll pertinent FMC books and records relating to the pricing of the changes imposed by Modifications No. 2 and No. 6 were made available to these Government personnel in connection with the negotiation of Modifications No. 137 and No. 138.}\footnote{49}

ASBCA attempted to distinguish \textit{Lockheed Aircraft Corp.} from \textit{American Bosch Arma Corp.} by indicating that in the latter case the Government auditor physically examined the pertinent records.\footnote{50} However, this distinction is questionable because the entire Kardex file was not only presented to the Air Force auditors but was used by them in preparation of their audit and eventually employed in the preparation of the Government's target price. It is, of course, possible that the entire file was not physically examined, but the contractor should in no way be liable for errors flowing from such oversights or value judgments. There is no language in the clause which indicates that the contractor should be held responsible for the Government's use, nonuse, or misuse of data presented to it; to hold him liable is to make him a guarantor of proper performance by Government employees.\footnote{51}

ASBCA seems to weigh heavily GAO's findings that approximately 90 per cent of the material for Model 813LQ had already been ordered prior to completion of negotiations with Lockheed in June 1962. Even if this is true, the undisputed fact is that Midwestern was unaware of this because of its Kardex system. No bill of materials was prepared until completion of performance. The inference from the Board's decision is that Midwestern nevertheless could have discovered this by drawing up a temporary bill of materials for the Model 813LQ. However, the Air Force officer who examined the Kardex file should also have been aware of this because the basic information which would be used to draw up a bill of materials would have come from the Kardex. Indeed, the bill of materials would have reflected no more than the Kardex, albeit in different form. The clause speaks in terms of data and does not specify any particular format for the presentation of that data. There is no requirement that the same data be submitted in various ways, but Midwestern actually went beyond what was required by offering to draw

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49. FMC Corp., ASBCA Nos. 10095, 11113, 66-1 BCA \$ 5483, at 25,710 (emphasis added).

50. Lockheed Aircraft Corp., ASBCA No. 10453, 67-1 BCA \$ 6356, at 29,447.

51. Reply Brief for Appellant at 4, Lockheed Aircraft Corp., ASBCA No. 10453,
up a bill of materials. The fact that this offer was declined should in no way reflect adversely on Midwestern.52

The Board’s decision in Lockheed may have far reaching and burdensome effects for parties engaged in government contracting. No longer is it safe for a contractor to submit all available data to Government auditors, even if such is actually used. It appears that the contractor must be sure that the auditors understand the data; it apparently will avail him little to offer to put the data in more usable form, for if Government hindsight indicates that there is a variance between the negotiated price and the price that would have been arrived at had total contract performance costs been known at the outset, the contractor is in great danger of suffering a loss in the amount of that variance. Lockheed Aircraft Corp. will make it more difficult for the contractor to obtain a satisfactory agreement through good, hard, bargaining, an essential part of negotiated procurement.

V. Significant Sums

Another troublesome question is the amount of increase in contract price that is necessary to warrant a price reduction. The present clause calls for a reduction in price when the price has been increased by "any significant sums"53 because of defective data, but it gives no indication as to what constitutes a significant sum. Nor are the regulations of any help, for they merely repeat the language of the statute in this respect.54 In the first case raising the question, American Bosch Arma Corp., ASBCA indicated that it would construe the term broadly. Although that case dealt with a pre-statutory clause requiring an equitable reduction in price when any significant data was defective, the Board treated the clause like the current statutory provision, finding that significant data is any data that has significant effect on the price. Significance, it held, is determined by dollar amount, not by a percentage relationship to the contract price: "How much it takes to be significant cannot be determined as a percentage of the total price, and we are of the opinion that pricing data which indicates a reduction in total estimated costs of $20,746 below what was otherwise indicated is significant pricing data."55

There is no way to determine from the Board’s ruling in American Bosch just how small a sum would have to be before it would be considered insignificant, but obviously it would have to be extremely small. The amount held significant in American Bosch represented only slightly over one tenth of one per cent of the total contract price, but the Board chose to completely reject the relationship between the $21,000 overcharge and the contract price. On a $15 million contract, this is

52. Id. at 22.
55. ASBCA No. 10505, 65-2 BCA ¶ 5280, at 24,852.
really de minimis, but ASBCA did not so recognize it. A more reasonable rule would seem to be that a sum is not to be considered significant unless it exceeds a specified dollar figure or a set percentage, for example, $50,000 or 10 per cent of the total contract price.\textsuperscript{56} If an increase in contract price is under $50,000 and does not exceed 10 per cent of the total, it would seem, as a practical matter, to be hardly worth the agency’s effort to effect a reduction and attempt to collect it. At the same time, overcharges which would be permitted without a subsequent reduction if a straight percentage formula were used, would be deemed significant if over $50,000. It is submitted that such a formula would be far more equitable and practical than the current ad hoc approach of ASBCA.

VI. Set-Off

The concept of set-off is neither specifically accepted nor rejected by the Defective Pricing clause, leaving somewhat in question the applicability of this doctrine in the area of negotiated procurement. Only recently, in the case of \textit{Cutler-Hammer, Inc.},\textsuperscript{57} involving a contract for nine airborne electronic reconnaissance systems for a target price of $24 million, was the issue squarely presented to the Board.\textsuperscript{58} Included in the contractor’s proposal were numerous duplications in quantities of parts purchased,\textsuperscript{59} resulting in an overestimate of approximately $600,000.\textsuperscript{60} Cutler-Hammer alleged, and the Board found, that it had made serious errors, such as the omission of necessary parts, which resulted in an understatement of some $512,879 in the target price. With some difficulty, ASBCA decided that P.L. 87–653, the Defective Pricing Statute, was enacted solely to provide the Government a vehicle for the recoupment of overpricing resulting from any of the reasons listed therein. In the absence of a clear congressional intent to the contrary, the Board felt compelled to apply a literal interpretation to the statute phrased in terms of adjusting for price deficiencies which tend to overstate the contract

\textsuperscript{56} Prior to the \textit{American Bosch} decision, it was suggested that “a reasonable interpretation would allow a ten per cent increase in the data furnished before action would be taken by the department or agency involved.” Cuneo & Crowell, \textit{supra} note 18, at 58. While this is more realistic than the Board’s position on contracts up to $500,000, it would allow extremely large sums to be deemed “insignificant” on large procurements. Thus, in \textit{American Bosch}, the overcharge would have to amount to at least $1.5 million before action would be taken to reduce the contract price.

\textsuperscript{57} ASBCA No. 10900, 67–2 BCA ¶ 6432.

\textsuperscript{58} Some consideration had been given to this matter in \textit{American Bosch} and \textit{Lockheed}, but the issue was not presented as directly in those cases.

\textsuperscript{59} It is clear that the duplications were unintentional. Cutler-Hammer was given an exceedingly short time to prepare its proposal and, in order to meet the Government-imposed deadline, used employees from other projects who were experienced in formulating proposals by a different method.

\textsuperscript{60} The Government asserted that the defective data caused a $613,159 overstatement of target cost, but the Board reduced this by $75,000, agreeing with the contractor’s contention that the prices were erroneously based on larger quantities than it was expected would be ordered. The smaller the quantities ordered, the higher the prices. ASBCA indicated that the relevant question is what the vendor would have quoted for the smaller quantity, not what the vendor actually charged the contractor. \textit{Cutler-Hammer, Inc.}, ASBCA No. 10900, 67–2 BCA ¶ 6432.
price. The Board cannot be faulted for an analytic reading of the statute, but it can hardly be complimented for its sense of equity.

In *American Bosch* certain deficient items of pricing data which tended to increase the contract price were offset by deficient items which tended to decrease it. Nevertheless, the Government did not raise the propriety of set-off in that appeal, so the Board did not specifically consider it. It is true, as the Board noted in *Cutler-Hammer*, that *American Bosch* involved a pre-statutory version of the clause so that congressional intent as to the issue of offset was not taken into consideration; but the fact remains that the Government felt it was proper to offset deficiencies, and the Board voiced no objection to this practice. Further, the failure of Congress to make mandatory the equitable doctrine of set-off is not to be considered as a rejection of it.

In *Lockheed Aircraft Corp.* the Board addressed itself to whether certain omitted developmental and royalty charges could be offset against overstated material costs:

The obvious answer to the offsetting suggestion is that the equitable reduction permitted under the clause is intended to cover solely the cost items concerning which the pricing data was defective. To permit unrelated offsets would be tantamount to repricing the entire contract, which is not within the contemplation of the clause.61

Although narrowing the concept of offset as it may have been interpreted in *American Bosch*, *Lockheed* made it clear that offset could be permitted in certain circumstances — where the effects are not “unrelated.” The reasonable inference that may be drawn from this case is that, while deleted royalties and experimental charges may not be offset against overstated materials costs, understated or omitted materials costs could be offset against them. In view of the well-recognized fact that perfect accuracy in a price proposal package is impossible of achievement, it is reasonable to assume that the Defective Pricing clause seeks accuracy of the over-all price and not of each and every component thereof; this is further buttressed by DOD’s negotiation methods, which are concerned with the total target price rather than part by part negotiation.62

The legislative history of P.L. 87–653 contains an indication that ASBCA arrived at the wrong result. In reply to Senator Saltonstall’s query about the effect of the bill on “the average contractor . . . a reasonably honest fellow . . . ,” Representative Vinson replied that “a truthful, honest contractor would have nothing to fear under this bill. It is only that contractor which is concealing actual information that he possessed at the time he negotiated that has problems.”63 Senator Saltonstall pursued the question further, wanting to know what happens if an honest

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contractor "makes a wrong guess or something of that kind, that is not from bad intention but is made perhaps, like all of us who make mistakes." 64 Senator Engle replied: "What happens if he does make a mistake? He doesn't get hurt." 65 Again, Representative Vinson stated: "I think no one wants any finality of a decision to be based on erroneous facts... that are not supported by evidence." 66

In spite of these assurances, it is clear from the Board's decision that honest contractors, like Cutler-Hammer, are going to be hurt if offset is totally rejected. In the instant case, the contractor overstated the contract price by $538,000 by overpricing certain materials, while at the same time underpricing or totally failing to include almost $513,000 in the target price. The net result is an overestimate of the target price by approximately $25,000, but the Board has called Cutler-Hammer to respond in damages for the full $538,000, directing it to seek its remedies, if it has any, elsewhere. 67

The issue of offset was specifically considered elsewhere in the hearings, but it appears to have been misunderstood. Senator Cannon commented that deficient data should not add compensation but rather should reduce the total price. 68 Mr. Moore, vice president of Electronic Industries Association, pointed out that the language of the bill provided only for a "one-way street," and that it was unfair to refuse to consider the total context in which a mistake accruing to the Government's benefit was made. 69 Senator Symington's reply was: "[y]ou do not want to make an excess profit even as the result of an honest mistake." 70 Later he asked: "But if you make a mistake, do you feel that you should get an incentive for it?" 71 The issue is not one of rewarding a contractor for his mistake, but is one of fairness to both sides. Equity should require that prior to arriving at any downward adjustment of contract price, offsetting adjustments should be made to reflect the amount by which the contract price was understated. 72 The Cutler-Hammer case is not unique; experience shows that many unintentional mistakes, many of them in

64. Id. at 26.
65. Id.
66. Id. at 27.
67. One administrative remedy open to the contractor is to petition the Comptroller General for relief. 31 U.S.C. § 71 (1964). Since an adverse ruling from the Comptroller General is not binding on the contractor and does not preclude him from judicial relief, it may be advisable for him to file such a petition prior to initiating any court action. 1961 COMP. GEN. ANN. REP. 9-10. For a description of the administrative and judicial remedies of the contractor, see GOVERNMENT CONTRACTS GUIDE ¶¶ 6002-7044 (1967); J. PAUL, supra note 16, chs. XVIII-XX.
68. Hearings on H.R. 5532, supra note 15, at 100.
69. Id.
70. Id.
71. Id. at 101.
72. In the First Session of the 88th Congress, a bill, H.R. 7909, was proposed to amend P.L. 87-653 by, inter alia, specifically allowing offset. Congress failed to act on that measure, so its intent on the matter is inconclusive. However, it is certainly arguable that Congress was merely intending to clarify P.L. 87-653 in regard to offset, thereby indicating that any resulting regulation should be read to include this equitable doctrine.
favor of the Government, are made in large-scale procurement contracts involving highly technical equipment. The position taken by the Board has placed an unfair burden on the contractor when there was no necessity to do so.\textsuperscript{73}

\textbf{VII. Conclusion}

It has been the purpose of this Comment to explore the problem areas created by the “truth-in-negotiating” certificate, to analyze ASBCA decisions dealing with these problems and, hopefully, to offer constructive criticism of these decisions through suggestions of more appropriate solutions. The Government justifiably has been required to bear the burden of proof if it is to receive a price reduction. Although the wording of the statute does not seem to require it, the contractor must apparently “disclose” all information which may affect price negotiations; merely making such information “available” is not sufficient. Regardless of the amount of the total price of the negotiated procurement, the slightest overcharge may result in a reduction under the clause. At least for the present, set-off will not be utilized by the Board to reach an equitable result, and it can only be hoped that the Court of Claims will correct this inequity.

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\textsuperscript{73} The indications are that the Board does not intend to modify its stand. In Sparton Corp., ASBCA No. 11363, 67-2 BCA \textsuperscript{\$} 6539, the cost of a particular tube for a sonobuoy was agreed upon as \$70, but the contractor incorrectly listed it in his Price Analysis as \$95. Each sonobuoy required two of these tubes, but the Analysis only accounted for one. Hence, although the contractor overstated the price by \$25 per tube, he underestimated the price per sonobuoy by \$45. The Government contended that the contractor could not offset the mistake made in the Government’s favor against the one running contrary to the Government. ASBCA stated that “[w]herever may be the appropriate rule regarding ‘set-offs,’ this solution is not regarded by the Board as one involving that principle.” \textit{Id.} at 30,379. The Board felt that Sparton had made a single representation as to total tube cost (\$95) and, even though this quotation was the result of two compensating errors, it actually produced an understatement of cost. Lest someone interpret this to mean that the Board was rejecting its earlier inequitable view of off-set, ASBCA stated: “It is not considered that this is in conflict with previous decisions relating to set-off.” \textit{Id.}
(f) A prime contractor or any subcontractor shall be required to submit cost or pricing data under the circumstances listed below, and shall be required to certify that, to the best of his knowledge and belief, the cost or pricing data he submitted was accurate, complete and current

(1) Prior to the award of any negotiated prime contract under this title where the price is to exceed $100,000;

(2) Prior to the pricing of any contract change or modification for which the price adjusted is expected to exceed $100,000, or such lesser amount as may be prescribed by the head of the agency;

(3) Prior to the award of a subcontract at any tier, where the prime contractor and each higher tier subcontractor have been required to furnish such a certificate, if the price of such contract is expected to exceed $100,000; or

(4) Prior to the pricing of any contract change or modification to a subcontract covered by (3) above, for which the price adjustment is expected to exceed $100,000, or such lesser amount as may be prescribed by the head of the agency.

Any prime contract or change or modification thereto under which such certificate is required shall contain a provision that the price to the Government, including profit or fee, shall be adjusted to exclude any significant sums by which it may be determined by the head of the agency that such price was increased because the contractor or any subcontractor required to furnish such a certificate, furnished cost or pricing data which, as of a date agreed upon between the parties (which date shall be as close to the date of agreement on the negotiated price as is practicable), was inaccurate, incomplete, or noncurrent: Provided, That the requirements of this subsection need not be applied to contracts or subcontracts where the price negotiated is based on adequate price competition, established catalog or market prices of commercial items sold in substantial quantities to the general public, prices set by law or regulation or, in exceptional cases where the head of the agency determines that the requirements of this subsection may be waived and states in writing the reasons for such determination.