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Government Contracts: Key Rules of Construction and Interpretation, Lessons From Recent Decisions

Contra Proferentem, Government's Duty of Good Faith and Fair Dealing, FAR's Hierachy of Definition

WEDNESDAY, SEPTEMBER 25, 2019

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

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Contract Interpretation in Government Contracts

Nicholas T. Solosky, Fox Rothschild, LLP

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Fox Rothschild LLP

- Fox Rothschild LLP is a full-service, 950-lawyer national law firm with 26 offices.
- We give our clients the focus and service of a boutique – with the reach and resources of a national firm.
- Our D.C. attorneys understand the nuances of the government contract and procurement process, particularly in connection with the construction industry. They routinely provide strategic counsel and representation to clients performing government contract work, helping them successfully understand and navigate the many rules and regulations governing all operations of their business while working under contracts as well as the methods and means available to secure equitable treatment and fairness under such contracts.

Berenzweig Leonard LLP

- Berenzweig Leonard is a mid-sized business law firm in the Tysons Corner area.
- Our experienced and dedicated group of attorneys provide a client-focused approach to lawyering, serving the needs of our clients above all else.
- We provide clients with a full suite of legal services including business litigation, employment and labor law, government contracts, corporate and technology law, cybersecurity law, white collar defense and corporate compliance, and intellectual property law.

Contract Interpretation is an Art, Not a Science

- "Contract interpretation is definitely more of an art than a science. It is an art where the words of the documents and the conduct of the parties are collected and aligned with the applicable principles of interpretation into a bouquet of argument, explanation, and justification." *Kenneth Allen, 15-4 BRPAPERS 1 at 3.*
- "Courts and boards follow no predetermined, well-defined analytical framework when giving a contract meaning through the interpretation process. The process of interpretation is fluid rather than rigid." *Cibinic, Nash & Nagle, Administration of Government Contracts 151 (Geo. Wash. Univ. 5th ed. 2016).*

Key Principles

- Intent of the parties is the goal
- What did the parties to the contract want the words of the contract to mean?
- Objective intent vs. subjective intent
- Not a “meeting of the minds”

Contract Interpretation Involves 3 Different Issues

- What constitutes the contract that is to be interpreted?
- What does 1 word/phrase mean?
- Conflicts among several contract words

What Constitutes the Contract That is to be Interpreted?

- At a pre-award oral presentation, a contractor describes the significant extent to which the management staff of its parent company would be involved in contract management. But, none of these commitments had been put in writing and made a part of the contract.
- *Example based on Universal Bldg. Maint., Inc., B-282456, July 15, 1999.*

What Does 1 Word/Phrase Mean?

- Plain Meaning
- Is the word or phrase ambiguous?
- Look at 4 types of extrinsic evidence to resolve the ambiguity:
  - Pre-contract communications
  - Course of performance
  - Course of dealing
  - Trade usage
- If the word or phrase is still ambiguous, use the doctrine of *contra proferentem*

Contract Contents

- It's the first issue analytically, although it is not a common issue
- It establishes the content of the contract– it does not deal with the meaning of the contract
- Are all the things the parties agreed to before signing the contract actually in the contract?

Contract Contents

- Missing, but applicable, contract terms to help establish plain meaning
  - Christian Doctrine
  - Definitions in FAR – FAR 2.101 and other parts of FAR, like FAR 33.101, that defines the word “day” for protest deadlines.
  - FAR Conventions: FAR 1.108: (a) Words and terms. Definitions in Part 2 apply to the entire regulation unless specifically defined in another part, subpart, section, provision, or clause. Words or terms defined in a specific part, subpart, section, provision, or clause have that meaning when used in that part, subpart, section, provision, or clause. Undefined words retain their common dictionary meaning.

What Does 1 Word/Phrase Mean?

- Pre-Contract Communications
- Contractor's actions taken during formation may provide evidence of the reasonableness of later claimed interpretation
  - *Diamond AH, Inc., ENGBCA 4304, 82-2 BCA ¶16,066* (rejecting contractor's seemingly reasonable interpretation that it was not responsible for performing a certain task when contractor made contingency for such performance in its bid and performed task without hesitation)

What Does 1 Word/Phrase Mean?

- Course of Dealing/Performance
- *Restatement (Second) of Contracts § 223*, Course of Dealing
  - A sequence of previous conduct between parties which can fairly be regarded as establishing a common basis of understanding for interpreting their expressions and conduct.
  - Unless otherwise agreed, a course of dealing between the parties gives meaning to or supplements or qualifies their agreement.

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What Does 1 Word/Phrase Mean?

- Trade usage
- A NASA contract required the contractor to put in “new lamps” when the construction project was completed. NASA interpreted the phrase “new lamps” to mean the contractor had to replace any existing lamp installed prior to construction, even those still working, so that all lamps in the building would be new. The contractor disagreed and won by pointing out that, in the industry, replacing all lamps is “relamping”; the contract’s phrase “new lamps” means replacing only those lamps that are defective, burned out, or broken.
- *Metric Constructors, Inc.*, 169 F.3d 747 (Fed. Cir. 1999).

Conflicts Among Several Contract Words in Different Parts of the Contract

Subpart 2.1(A) of a construction specification, "Materials" called for a contractor to use painted steel sheet for a roof deck and did not refer to galvanization. But subpart 2.3(A) dealing with fabrication of the roof decking said the roof deck had to use galvanized sheet. The court interpreted the contract to require galvanized steel. Although subpart 2.1(A), standing alone, might support the contractor's position, the contractor's interpretation failed to harmonize its position with subpart 2.3(A). Contract clauses cannot be interpreted in isolation.

- *H.B. Zachry Co. v. United States*, 28 Fed. Cl. 77, 80–81 (1993), *aff'd*, 17 F.3d 1443 (Fed. Cir. 1994)

Contract Contents

- Parol Evidence Rule
  - A deal is a deal.
    - When the parties enter into what they (objectively) intend to be their total agreement, prior agreements and commitments that have not been captured in their final written agreement cannot be used to add to, detract from, or change the final agreement.
    - IMPORTANT: However, as we will see later, parol evidence -- prior agreements and commitments that have not been captured in their final written agreement – can be used to interpret ambiguous language. The parol evidence rule does not bar the use of evidence to interpret a contract--some other rule might; but not the parol evidence rule.
    - *15-4 BRPAPERS 1, 15-4 Briefing Papers 1, 5*

Contract Contents

Best practices:

- Control the contract's contents!
- Incorporate a document by reference
- Make a document into a completely integrated agreement

The Wrong Way to Incorporate By Reference

- Contractor bought software from a developer that the contractor in turn leased to the U.S. Army. But, before the government signed a contract, an army employee signed a "Letter of Essential Need," claiming that the software was "essential to the operation of" and "integral to" Army computers. After using the software for several years, the Army refused to exercise a renewal option. The contractor sued the Army arguing that the government could not cancel its renewal option because not only had the language in the Letter of Essential Need prevented the government from doing so but also the Letter had been incorporated into the government contract. The CAFC disagreed, concluding that the letter had not been properly incorporated by reference into the contract.
- *Northrup Grumman Information Technology, Inc. v. U.S.*, 535 F.3d 1339 (Fed.Cir. 2008).

It Was Wrong Because …

- The contract DID incorporate by reference the "[t]he 'LEASING TERMS AND CONDITIONS' to Special Offer # 330 Revision 03 ... were incorporated ... in order to facilitate this [Delivery Order]" By thus explicitly referring to the Terms and Conditions and reciting that they "were incorporated."
- But the Terms and Conditions did NOT incorporate the Letter of Essential Need by reference. The Terms and Conditions simply stated "[i]t is hereby mutually understood and agreed that as inducement for Contractor entering into this Agreement, the Government has provided required information relative to the essential use of the software Asset which includes, but is not limited to, a description of the currently identified applications to be supported and planned life-cycle operations for the leased software" (emphasis added). According to Northrop, the "required information" referenced here is the statement, contained in the Letter of Essential Need, that the leased software was "essential to the operation of ABCS 6.0 as [it is] integral to the system."
- However, the Terms and Conditions do not refer to the Letter of Essential Need explicitly, as by title or date, or otherwise in any similarly clear, precise manner.
- *Northrop Grumman Info. Tech., Inc. v. United States*, 535 F.3d 1339, 1346 (Fed. Cir. 2008)

Incorporating a Document by Reference, the Right Way

- Use clear and express language that leaves no ambiguity about the identity of the document being referenced.
- Use an integration clause that expressly incorporates the extrinsic evidence.
- The parties do not have to use any kind of magic words but some helpful phrases were “is incorporated as though fully set forth herein” and by identifying a particular document, such as the title, date, parties to, and section headings of any document to be incorporated.

Merger Clauses-Integrated Agreements

According to the parol evidence rule, prior written or oral agreements:

- Cannot contradict language in a **partially or fully integrated** agreement.
- Cannot add to or modify the terms of a **fully integrated** agreement.

Merger Clauses-Integrated Agreements

- "If the parties did not intend their document to be the final expression of their thoughts, it was the claimant's folly to have signed it."
- *Brawley v. United States*, 96 U.S. 168, 173–74, 24 L.Ed. Brawley v. United States, 96 U.S. 168, 173–74, 24 L.Ed. 622 (1878)

Merger Clauses-Integrated Agreements

- (1) An integrated agreement is a writing or writings constituting a final expression of one or more terms of an agreement.
- (3) Where the parties reduce an agreement to a writing which in view of its completeness and specificity reasonably appears to be a complete agreement, it is taken to be an integrated agreement unless it is established by other evidence that the writing did not constitute a final expression.
- *Restatement (Second) of Contracts § 209 (1981)*

Clause Creating a Completely Integrated Agreement

- "Both parties expressly state that the aforesaid recitals are the complete and total terms and conditions of their Agreement."
- An integration clause "conclusively establishes that the integration is total unless (a) the document is obviously incomplete or (b) the merger clause was included as a result of fraud or mistake or any other reason to set aside the contract."
- *Rumsfeld v. Freedom NY, Inc.*, 329 F.3d 1320, 1323 (Fed. Cir.), *adhered to on denial of reh'g en banc*, 346 F.3d 1359 (Fed. Cir. 2003).

Partially Integrated Agreement

The typical government contract should be considered a partially integrated agreement:

> "The scope and complexity of problems encountered throughout the performance of the government contract ordinarily involve contingencies not expressly provided for under the terms of the agreement. Resolution of such problems often requires information outside the contract documents. The written contracts in many instances cannot be characterized as the 'complete and exclusive' agreement of the parties and therefore should be considered to be partially integrated. This is particularly so for contract modifications and other agreements entered into during contract performance."

- *J. Cibinic, Jr., J.F. Nagle, and R.C. Nash Jr., Administration of Government Contracts, 5th ed. (Washington, DC: George Washington University, 2016) at 192.*

Merger Clauses-Integrated Agreements

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Merger Clauses-Integrated Agreements

- Proper use of parol evidence:

A contractor agreed to lower its bid on a contract for building a hydrant refueling station on an isolated island if the government would award him a contract to build on the same island at the same time a diesel-powered generator. The agreement was oral.

The ASBCA allowed evidence of the oral agreement to be considered in a claim for delay damages under the hydrant refueling station contract. The saving the contractor expected from concurrent performance of the two contracts did not materialize because the government delayed the construction of the diesel-powered generator. The oral agreement of concurrent performance did not contradict the terms of the hydrant refueling station contract.

- *Pan Arctic Corp.*, ASBCA 20133, 77-1 BCA P 12,514 (1977).

Key Principles of Contract Construction and Interpretation

- **Objective Intent Is the KEY**
- **Court or Board Will Be Looking to Determine the Intent of the Parties (as manifested in words and circumstances)**
- **Reasonable Person Test**
  - Boards/Courts apply an objective test -- What a "similarly situated, reasonably prudent contractor would have understood the contract language to mean." *KMS Fusion, Inc. v. United States, 36 Fed. Cl. 68, 77 (1996) (citing City of Oxnard v. United States, 851 F.2d 344, 347 [Fed. Cir. 1988])*.

Best case scenario is that the parties are on the same page when executing the contract . . . and are able to remain on the same page through successful completion.

The Written Contract Controls

- The Written Contract is the Primary (and **Often Exclusive**) Evidence of the Parties' Agreement
- True for almost all government contract disputes
- Rely on the Contract – not other sources
- Example:

Program & Constr. Mgmt. Group v. GSA, 246 F.3d 1363 (Fed. Cir. 2001)

  - GSA **deletes** requirement for cafeteria from RFP . . .
  - Contract **includes** requirement to keep cafeteria open
  - **Outcome: The CONTRACT Controls**

Intrinsic Evidence

- **Definitions of terms:**
  - Definitions written specifically for the contract given most weight
  - FAR 2.101 provides definitions for common contracts terms, phrases
  - Dictionaries can be used when terms are undefined. *FAR 1.108(a)*.
  - Technical language as it's commonly used prevails in transactions within related technical field, unless a different intention is manifested. *RS (2d) § 202*.

Key Contract Interpretation Principles

- **Read the Writing as a Whole**
  - In other words . . . Read and interpret all writings that are part of the same transaction **together**
  - **Avoid** attempts to interpret a Contract provision in a way that divorces it from the rest of the agreement.
  - **Examples:** Drawings, Addenda, Q&A

Dispute Resolution Evidence

- **Extrinsic Evidence**
  - **Court/Board Will NOT Consider Extrinsic Evidence if the Contract Is Clear on its Face**
- **Unambiguous** means "amenable to only one reasonable construction." *Dana Corp. v. United States, 470 F.2d 1032, 1043 (Ct. Cl. 1972)*
- **Ambiguity** "exists when a contract is susceptible to more than one reasonable interpretation." *E.L. Hamm & Associates v. England, 379 F.3d 1334, 1341 (Fed. Cir. 2004)*

Extrinsic Evidence

- Once **Ambiguity** Exists . . . Courts/Boards Give **Extrinsic Evidence <u>Great Weight</u>**
- **Three Basic Forms**
  1. **Discussions and Concurrent Actions**
  2. **Prior Course of Dealing**
  3. **Custom and Trade Usage**

Extrinsic Evidence

- **Discussions and Concurrent Actions**
  - **Requests for Clarification**
    - Government clarifications provided prior to Contract formation or during early performance
    - Reliance on oral representations or clarifications
    - Cannot conflict with express Contract language
  - **Pre-Bid Conferences**
    - Not binding if Government representations conflict with clear Contract language

Extrinsic Evidence

- **Discussions and Concurrent Actions**
  - **Pre-Dispute Interpretations**
    - Shared interpretation of key issue(s) in dispute
    - *Sundstrand Corp.*, *ASBCA 51572 – ASBCA* holds Government bound to Contracting Officer's interpretation prior to obtaining legal advice
    - Evidence from prior Contracts
  - **Pre-Dispute Actions Evidencing Interpretation**
    - Actions taken during formation, performance, or prior to dispute

Course of Dealing/Performance

- The actions of **Government and its employees** can be evidence of how the parties interpret the contract:
  - Board found a government project engineer's failure to object to contractor testing a cleaning method in accordance with its interpretation to be persuasive evidence of how the parties interpreted their contract. *Sentell Bros., Inc., DOTBCA 1824, 89-3 BCA ¶21,904*
  - The government making payments for eight years based on contractor's interpretation was course of performance evidence demonstrating shared interpretation. *KD1 Dev., Inc. v. Johnson, 495 Fed. Appx. 84 (Fed. Cir. 2012)*

Course of Dealing/Performance

- **Restatement (Second) of Contracts § 223, Course of Dealing**
  - A sequence of previous conduct between parties which can fairly be regarded as establishing a common basis of understanding for interpreting their expressions and conduct.
  - Unless otherwise agreed, a course of dealing between the parties gives meaning to or supplements or qualifies their agreement.
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Custom and Trade Usage

- How language is used in a particular trade is taken into account when interpreting technical contracts
- Evidence of trade usage may be considered when contract language is unambiguous **BUT** it cannot be used "to create an ambiguity where a contract was not reasonably susceptible of differing interpretations at time of contracting." There are, however, many decisions that refuse to admit evidence of trade usage when contract language is unambiguous. *TEG-Paradigm Envtl., Inc. v. U.S., 465 F.3d 1329, 1338 (Fed. Cir. 2006).*

For More Information

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