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James "Ty" Hughes, Esq.
Deputy General Counsel for Acquisition Policy
United States Airforce
In care of Ms Laura Auletta
Designated Federal Officer
Acquisition Advisory Panel

VIA EMAIL: laura.auletta@gsa.gov

Re: Acquisition Advisory Panel Commercial Practices Working Group / Revisions to
Proposal For Statutory Reform of Interest Provisions

Dear Mr. Hughes:

We are writing to you on the subject of interest in your capacity as Chairman of the Commercial Practices Working Group of the Acquisition Advisory Panel (the "Panel," also called the "Section 1423 Panel"). As you know, on March 4, 2006, Alan Peterson made a presentation to the Council of the Section of Public Contract Law of the American Bar Association. The ABA presentation concerned our proposal to provide for more equitable payment of interest in disputes, claims and similar situations, as well as fairness and efficiency, and was similar to the presentation we made to the Panel in June 2005.

Following that March 4, 2006 Council presentation, and as a result of suggestions made by senior members of the Council, we have revised the proposed statutory language we first submitted to the Panel on August 15, 2005.

The revised language, entitled "Proposal For Reform Of Interest Provisions," is contained in the attached file. Major changes to the previous language include a "streamlining" to deal only with modifications to the Contract Disputes Act, the addition of a "Preface," and a new paragraph to address "stand alone" interest claims [see paragraph B.(b) in the accompanying file], together with an explanatory paragraph. The revised proposed language was submitted to the Contract Claims and Disputes Resolution Committee of the Section of Public Contract Law late last week.

We thought it important that you should have our latest proposal even though it appears that the Panel will be unable to consider the interest questions given the various other issues that the Commercial Practices Working Group is tackling and the limited amount of time the Panel has to address the complex and wide-ranging matters in its Congressional charter. Again, we ask that the record be clear that the Panel was not able to reach the merits of our views.

We would be pleased to discuss any of the above matters further with you or other Panel members and staff.

Thank you.

Very truly yours,


Alan E. Peterson


Alan V. Washburn


Thomas Patrick

PROPOSAL FOR REFORM OF INTEREST PROVISIONS

May 3, 2006

Preface

The Supreme Court has repeatedly recognized in a variety of contexts that interest is awarded because of considerations of fairness, as a step toward making a party reasonably whole for another party's act or omission. E.g., *Milwaukee v. Cement Div., National Gypsum Co.*, 516 U.S. 189, 194-197 (1995) (citing numerous authorities). Awarding interest to contractors with the Federal government also carries out another recognized principle, namely "The United States does business on business terms." *United States v. National Exchange Bank*, 270 U.S. 527, 534 (1924). That principle has been reiterated several times by the Supreme Court; among recent instances is *United States v. Winstar*, 518 U.S. 832, 895 (1996) (plurality opn).

Congress took a major step toward achieving such objectives by providing for Government liability for interest in certain circumstances under contracts covered by the Contract Disputes Act of 1978. Since that Act took effect, experience and analysis have shown the desirability of extending interest coverage of the Act to additional contracts and refining the interest provisions of that Act. The following revisions to current law are proposed in accordance with the foregoing philosophies to enhance fairness and comparability with commercial contracting; the changes are easily accomplished.

A. The Contract Disputes Act of 1978, 41 U.S.C. sec. 601 ff., covers interest in connection with contracts covered by that Act. That Act does not, however, apply to a variety of contracts that the United States makes, and fairness would be enhanced by extending the interest provisions of that Act to such other contracts. The following language is suggested as a new section in Title 41, which deals with government contracts:

"Interest shall be payable on all amounts found due to the contractor upon all claims, increased costs, damages, or any other amount found due the contractor for any reason in connection with any contract of the United States, including but not limited to repayment, restitution, or an underpayment, whether or not the contract is identified as a contract covered by Sections 3 and 4 of the Contract Disputes Act of 1978, 41 U.S.C. sec. 602 and 603. Such interest shall be determined by the methods set out in Section 12 of that Act, as amended. For any contract not covered by said Sections 2 or 3 of that Act, the term "claim" as used in said Section 12 shall be deemed to mean a presentation meeting the requirements of the United States agency responsible for the contract or any administrative tribunal or court with jurisdiction."

B. To provide greater fairness, including an earlier starting date, a more realistic interest rate, and compounding for interest payable to contractors with the U.S.:

"Section 12 of the Contract Disputes Act of 1978, 41 U.S.C. sec. 611, is revised as follows:

(a) Interest on amounts found due contractors on (i) claims against the United States in relation to a contract with the United States, including, but not limited to any increased costs, caused by the United States and compensable under a contract clause, or any damages for breach of contract, or (ii) any other amount found due the contractor for any other reason in connection with any contract of the United States, including, but not limited to, repayment, restitution, or an underpayment, shall be paid to the contractor and determined as follows:

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(1) for any such amount found due the contractor for increased costs for which a contract clause or doctrines of breach of contract provide a remedy to the contractor, with such interest to run from the date on which each increment of increased costs was incurred; or

(2) for any other such amount found due the contractor for any reason, including but not limited to breach of contract, repayment, restitution, or underpayment, in connection with any contract of the United States, with such interest to run from the date on which the contractor's right against the United States accrued.

(3) Interest under this Section shall be computed at the applicable underpayment rate effective for each calendar quarter as prescribed by the Secretary of the Treasury under 26 U.S.C. sec. 6621(a)(2), and shall be compounded quarterly. Interest payable under this paragraph (a) shall be calculated by applying the foregoing rate to that portion of the principal amount found due, with such amount assigned to each related calendar quarter using any calculation method that results in an equitable determination of interest.

(4) Any partial or provisional payment made by the United States to the contractor on account of, or allocable to, the principal amount in a calendar quarter shall be deducted from that principal amount before interest is computed for that quarter.

(5) Interest under this Section shall run until the earlier of (1) the date of payment by the United States, by means of mailing, electronic transmission, or physical delivery; or (b) the commencement of interest that may be due under another statute of the United States and applicable to any amount for which interest is due under this Section."

[Some Boards and Courts have held that current law denies recovery to contractors with the United States of damages for incurred interest when represented as interest on a "stand alone," or interest only basis, i.e., interest that is not incurred as a result of financing an element or elements constituting an amount found due, and is claimed without an accompanying claim for the principal amount from which the incurred interest cost derives. To take only one example, in *J.D. Hedin Construction Co. v. United States*, 456 F.2d 1315, 1330-1331 (Ct. Cl. 1972), the contractor was denied interest incurred when a Government-caused "delay forced the contractor to borrow money to carry on his contract." In accordance with the objective of providing greater overall interest fairness, the following paragraph (b) amends the Contract Disputes Act to provide compensation to contractors for such "stand alone" or interest only damages, or component of damages, without regard to whether the nature of the capital generating the applicable incurred interest--the cost of capital--is equity or borrowed capital. Paragraph (b) treats the amount of such incurred interest damages as an amount found due, which amount is entitled to earn Contract Disputes Act interest until final payment by the United States, consistent with any other claim that is determined to be an amount found due.]

(b) Whenever a contractor incurs interest costs, whether for debt or equity financing, as a result of an act or omission of the United States coming within subparagraphs (a)(i) or (a)(ii) above, but the principal to which such interest is applicable is not an amount found due from the United States to the contractor, the United States shall compensate the contractor for such costs. Such costs shall be treated as an amount found due and subject to this Section."

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C. To avoid any potential conflict with language barring inclusion of interest in the pricing of various U.S. contracts, the following section should also be added to Title 41:

“Effective with the enactment of this Section, no regulation or contract clause shall limit the payment of interest provided by this Section.”