



FEDERAL CONTRACTS



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Interest

Contrasting CBCA and COFC Decisions Illustrate What “Disputes” Will Toll the Accrual of Prompt Payment Act Interest

By DAVID W. BURGETT AND
EDWARD C. EICH*

In recent decisions, the Civilian Board of Contract Appeals (CBCA) and U.S. Court of Federal Claims both analyzed the scope of the Prompt Payment Act’s (PPA), 31 U.S.C. §§ 3901-3907 (2006), “dispute” exception. *Delta Air Lines, Inc. v. General Services Admin.*, CBCA No. 1306, 09-1 BCA ¶ 34,052 (Jan. 23, 2009); *PCL Constr. Servs., Inc. v. United States*, 84 Fed. Cl. 601 (2008). Although the forums reached different outcomes, the opinions are consistent with each other and provide guidance on when the United States government is required to include an interest penalty on funds paid after the designated payment date.

Enacted in 1982, the PPA entitles contractors to receive interest at a rate set by the Department of the Treasury when the government fails to make a payment within 30 days of receiving a proper invoice, unless the contract or another statutory provision establishes a different deadline. 31 U.S.C. § 3902. Interest accrues from the required payment date through the date the final payment is made, the contractor files a claim under the Contract Disputes Act (CDA), 41 U.S.C. §§ 601-613, or one year passes, whichever occurs first. See 5 C.F.R. § 1315.10.

In 1988, Congress amended the PPA to close a number of loopholes that the government had used to avoid paying interest. See Pub. L. No. 100-496 §§ 1-14, 102 Stat. 2455 (1988). It removed the late payment grace periods, clarified when an agency receives an invoice, and

expanded the statutory requirements to cover progress payments and subcontracts. *Id.* However, Congress left in place the exception for disputes over quantity, quality, or compliance with any contractual requirement. See 31 U.S.C. § 3907(c). Claims related to such a dispute and interest payable for the period during which the dispute is being resolved are subject exclusively to the CDA. 31 U.S.C. § 3907(c); 41 U.S.C. § 605. Accordingly, interest on disputed payments will only accrue once the contracting officer receives a proper claim. 41 U.S.C. § 611.

The following CBCA and COFC decisions, when read together, illustrate the critical distinction between legitimate and improper withholdings and the limits of the PPA’s “dispute” exception.

Delta Air Lines, Inc. v. General Services Administration:

On January 23, 2009, the CBCA found the General Services Administration liable for unpaid PPA interest based on its improper withholding of funds owed to Delta Air Lines, Inc. (Delta) for post-bankruptcy petition transportation services. The facts giving rise to the case began in March 2004 when the Government Accountability Office issued a report alleging that the Department of Defense paid several commercial airlines, including Delta, for unused airline tickets in 2001 and 2002.

GSA demanded repayment and threatened to recoup the alleged overpayments from invoices for future government travel. In September 2005, the agency began

withholding payment on thousands of travel requests performed after Delta filed for Chapter 11 bankruptcy protection.¹ GSA's action, however, was not based on concerns about Delta's performance of the invoiced contracts. Instead, it was trying to collect funds paid to Delta under separate travel contracts that had been closed out three to six years earlier.

In November 2006, the bankruptcy court issued a declaratory judgment that GSA lacked authority to offset Delta's preexisting debts from amounts due for services performed while the airline was operating in bankruptcy. Although the withholding would have been authorized outside of bankruptcy under a variety of recovery statutes, it was specifically prohibited by the Bankruptcy Code's automatic stay provision. GSA eventually paid the invoices without interest in March and August 2007. On January 31, 2008, Delta filed a certified claim under the CDA for the unpaid interest. GSA denied the claim and Delta appealed the agency's decision to the CBCA.

The issue before the Board was whether a dispute over the performance of an unrelated contract could excuse the government from its obligation to include interest on late payments. There was no question about the validity of Delta's post-petition invoices. The fact that GSA was trying to recoup other debts by withholding payment was conclusive evidence that it did not question Delta's performance of the 2005, 2006, and 2007 contracts.

Nevertheless, GSA argued that a good faith withholding – even though later held erroneous – was sufficient to invoke the exception. It also claimed that the parties' litigation over the applicability of the automatic stay provision constituted a dispute. Delta interpreted the exception far more narrowly. The airline argued that the plain language of the statute and its legislative history only exempt the payment of interest when there is a dispute related to the particular contract under which the late-paid invoice is issued.

The CBCA agreed with Delta. It held that "PPA interest fails to run on payment[s] for contracted-for property or services only when an agency disputes that the contractor performed the work for which it has invoiced or the invoice is otherwise defective." The decision stated that these were the "sole situations" when the government could avoid its obligation to pay interest. GSA never claimed that Delta failed to provide the required services or that the invoices were improperly prepared. Since the setoff had been held improper and no statutory exception was applicable, the CBCA awarded Delta interest starting thirty days after each invoice was received by the government and continuing to the date of payment or one year after the invoice became due, whichever occurred first.

PCL Construction Services, Inc. v. United States:

On November 14, 2008, the COFC issued a sixth opinion in the long-standing dispute between PCL Construction Services, Inc. (PCL) and the Department of Interior's Bureau of Reclamation (USBR) over the construction of the Hoover Dam's visitor center and parking garage. The issue was whether the PPA entitled PCL to recover interest on funds "temporarily withheld" for

protection of the government's interests that were ultimately returned to the contractor. However, unlike the prior example, the COFC concluded that the withholding was legitimate and that there was a dispute over the performance of the underlying contract.

In March and April 1995, the USBR withheld \$1,351,838 from payments for completed work to cover "accrued liquidated damages, outstanding required submittals, and credits due the government for changes and/or reductions in work." The contracting officer later certified that the contract was substantially complete as of May 11, 1995. After USBR denied PCL's request that the retainage be released, the contractor appealed to the COFC, which ordered that the entire amount be paid "plus interest." The Court's prior decision explained that (i) there was insufficient evidence to allocate the responsibility for delay, which annulled PCL's liability for liquidated damages and (ii) the government failed to provide a basis for the amount of its withholding for incomplete work.

On September 12, 2003, the Department of Treasury paid PCL \$1,984,690, which included the entire retainage plus \$632,852 in CDA interest. The matter then returned to the COFC where PCL argued that it was also entitled to an additional \$45,132 in PPA interest. PCL claimed that the prior decision's non-specific award of principal "plus interest" encompassed both CDA interest, which was undisputed, and PPA interest beginning thirty days after the government received its invoice seeking the release of the withheld funds and ending when PCL filed its certified claim.

The government successfully opposed PCL's claim on two grounds.² It argued that Federal Acquisition Regulation (FAR) clause 52.232-27, Prompt Payment for Construction Contracts (Apr. 1989), prohibited the accrual of PPA interest because the funds were retained in accordance with the contract, and that there was a bona fide dispute over PCL's performance of the contract. *PCL Constr. Servs., Inc.*, 84 Fed. Cl. at 605-06 (citing 48 C.F.R. § 52.232-27(a)(4)(iv) (Apr. 1989)).³

Withholding Authorized by a Contract Provision.

The COFC accepted the government's position that the initial withholding complied with the contract's retainage clause. Relying on the discretion traditionally afforded to agency officials administering construction contracts, it held that the record contained sufficient evidence of incomplete work and contractor-caused delays to justify USBR's action. Thus, the retainage was legitimate and the government was not obligated to pay PPA interest, even though the Court could not ultimately allocate causation and responsibility between the parties.

A withholding is legitimate when: (i) it is authorized by law, regulation, or contract; (ii) the procedural requisites are followed; and (iii) the action is reasonable. If a court or board finds that either the amount of a withholding or the withholding itself is improper, then the government will be liable for PPA interest unless another exception applies. For example, under the Debt

¹ In this context, each airline ticket constitutes a separate contract. *American Airlines, Inc. v. Austin*, 778 F. Supp 72, 76 (1991).

² The government also argued, unsuccessfully, that PCL's failure to request PPA interest in its complaint should bar the recovery of any additional interest. However, citing a long line of contrary authority, the COFC held that PCL was not required to specifically cite the statute.

³ The current FAR clause moved the referenced language to 48 C.F.R. § 52.232-27(a)(4)(ii).

Collection Act, the failure to provide a contractor with written notice of the type and amount of the claim, the government's intention to collect the claim by administrative offset, or an explanation of the contractor's rights would result in a determination that a withholding was improper. See 31 U.S.C. § 3716. A court or board would then consider if any other exception applied. If not, PPA interest would accrue. This was the situation in *Delta Air Lines*. A federal court held that GSA had no right to offset Delta's prior debts against travel purchased after the airline filed for bankruptcy. Delta was then entitled to recover PPA interest because the alleged dispute involved contracts unrelated to the invoices seeking payment.

In *PCL Construction Services*, the contractor unsuccessfully argued that the government's retainage was unreasonable. Relying on a prior COFC decision, PCL claimed that the agency improperly contested the release of the retained funds after the contracting officer certified that the project was substantially complete. In *Arkansas Best Freight Systems, Inc. v. United States*, 20 Ct. Cl. 776 (1990), the Court awarded PPA interest after holding that the agency's attempt to "create a dispute out of generic review responsibilities and complexities inherent in an audit is inconsistent with [the PPA's] language." *Id.* at 779. PCL's situation, however, could not support such a theory. There was no evidence of bad faith in the record and the trial testimony clearly showed the existence of significant contractor-caused delays and incomplete work.

Dispute Exception. The rest of the *PCL Construction Services* decision addresses the government's alternate argument, that there was a "dispute" over the amount of the payment or compliance with the terms of PCL's contract. The Court explained that "[PPA] interest is only available when government payments are 'inadvertently late, and not when the Government refuses to pay or questions its underlying liability.'" *PCL Constr. Servs., Inc.*, 84 Fed. Cl. at 607 (quoting *Laurelwood Homes LLC v. United States*, 78 Fed. Cl. 290, 292-93 (2007)); but see *Arkansas Best Freight Sys., Inc.*, 20 Ct. Cl. at 778-79 (holding that one must assume there was no dispute, only an offset or mistake where the government eventually pays a contractor the full amount invoiced).

In this case, there was no question that the dispute arose out of PCL's performance of the Hoover Dam visitor center and parking garage contract. In a July 28, 1995, letter, the USBR specifically rejected PCL's request that the retained funds be released based on unresolved claims for liquidated damages, unfinished work, and reductions in contract scope. The parties then presented extensive evidence at trial on the cause of various construction delays and outstanding punch list items. Moreover, the COFC recognized that, as a matter of law, the refusal to pay the entire amount requested is sufficient evidence of a dispute over payment

of the invoice. *Id.* at 608 (quoting *MCI Worldcom Commc'ns, Inc. v. Soc. Sec. Admin.*, GSBGA No. 16169-SSA, 04-2 BCA ¶ 32,689 (Aug. 4, 2004)).⁴ Accordingly, the Court held that there was an applicable dispute between USBR and PCL regarding the invoiced work and denied the claim for PPA interest on this ground as well.

Although COFC's description of the "dispute" exception is slightly broader than the rule adopted by the CBCA, it must be read in terms of the PPA's language which limits the exception to questions related to the performance of the underlying contract. 31 U.S.C. § 3907(c); see also H.R. Rep. No. 100-784, at 11, as reprinted in 1988 U.S.C.C.A.N. 3036, 3039 ("The Act's protections apply only when there is no dispute relating to a contractor's performance in accordance with the terms and conditions of the contract."). Taken together, these two decisions draw a consistent and principled distinction between withholdings authorized by a statute, regulation, or contract clause (which do not accrue PPA interest) and improper withholdings (for which interest accrues). In *Delta Air Lines*, GSA conceded that Delta provided the services for which it sought payment. The only qualifying disputes involved questions about whether the Department of Defense had paid for unused airline tickets. Therefore, the exception did not apply to GSA's withholding. The opposite was true in *PCL Construction Services*. The dispute in that case was based entirely on the parties' differing interpretations of the contractor's performance of the underlying contract. As a result, the USBR was not obligated to provide PPA interest.

Conclusion. The PPA requires the payment of interest penalties to provide an incentive for the government to make timely payments and to compensate contractors for the lost time value of money. When the government improperly withholds or delays a contract payment, the contractor is injured regardless of whether the agency acted in a good faith. Accordingly, the PPA does not make distinctions based on the government's subjective belief. The entitlement to interest is based on clear, objective standards. It automatically begins to accrue once the required payment date passes, unless (i) the contractor's invoice is defective; (ii) a statute, regulation, or contract clause authorizes a withholding and the procedural requisites are observed; or (iii) the amount due under the particular contract being invoiced is disputed.

David W. Burgett is a partner and Edward C. Eich is an associate in the Government Contracts and Grants Group of Hogan & Hartson LLP, Washington, D.C.

⁴ While the decision does not state that USBR paid PCL a portion of its March and April 1995 invoices, the COFC's extensive reliance on the *MCI Worldcom Commc'ns, Inc.* suggests that this was the case.