

Government Contracts Blog

Posted at 10:19 AM on May 29, 2009 by Sheppard Mullin

"There You Go Again" - Does the Fourth Estate Even Try to Get it Right When it Comes to Government Contracts?

The influential inside-the-Beltway newspaper and website *Politico* "reports" in its May 26th edition that, as the Administration is "following through" on its campaign pledge to cut wasteful Pentagon spending, it is finding that "the price is high." *Politico*, May 26, 2009 at 14. Well, OK, as a well worn bumper sticker says "Choices have consequences," and the choice to cancel a contract is no exception to that rule. But the story's headline and subheadline presage *Politico*'s insidious and inaccurate message:

Pentagon Shells Out for Work Undone

Despite spending cuts contractors get 'termination' pay

The story gets directly to its purported point in its second paragraph, with the following comment --

"After putting numerous programs on the chopping block, the government is going through the painful process of paying contractors for the work it won't get---what the Pentagon calls "termination costs."

Let's focus on the key phrases that drive this comment – “the painful process” and “paying ... for the work it won't get.” These are loaded words, designed to malign the contractors and suggest unquenchable rapaciousness against the public fisc, and they are dead wrong:

(1) The pain inflicted here rests most heavily on the contractor, unilaterally deprived of a business arrangement by a Government that has, in effect, adopted the attitude of Emil Litella, as immortalized by Gilda Radner on *Saturday Night Live* so many years ago – “Never mind.” Contractors live with the constant reality that agreements negotiated in good faith and priced on assumptions given to them by Uncle Sam will be abrogated by their Government for its “convenience.” Yes, that is what the contracts say – termination “for the convenience of the Government.” It is an awesome power and one that finds few if any analogues in commercial practice, where failure to perform equals “breach” and “breach damages” are the norm. So, our Government has

reserved for itself the choice to live up to its obligations by performing, or not. But that choice has consequences.

(2) The consequences are – as anyone who has expended the energy to understand the process knows full well – “termination costs.” If *Politico* had actually looked, it would easily have discovered that these costs are not for work the Government “won’t get.” To the contrary, the only reason that the Government has the right to terminate contracts for its own convenience is because, in exchange for that right, it has given contractors the right to be compensated, not for the work the Government “won’t get,” but rather for the work the Government *did* get, *i.e.*, the costs expended and incurred up to the point of termination while performing a contract that could be ended by Uncle Sam in a “New York minute.” *Politico* seems to not understand that without this agreement to pay terminations costs, it is the Government that gets “something for nothing,” that it can induce contractors to incur huge costs and liabilities to meet the contract’s requirements only to be given the proverbial “kiss on the cheek” that precedes abandonment. In the law, we call it “consideration,” and “consideration” is a good thing. It puts some measure of reliability into the contracting process.

For *Politico*’s edification, and for the benefit of those inflamed by its misleading rhetoric, let’s indulge in some reality:

- (1) The Government never, ever pays for work it "won't get." It reimburses contractors only for costs they have incurred, *i.e.*, costs the contractors have already paid or that they are already obligated to pay (like payments to employees and to subcontractors providing the titanium for those lightweight aircraft). The Government *may* also "pay" the contractor a reasonable profit on those incurred costs, but the contractor won't get its anticipated profit or, for that matter, any profit on a fixed price contract if the Government's auditors determine that the contractor would have lost money had the contract been fully performed.
- (2) Contractors don't get "termination pay" and Politico can search the regulations and court decisions in vain to support its assertions to the contrary. Yes, contractors do get reimbursed for some costs they would never had incurred had the contract not been terminated by the Government– like legal, administrative, accounting costs incurred to settle up with vendors and to prepare the termination proposal required by the regulations. But those are a clear consequence of Uncle Sam’s election to abandon the contract and why should the contractor have to pony up for those consequences? And, oh by the way, *Politico*, an entire army of regulators drafted and promulgated the regulations that give the contractor the right to those costs.

- (3) Contractors are almost never paid the fixed and semi-fixed costs of performance that cannot be turned off like a spigot when Uncle Sam deems it “convenient” to walk away from the deal – the *pro rata* share of plant, facilities, equipment and the like that were built into the price of the now defunct contract, the balance of which the Government will not be paying. But those costs do not go away. They often end up as a charge against profit, which is another term for “red ink.”
- (4) Defense contractor termination settlement proposals will always be audited by DCAA , an agency which has never heard of "termination pay" and is by statute required to prevent the Government from "shelling out" for "work undone." No one has ever accused DCAA of being a contractor’s best friend, benefactor or “Sugar Daddy.”
- (5) Termination proceedings often take years to be resolved. If that is a case of the Government "shelling out" money, well, that nut obviously had an awfully hard shell to crack.

These are not opinions, they are not musings, and they are not agenda driven. What they are, actually, is the law. Law is a good thing. It organizes society and provides predictable outcomes for choices that people and companies make. So, what *Politico* laments, at bottom, is the law. Change it if you like but, in the meantime, let people who relied on the law enjoy the protections to which that law legitimately entitles them.

* * * * *

Government contractors make appealing targets for journalists and politicians, and there can be little doubt that some contractors can be their own worst enemies in this regard. But when the Press adopts the blood lust of the wolf pack and resorts to yellow dog journalism, it demeans itself as well as its victims. *Politico*’s readers deserve better, and so do the men, women and companies that supported and contributed so mightily to the winning of the Cold War. *Politico* might do well to appreciate that it is those sorts of efforts that serve to preserve, day-by-day, *Politico*’s freedom to ignore the truth.

Authored by:

[John W. Chierichella](#)

(202) 218-6878

jchierichella@sheppardmullin.com

and

[W. Bruce Shirk](#)

(202) 741-8426

bshirk@sheppardmullin.com