



Government Contracts Advisory

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Raymond E. Maybus, Secretary of the Navy v. General Dynamics C4 Systems Inc.

On February 4, 2011, the United States Court of Appeals for the Federal Circuit (the “Federal Circuit”) issued ***Raymond E. Maybus, Secretary of the Navy v. General Dynamics C4 Systems Inc., No. 2009-1550, -1560 (Fed. Cir. Feb. 4, 2011)***, extending the equitable estoppel doctrine to indefinite delivery/indefinite quantity (“IDIQ”) contracts and affirming the *Aukerman* test as the standard for equitable estoppel. Reversing an earlier decision by the Armed Services Board of Contract Appeals (the “ASBCA”), the Federal Circuit held that General Dynamics was estopped from refusing to fill emailed Delivery Orders (“DOs”) under a contract with the Navy, a method prohibited by the contract terms, because General Dynamics had accepted and filled prior DOs by email.

Factual Background of the Case

In September 2001, General Dynamics assumed an IDIQ contract with the Navy for the development and delivery of digital modular radios. The contractor quickly became unsatisfied with the price terms it inherited, and hoped to avoid filling orders with the unfavorable prices. In reviewing the contract, General Dynamics noticed that the contract’s ordering clause prohibited the government from issuing a DO via email, unless authorized by the contract’s schedule. The contract stated:

If mailed, a delivery order or task order is considered “issued” when the Government deposits the order in the mail. Orders may be issued orally, by facsimile, or by electronic commerce methods only if authorized in the schedule.

Id. at 3. There was no schedule permitting the issuance of DOs via email.

General Dynamics took action upon receiving 10 DOs from the Navy via email within one day of the expiration of the option period. Although the Navy had issued prior DOs via email and General Dynamics had delivered the radios based upon the same, General Dynamics decided to reject these 10 DOs placed by email. General Dynamics argued that these orders did not comply with the contract’s ordering clause which required DOs to be issued in writing via mail. General Dynamics also argued that its prior acceptance of emailed DOs followed negotiations between the parties, but the 10 DOs it rejected did not follow such negotiations. Despite General Dynamic’s rejection of these DOs, the Navy demanded delivery. General Dynamics viewed this demand for delivery by the Navy as direction to proceed under the contract’s Changes Clause, which required the contractor to continue its work despite the dispute.

Upon filing these orders, General Dynamics filed a claim with the Contracting Officer that was denied. General Dynamics appealed to the ASBCA. The government argued that General Dynamics should be estopped from making its claim because General Dynamics had previously filled DOs issued by email. The Board stated that, in accordance with established precedent, DOs not issued in accordance with contract terms are like invalid option exercises. In addition, the ASBCA decision noted that the Navy had not directed the Board's attention to any case in which waiver or estoppel had been applied in the event of improper option exercise or improper issuance of a DO under an IDIQ contract that the contractor protested prior to performance. Without deciding whether estoppel could ever apply under those circumstances, the Board found that the Navy failed to meet its burden of proof. Applying a four-part test for estoppel, the ASBCA ruled that no estoppel was established and, therefore, that the DOs were invalid because they did not comply with the strict terms of the contract.

The Navy appealed the estoppel ruling to the Federal Circuit. The Federal Circuit reversed, holding that General Dynamics was equitably estopped from refusing to fill the 10 emailed DOs.

Extension of the Equitable Estoppel Doctrine to IDIQ Contracts

On appeal, the Federal Circuit held that "the doctrine of equitable estoppel may apply to an IDIQ contract," noting that while the issuance of a DO in an IDIQ contract may be equivalent to exercising an option, that "does not preclude the application of this equitable doctrine." *Id.* at 14. With this holding, it is now clear that the doctrine of equitable estoppel applies to IDIQ contracts. However, the court left open the possibility that the equitable estoppel doctrine may also be applied to the exercise of options.

Federal Circuit Affirms the use of *Aukerman* Test for Equitable Estoppel Cases

The ASBCA used a four-part equitable estoppel test derived from *Rel-Reeves, Inc. v. United States*, 534 F.2d 274 (Ct.Cl. 1976). The Federal Circuit analyzed equitable estoppel under a different three-part standard derived from *A.C. Aukerman Co. v. R.L. Chaides Constr. Co.*, 960 F.2d 1020 (Fed. Cir. 1992), a patent infringement case between two private parties. Finding equitable estoppel under *Aukerman* requires (1) misleading conduct, (2) reliance on the misleading conduct, and (3) material prejudice due to this reliance. Although the tests cited by the ASBCA and Federal Circuit are articulated differently, both require essentially the same elements – misleading conduct and detrimental reliance. The Federal Circuit's holding in this case confirms that the *Aukerman* test is the correct standard to apply for equitable estoppel cases involving government contracts.

Based on the facts, the Federal Circuit concluded that the government had met its burden of proving that General Dynamics should be equitably estopped in this case – General Dynamics' conduct had misled the government into believing that emailed DOs would be accepted, and that the government relied on that misleading behavior to its detriment.

Conclusion

With this decision, the Federal Circuit has extended the equitable estoppel doctrine to IDIQ contracts and affirmed the *Aukerman* test as the appropriate standard for proving equitable estoppel in government contracts. Whether the equitable estoppel doctrine can also be applied in the context of an option exercise is a question left

unresolved by the Federal Circuit. However, contractors should expect to see greater reliance by the government on estoppel as a basis for avoiding the consequences of the government's failure to comply with contract terms, including provisions regarding options.

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