Who's on First—Do Contracting Officers Decide the Merits of Employment Discrimination Cases Filed Against Government Contractors After *Boeing v. Roche*?[1]

Major Gregory R. Bockin
Trial Attorney, Contract Appeals Division
United States Army Legal Services Agency

> ***Costello:*** *Have you got a contract with the first baseman?*
> ***Abbott:*** *Absolutely.*
> ***Costello:*** *Who signs the contract?*
> ***Abbott:*** *Well, Naturally!*
> ***Costello:*** *When you pay the first baseman every month, who gets the money?*
> ***Abbott:*** *Every dollar. Why not? The man's entitled to it.*[2]

Imagine that you are in your office, when a contracting officer (CO) contacts you with a sexual harassment question. You remind the CO that you are a contracts attorney and offer to refer her to the labor counselor. She laughs, but insists that this is a contracts matter and begins telling you about a sexual harassment lawsuit against a government contractor. The CO tells you that on 18 November 1999, the Directorate of Contracting, Fort Bragg, North Carolina awarded Contract ABC123-45-99-C-0001 to *XYZ, Inc*.[3] (*XYZ*), a government and commercial contractor. Fort Bragg awarded *XYZ* a cost plus fixed-fee contract for labor, management, supervision, supplies, materials, equipment, tools, services supporting family housing maintenance and repair activities, and occupant self-help activities at Fort Bragg.[4]

The CO tells you that an *XYZ* employee, *Ms. B*, filed a lawsuit against *XYZ* alleging that she was fired as a reprisal for her complaints of sexual harassment.[5] That is all that the CO can tell you, because *Ms. B* has since settled the suit, and is now bound by the settlement's confidentiality agreement.[6] *XYZ* is requesting money for legal fees, and the CO wants to know if she should pay them.

This article provides an overview of the law regarding the cost allocability and allowability of a contractor's legal fees in the defense of civil suits filed by a contractor's employees. First, this article discusses the history of how the courts have dealt with the allocability and allowability of third-party legal fees. Second, it discusses the state of the law following the Court of Appeals for the Federal Circuit's (CAFC) 29 July 2002 decision in *Boeing North American, Inc. v. Roche* (*Boeing II*).[7] The discussion includes an application of the CAFC's *Boeing II* decision to a hypothetical set of facts. This analysis explains the issues, exposes the inherent weaknesses in the current standard, and reviews the CAFC's new "similarity test."[8] Third, this article explores the aftermath of unresolved contract issues regarding the scope of *Boeing II*. Finally, it concludes that the current standard creates a difficult situation that forces procurement professionals to evaluate the merits of complex civil actions, for which they have little training or experience.

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1. Boeing N. Am., Inc. v. Roche, 298 F.3d 1274 (Fed. Cir. 2002) [hereinafter Boeing II].

2. *The Colgate Comedy Hour* (NBC television broadcast, Jan. 7, 1951).

3. *XYZ* is a fictional company; however, some of the facts in this hypothetical scenario are loosely based upon the facts from the government's brief in a pending case. *See* Motion for a Board Order to Compel, Tecom, Inc., ASBCA No. 53884, (Oct. 7, 2002) (on file with author). The author wishes to express his appreciation to Craig Clarke, Esq., Supervisory Trial Attorney, and CPT Jennifer Zucker, Trial Attorney, both from the U.S. Army's Contract Appeals Division, for their assistance. Captain Zucker and Mr. Clarke are also government counsel for Tecom, Inc.

4. *See* Motion for a Board Order to Compel, Tecom, Inc., at 3.

5. *See id.*

6. *See id.*; U.S. Dep't of Agriculture, *What is a Confidentiality Agreement?*, *at* http://www.saa.ars.usda.gov/ott/whatisca.htm (last visited Sept. 30, 2003). A confidentiality agreement is an agreement not to disclose certain information to a third party. Generally, such agreements provide that in exchange for the consideration provided for within the settlement agreement, the parties agree not to disclose any of the terms of the settlement agreement. The agreement in the fictional scenario above includes a confidentiality provision which may hold *Ms. B* liable to pay *XYZ* $10,000 if she breached it. The agreement also contained a general "Breach of Agreement" provision that stated, "*B* further agrees that if she breaches this Agreement in any respect she will forfeit all monies due her under this Agreement." *See* Motion for a Board Order to Compel, Tecom, Inc., at 3-4.

7. *Boeing II*, 298 F.3d 1274 (Fed. Cir. 2002) (vacating an earlier CAFC decision in Boeing N. Am., Inc. v. Roche, 283 F.3d 1320 (Fed. Cir. 2002) [hereinafter Boeing I]).

8. *Boeing II*, 298 F.3d. at 1285.

The History of Cost Allocability and Allowability of Costs

One commentator has suggested that "unraveling the Federal Circuit's benefit concept begins by distinguishing allocability from allowability."[9] In the past, the concepts have been confusingly interchanged.[10] Under Federal Acquisition Regulation (FAR) section 31.201-1(b),[11] the total cost of performing a contract includes all costs that are properly allocable to the contract.[12] Section 31.201-4 of the FAR further defines which costs are allocable.[13] In general, allocability refers to whether a cost can be charged to a particular contract, and allowability refers to whether a cost can be charged to a government contract. The government, however, does not pay a contractor the total allocable cost of contract performance. Rather, the government pays the contractor only allowable costs, which are a portion of the costs actually allocable to the contract.[14] The FAR specifies five factors to determine whether costs are allowable.[15]

The confusion between allocability and allowability began with *Lockheed Aircraft Corp. v. United States*.[16] In *Lockheed*, the court held that "the criterion . . . for allocating indirect costs is 'benefit.'"[17] The court described the "benefit" requirement for indirect costs as the following:

> No one would quarrel with the general proposition that it is fair to allocate to government contracts the costs of services which facilitate performance of the particular contracts or are essential to the existence and continuance of the business entity. But the burden shall be on the contractor to show the benefit and a reasonable allocation among different government contracts and between government and commercial work generally.[18]

The "benefit theory" announced in *Lockheed* continued to develop in *Caldera v. Northrop Worldwide Aircraft Services, Inc.*[19] In *Northrop*, the contractor incurred legal fees in an Oklahoma state court during the unsuccessful defense of a wrongful employment termination claim by former employees. The employees claimed they were terminated because they refused to follow the contractor's "directions and participate in fraud against the Army in connection with the contract."[20] The jury agreed. Citing the language of FAR section 31.201-4, the

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9. John D. Inazu, Boeing v. Roche *and the Benefit Theory of Allocability: Unlocking Lockheed or Ignoring Northrop?*, 32 PUB. CONT. L.J. 39, 41 (2002).

10. Ralph C. Nash & John Cibinic, *Postscript: Allocability and Allowability of Costs*, 16 NASH & CIBINIC REP. 9, ¶ 45 (2002).

11. GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 31.201-1(b) (July 2002) [hereinafter FAR].

12. Inazu, *supra* note 9, at 41. The FAR provides that "[w]hile the total cost of a contract includes all costs properly allocable to the contract, the allowable costs to the Government are limited to those allocable costs which are allowable pursuant to part 31 and applicable agency supplements." FAR, *supra* note 11, at 31.201(b).

13. *Id.* at 31.201-4. The following costs are allocable under the FAR:

> A cost is allocable if it is assignable or chargeable to one or more cost objectives on the basis of relative benefits received or other equitable relationship. Subject to the foregoing, a cost is allocable to a Government contract if it—
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> (a) Is incurred specifically for the contract;
> (b) *Benefits both the contract and other work*, and can be distributed to them in reasonable proportion to the *benefits* received; *or*
> (c) *Is necessary to the overall operation of the business*, although a direct relationship to any particular cost objective cannot be shown.

Id. (emphasis added).

14. *See supra* note 12.

15. The FAR determines whether a cost is allowable by considering the following factors:

> (1) Reasonableness.
> (2) Allocability.
> (3) Standards promulgated by the Cost Accounting Standards Board, if appropriate; otherwise, generally accepted accounting principles and practices appropriate to the particular circumstances.
> (4) Terms of the contract.
> (5) Any limitations set forth in this subpart.

FAR, *supra* note 11, at 31-201-2.

16. 375 F.2d 786 (Ct. Cl. 1967).

17. Inazu, *supra* note 9, at 44 (citing *Lockheed*, 375 F.2d at 793).

18. *Id*. (citing *Lockheed*, 375 F.2d at 794).

19. 192 F.3d 962 (Fed. Cir. 1999).

court held that the attorneys' fees were not allocable to the contract because they did not "benefit" the government as follows:

> It is established that the contractor must show a benefit to government work from an expenditure of a cost that it claims is "necessary to the overall operation of the [contractor's] business." . . . We can discern no benefit to the government in a contractor's defense of a wrongful termination lawsuit in which the contractor is found to have retaliated against the employees for the employees' refusal to defraud the government.[21]

This background helps put the *Boeing II* decision into context—the "benefit theory" was the state of the law regarding cost analysis until March 2002.[22]

In *Boeing II*, the CAFC addressed the issue of the allowability of legal fees that a government contractor incurred while defending a shareholder derivative suit.[23] *Boeing II* rejected the government's reliance on the "benefit theory."[24] The case revolves around Rockwell International Corp. (Rockwell), a predecessor of Boeing North American, Inc., who was a large defense contractor. In June 1989, four Rockwell shareholders, with Citron as the plaintiff's representative, filed a shareholder's derivative complaint in Los Angeles County Superior Court.[25] The suit alleged that:

> "John Does" who were "officers, directors and other members of management and employees, who [sic] were involved in the wrongdoing complained of." The gravamen of the complaint was that the "defendants knowingly, recklessly, or culpably breached their fiduciary duties to the corporation by . . . failing to establish internal controls sufficient to insure that the corporation's business was carried on in a lawful manner . . . ."[26]

The complaint alleged that "the named defendants were 'controlling persons of Rockwell and had the power and influence, and exercised the same, to cause Rockwell to engage in the illegal practices complained of' and that the unidentified defendants aided, abetted, and participated in the wrongful acts and conduct."[27] In a joint statement of facts, "the parties stipulated that the Citron 'complaint did not directly allege that the director-defendants participated in, or had prior knowledge of, any of the . . . instances of wrongdoing' described in the complaint."[28]

During 1989 through 1991, "Rockwell incurred approximately $4,576,000 of legal fees and costs associated with the Citron action, including costs incurred for representing Rockwell, for representing the director defendants, for legal counsel to the SLC [special litigation committee], and for reimbursement of the plaintiff's legal fees and costs."[29] The company "included these costs as general and administrative ('G&A')[30] costs in its home office overhead for fiscal years 1989, 1990, and 1991, and it claimed reimbursement for a portion of the [Citron] costs under its various contracts with the government."[31]

The CO excluded the legal costs under "FAR [section] 31.204(c), which provides that [the] allowability of costs not specifically addressed by the FAR is to be based on the principles of the FAR and the 'treatment of similar or related . . . items [that are specifically addressed under the FAR].'"[32] The CO determined that Rockwell's legal fees were "'similar or related'[33] to the costs incurred in connection with or related to mischarging of costs on government contracts, which are expressly unallowable under FAR [section] 31.205-15,[34] and

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20. *Id.* at 965.

21. *Id*. at 972.

22. *Id*. *Boeing I* vacated a decision of the Armed Services Board of Contract Appeals disallowing legal costs on 15 March 2002. Boeing I, 283 F.3d 1320 (Fed. Cir. 2002); *see* Boeing N. Am., Inc., ABSCA No. 49994, 00-2 BCA ¶ 30,970.

23. *Boeing II*, 298 F.3d 1274 (Fed. Cir. 2002).

24. *Id*. at 1284.

25. *Id.* at 1276 (citing Citron v. Beall, No. C728809 (Cal. Super. Ct. June 26, 1989)).

26. *Id.*

27. *Id*. at 1277 n.2.

28. *Id*. The parties to *Citron* agreed that the following five instances of underlying misconduct formed the basis of the shareholder's suit: (1) the government alleged that Rockwell fraudulently mischarged the government for work performed on a contract in 1975-1977; (2) the government brought criminal charges against Rockwell for making false statements in connection with work performed under a government contract in 1982; (3) the government alleged that Rockwell had engaged in defective pricing related to a 1982-83 subcontract; (4) a *qui tam* lawsuit alleged that Rockwell permitted employees to use government assets for personal gain; and (5) the Department of Justice alleged that Rockwell engaged in hazardous waste dumping and other environmental law violations between 1975 and 1989. *Id*.

29. *Id*. at 1278.

'similar or related'[35] to costs for the unsuccessful defense of fraud charges, which are expressly unallowable under FAR [section] 31.205-47."[36] While the litigation was still ongoing, "in December 1996, [Rockwell] merged with a wholly owned subsidiary of the Boeing Company and changed its name to Boeing North American, Inc."[37] Boeing appealed the CO's decision to the Armed Services Board of Contract Appeals (ASBCA).[38] Boeing argued that the legal costs were allowable because "the costs were ordinary, necessary, and allowable 'professional services' costs under the FAR [section] 31.205-33(b)."[39] They also argued that "the costs were reasonable in relation to the services rendered, pursuant to FAR [sections] 31.201-3[40] and 31.205-33(b)."[41] Finally, Boeing stated that "the costs were allocable to the contract because they conferred

30. The Cost Accounting Standards define General and Administrative (G&A) expenses as follows:

> [A]ny management, financial, and other expense which is incurred by or allocated to a business unit and which is for the general management and administration of the business unit as a whole. G&A expense does not include those management expenses whose beneficial or causal relationship to cost objectives can be more directly measured by a base other than a cost input base representing the total activity of a business unit during a cost accounting period.

CCH GOVERNMENT CONTRACTS REPORTER, COST ACCOUNTING STANDARDS BOARD REGULATIONS pt. 9904.410-30(6) (1 July 2002) [hereinafter COST ACCOUNTING STANDARDS BOARD REGULATIONS].

31. *Boeing II*, 298 F.3d at 1278.

32. *Id*. at 1279. The FAR section regarding application of principles and procedures provides that:

> Section 31.205 does not cover every element of cost. Failure to include any item of cost does not imply that it is either allowable or unallowable. *The determination of allowability shall be based on principles and standards in this subpart and the treatment of similar or related selected items*.

FAR, *supra* note 11, at 31.204 (emphasis added).

33. *Id*.

34. The FAR section regarding fines, penalties, and mischarging costs provides:

> (a) Costs of fines and penalties resulting from violations of, or failure of the contractor to comply with, Federal, State, Local, or foreign laws and regulations, are unallowable except when incurred as a result of compliance with specific terms and conditions of the contract or written instructions with the CO.
>
> (b) Costs incurred in connection with, or related to, the mischarging of costs on Government contracts are unallowable when the costs are caused by, or result from, alteration or destruction of records, or other false or improper charging or recording of costs. Such costs include those incurred to measure or otherwise determine the magnitude of improper charging, and costs incurred to remedy or correct the mischarging, such as costs to rescreen and reconstruct records.

Id. at 31.205-15.

35. *Boeing II*, 298 F.3d at 1279.

36. *Id*. The FAR section regarding costs related to legal and other proceedings provides that costs

> incurred in connection with any proceeding brought by a Federal, State, local or foreign government for a violation of, or a failure to comply with, law or regulation by the contractor (including its agents or employees), or costs incurred in connection with any proceeding brought by a third party in the name of the United States under the False Claims Act, 31 U.S.C. 3730, are unallowable if the result is—
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> (1) In a criminal proceeding, a conviction;
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> (2) In a civil or administrative proceeding, either a finding of contractor liability where the proceeding involves an allegation of fraud or similar misconduct or imposition of a monetary penalty where the proceeding does not involve an allegation of fraud or similar misconduct;
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> (3) A final decision by an appropriate official of an executive agency to—
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> (i) Debar or suspend the contractor;
> (ii) Rescind or void a contract; or
> (iii) Terminate a contract for default by reason of a violation or failure to comply with a law or regulation.

FAR, *supra* note 11, at 31.205-47(b).

37. *Boeing II*, 298 F.3d at 1276.

38. Boeing N. Am., Inc. ASBCA No. 49994, 00-2 BCA ¶ 30,970.

a benefit to the contract, in accordance with FAR [section] 31.204;[42] and the costs were not limited or disallowed by any FAR cost principles."[43] While that appeal was pending, the CAFC decided *Northrop*.[44]

The ASBCA denied Boeing's appeal because there could be "no benefit to the Government in a contractor's defense of a third party lawsuit in which the contractor's prior violations of federal laws and regulations were an integral element of the third party's allegations."[45] The ASBCA "reasoned that 'but for' Rockwell's wrongdoing[,] the Citron suit would not have been brought, and the costs would not have been incurred."[46]

On 29 July 2002, the CAFC, acting en banc, issued the *Boeing II* decision.[47] The case established two new and important legal standards for allocability and allowability of costs under government cost-reimbursement contracts. With respect to allocability, the CAFC deviated from its earlier decisions, which provided that costs were allocable only if there was some "benefit to the government" for incurring the cost, and that the contractor had to show a benefit to government work from an expenditure of a cost that it claims is necessary to the overall operation of the contractor's business.[48]

In *Boeing II*, the CAFC held that the proper test for determining the allocability is the cost accounting standards (CAS)[49]

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39. The FAR section regarding professional and consultant cost services provides that the "costs of professional and consultant services are allowable subject to this paragraph and paragraphs (c) through (f) of this subsection when reasonable in relation to the services rendered and when not contingent upon recovery of the costs from the Government (but see 31.205-30 and 31.205-47)." FAR, *supra* note 11, at 31.205-33.

40. The FAR section regarding reasonableness determinations provides:

> (a) A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person in the conduct of competitive business. Reasonable specific costs must be examined with particular care in connection with firms or their separate divisions that may not be subject to effective competitive restraints. No presumption of reasonableness shall be attached to the incurrence of costs by a contractor. If an initial review of the facts results in a challenge of a specific cost by the CO or the CO's representative, the burden of proof shall be upon the contractor to establish that such cost is reasonable.
>
> (b) What is reasonable depends upon a variety of considerations and circumstances, including—
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> (1) Whether it is the type of cost generally recognized as ordinary and necessary for the conduct of the contractor's business or the contract performance;
> (2) Generally accepted sound business practices, arm's length bargaining, and Federal and State laws and regulations;
> (3) The contractor's responsibilities to the Government, other customers, the owners of the business, employees, and the public at large; and—
> (4) Any significant deviations from the contractor's established practices.

Id. at 31.201-3.

41. FAR, *supra* note 11, at 31.205-33.

42. The FAR section regarding the application of principles and procedures provides:

> *Costs shall be allowed to the extent they are reasonable, allocable, and determined to be allowable under 31.201, 31.202, 31.203, and 31.205.* These criteria apply to all of the selected items that follow, even if particular guidance is provided for certain items for emphasis or clarity.

Id. at 31.204 (emphasis added).

43. *Boeing*, ASBCA No. 49994, BCA ¶ 30,970.

44. Caldera v. Northrop Worldwide Aircraft Servs., Inc., 192 F.3d 962 (Fed. Cir. 1999).

45. Boeing, ASBCA No. 49994, BCA ¶ 30,970, at 24.

46. Boeing II, 298 F. 3d 1274, 1274 (Fed. Cir. 2002) (citing *Boeing*, ASBCA No. 49994, BCA ¶ 30,970, at 22-24).

47. *Boeing II*, 298 F. 3d 1274.

48. *See, e.g.*, FMC v. United States, 853 F.2d 882, 885 (Fed. Cir. 1988); Lockheed Aircraft Corp. v. United States, 375 F.2d 786 (Ct. Cl. 1967).

49. Cost Accounting Standards Board Regulations, *supra* note 30, ¶ 9904.410. The Cost Accounting Standards section regarding allocation of business unit general and administrative expenses to final cost objectives provides the following:

> The purpose of this Cost Accounting Standard is to provide criteria for the allocation of business unit general and administrative (G&A) expenses to business unit final cost objectives based on their beneficial or causal relationship. These expenses represent the cost of the management and administration of the business unit as a whole.

Id.

"nexus" test: "whether sufficient 'nexus' exists between the costs and the government contract."[50] The CAFC decided that the proper test for allowability is determining whether the legal costs sought by the contractor for third party civil suits were "similar or related" to costs allowable under the regulations.[51] *Boeing II* "recognized that it was bound by its *Northrop* decision, but concluded that the decision should have been based on allowability, not allocability."[52] Therefore, the CAFC distinguished between the concepts of cost allocability and cost allowability under the FAR, holding that the issue of legal costs in this case is one of allowability.[53]

The Similarity Test Under FAR Section 31.204(C)—Similar or Related

After deciding that the issue was one of allowability, *Boeing II* focused on FAR sections 31.204 and 31.205.[54] The CAFC began by disavowing Boeing's argument "that the only professional service costs that are not allowable under FAR [section] 31.205-33 are those costs that are specifically disallowed under another FAR provision."[55] The court reiterated that FAR section 31.201-2 explains the factors to consider in determining whether a cost is allowable, in conjunction with FAR section 31.204 (c), which "explains how to apply the principles and procedures, and FAR [section] 31.205 [which] contains over fifty subsections, each of which covers, in detail, the allowability of particular selected costs."[56]

In *Boeing II*, the court held that "[a]lthough the FAR [section] 31.205 subsections covering selected costs are extensive, FAR [section] 31.204 makes clear that 'section 31.205 does not cover every element of cost. Failure to include any item of cost does not imply that it is either allowable or unallowable.'"[57] When a cost is not specifically covered under FAR section 31.205, the CAFC noted, "FAR [section] 31.204(c) instructs us: 'The determination of allowability shall be based on the principles and standards in this subpart and the treatment of similar or related selected items.'"[58]

The CAFC applied the "similar or related"[59] standard of FAR section 31.204 to the facts in *Northrop*. They concluded that Northrop's attorneys' fees were "similar"[60] to costs that FAR section 31.205-47 made specifically unallowable, but that consideration of the term "related"[61] was required in *Boeing II* as follows:

> Properly understood, *Northrop* and FAR [section] 31.205-47 taken together establish a simple principle—that the costs of unsuccessfully defending a private suit charging contractor wrongdoing are not allowable if the "similar" costs would be disallowed under the regulations. The present case is, however, distinguishable from the situation involved in *Northrop*. Here the costs of defending the *Citron* lawsuit would not be, as in *Northrop*, "similar" to disallowed costs. The regulations disallowing particular items of cost do not address costs similar to the costs of defending a contractor's directors from charges that they tolerated inadequate controls concerning possible fraud or similar misconduct. However, we must also consider whether those costs are "related" to a category of disallowed costs, that is, costs of defending against government charges of contractor wrongdoing.[62]

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50. *Boeing II*, 298 F.3d at 1281.

51. *Id*. at 1286.

52. Brief for Respondent, Tecom, Inc., at 7, ASBCA No. 53884 (Oct. 7, 2002); *see Boeing II*, 298 F.3d at 1281.

53. *Boeing II*, 298 F.3d at 1280.

54. *Id*. at 1285.

55. *Id*.

56. *Id*.

57. *Id*. (citing FAR, *supra* note 11, at 31.204).

58. *Id*. (citing FAR, *supra* note 11, at 31.204(c)).

59. *Id*. at 1286.

60. *Id*.

61. *Id*.

62. *Id*. at 1286-87.

The CAFC admitted that it had not previously interpreted FAR section 31.204(c), but that the ASBCA had previously applied this regulation on several occasions.[63] In *Boeing II*, the CAFC noted that the ASBCA has previously found "similar or related" costs in several cases.[64] For example, fees for "the issuance of state tax-exempt bonds were unallowable because they were 'similar or related' to 'interest on borrowed capital.'"[65] However, "launching and roll out costs for a new aircraft were allowable because they were similar to advertising and sales promotion costs."[66] The ASBCA had previously decided that "[d]ividends paid to a contractor's employees on restricted stock were allowable because they were 'similar or related to' allowable cash compensation or stock bonuses."[67] Stock appreciation rights "were allowable because they were 'similar or related to' allowable cash or stock bonuses."[68]

The CAFC then interpreted the term "related," concluding that "related" did not mean "but for."[69] It stated, "[W]e think it unlikely that the related test under FAR [section] 31.204(c) was designed to make a particular cost item unallowable simply because it would not have occurred but for the occurrence of an event that resulted in a disallowed cost."[70] Rather, the court decided that "[i]n order for a particular cost to be 'related,' there must be a more direct relationship to the disallowed cost."[71] Applying this standard, the court held that the "required direct relationship, we think, would exist here if there were a judicial determination that the Rockwell directors had failed to maintain adequate controls to prevent the occurrence of the wrongdoing against the government."[72] However, in *Boeing II*, no judicial determination was made, because the *Citron* suit was settled. Therefore, the CAFC looked to "the regulations for guidance as to the treatment of settlements."[73]

The CAFC then reviewed the FAR[74] and determined that the regulations "reflect a policy judgment that [when] the action is brought by a federal or state government entity and the costs would be disallowed in an unsuccessful suit, the defense costs should also be disallowed in a settlement situation, see FAR [section] 31.205-47(b)(4)."[75] This does not apply if the "U.S. government specifically agrees that they will be allowable."[76] The CAFC concluded that this FAR provision represented a policy judgment "based on the assumption that suits brought by government entities in most situations are likely to be meritorious, thus justifying a bright line rule that does not look behind the settlement."[77]

The court refused to extend this same assumption to private suits, however. Rather, the court opined that:

> [W]here a private suit is involved[,] an inquiry is necessary to determine whether the plaintiff was likely to prevail . . . . This approach is most clearly reflected in the FAR regulations' treatment of settlements of private suits brought under the False Claims Act where the government does not intervene. FAR [section] 31.205-47(c)(2)."[78]

The CAFC explained that under this new standard, "costs may be allowable if the contracting officer determines that there was

63. *Id.* at 1285.

64. *Id*. at 1286.

65. *Id*. (citing Stanford Univ., ASBCA No. 28240, 85-3 BCA ¶ 18,446).

66. *Id*. (citing Gen. Dynamics Corp., ASBCA No. 31359, 92-1 BCA ¶ 24,698).

67. *Id*. (citing Grumman Aerospace Corp., ASBCA No. 34665, 90-1 BCA ¶ 22,417).

68. *Id*. (citing Boeing Co., ASBCA No. 24089, 81-1 BCA ¶ 14,864).

69. *Id.* at 1287.

70. *Id.*

71. *Id*.

72. *Id*.

73. *Id*. at 1287-88.

74. FAR, *supra* note 11, at 31.205-47(b)(4).

75. *Boeing II*, 298 F.3d at 1288.

76. *Id*. (citing, FAR, *supra* note 11, at 31.205-47(c)).

77. *Id*.

78. *Id*.

'very little likelihood that the third party [plaintiffs] would have been successful on the merits.'"[79] Applying this test to the facts in *Boeing II*, the CAFC held that for "the costs to be allowable in a settlement situation (where the costs of an unsuccessful defense would be disallowed), Boeing must show that the allegations in the Citron action had 'very little likelihood of success on the merits.'"[80]

John D. Inazu, an Associate General Counsel for the Department of the Air Force, has suggested that this new standard means that for legal fees to be allowable, the costs must be dissimilar to, but also unrelated to, costs disallowed under the FAR.[81] Focusing on the frivolous nature of some modern lawsuits, he argues that "while 'the costs of defending corporate directors against frivolous lawsuits are essential to any business operation,' if the lawsuits were not 'frivolous,' then the costs would not be 'related' to costs of defending against government charges of contractor wrongdoing."[82] Mr. Inazu concludes that the CAFC essentially "held that a proper determination of allowability depended on a showing by the contractor that the shareholder suits were frivolous."[83]

Applying the *Boeing II* Standard to the *XYZ* Scenario

To properly understand the current state of the law, it is helpful to apply this new CAFC standard to the hypothetical situation discussed earlier. These are the theoretical facts: [84] *XYZ* hired *Ms. B*. as a carpenter and she began working at a commercial construction project. At that job site, another carpenter, *Mr. T*, took an interest in *Ms. B* and asked her out for a date. At first, *Ms. B* made excuses why she could not go out with him. After he had asked her out for the second time, *Ms. B* told him that she was not interested. Following this incident, *Mr. T* began to make derisive comments to *Ms. B* at the job site in front of other workers. *Ms. B* said nothing at the time, having experienced the rough language of construction sites during her career.

A short time later, *XYZ* learned of the damage that Hurricane Oscar caused at Fort Bragg in April 2001. Hurricane Oscar destroyed the roofs on five barracks buildings on Fort Bragg. Under contract ABC123-45-99-C-0001, *XYZ* sent out crews to repair the barracks. *Ms. B* and *Mr. T* were part of the crews that *XYZ* sent to Fort Bragg. After several days, *Mr. T* again asked *Ms. B* for a date while only he and *Ms. B* were present; the foreman was working at another location on Fort Bragg. After work, *Ms. B* complained to the foreman about *Mr. T*'s comments and behavior. The foreman listened politely, but said nothing. A week later, the foreman told her that the work at Fort Bragg was almost complete, and he didn't have any large jobs lined up. He told *Ms. B* to finish out the day but that he would have to lay her off.

On 3 July 2001, *Ms. B* hired an employment law attorney, *Ms. W.* On behalf of *Ms. B*, *Ms. W* filed a claim on 10 July 2001 alleging unlawful workplace harassment due to unwelcome or unsolicited speech or conduct based upon sex.[85] On 13 October 2001, the State of North Carolina informed *Ms. W* that the agency finished processing *Ms. B*'s claim, and would soon issue a final decision. This news made *Ms. B* impatient and she fired *Ms. W.* On 18 November 2001, *Ms. B* hired another employment law attorney, *Mr. S.* On 20 November 2001, *Mr. S* filed a

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79. *Id*.

80. *Id*. at 1288-89 (quoting FAR, *supra* note 11, at 31.205).

81. Inazu, *supra* note 9, at 55 (citing *Boeing II*, 298 F.3d at 1286).

82. *Id*. (citing *Boeing II*, 298 F.3d at 1288).

83. *Id*.

84. The author has created these background facts to aid in the hypothetical. *See generally* Opinion and Order on Government's Motion to Compel, Tecom, Inc., ASBCA No. 53884, (Dec. 4, 2002) (on file with author) (denying government's motion to compel and holding that the court has "no jurisdiction to require the release of any confidentiality agreement").

85. *See* Motion for a Board Order to Compel, Tecom, Inc., at 3, ASBCA No. 53884 (Oct. 7, 2002). North Carolina state law provides:

> It is the public policy of this State to protect and safeguard the right and opportunity of all persons to seek, obtain and hold employment without discrimination or abridgement on account of race, religion, color, national origin, age, sex or handicap by employers which regularly employ 15 or more employees. It is recognized that the practice of denying employment opportunity and discriminating in the terms of employment foments domestic strife and unrest, deprives the State of the fullest utilization of its capacities for advancement and development, and substantially and adversely affects the interests of employees, employers, and the public in general.

N.C. GEN. STAT. § 143-422.2 (2002).

> The plain language of this statute provides no guidance concerning the requisite elements to establish a prima facie case of a claim under it and there is no basis in the decisional or statutory law of North Carolina for determining even such crucial matters as the burden of proof, which party is to bear that burden, whether there is a defense to a claim flowing from this section, or even whether damages may be compensatory only or punitive.

Newton v. Lat Purser & Assocs., 843 F. Supp. 1022 (W.D.N.C. 1994).

complaint with the Equal Employment Opportunity Commission (EEOC) alleging harassment in violation of Title VII of the Civil Rights Act of 1964, because they were still within the 300-day statute of limitations.[86]

XYZ's corporate counsel, *Ms. R.*, decided to settle the case. She knew that the contract incorporated by reference FAR section 52.222-26, Equal Opportunity. This section states that "[t]he Contractor shall not discriminate against any employee or applicant for employment because of race, color, religion, sex or national origin."[87] After reviewing all of the facts in this case, and considering the mounting legal fees that *XYZ* incurred defending the pending state claim, as well as the potential cost of the EEOC matter, *Ms. R* entered into settlement negotiations with *Mr. S*. The parties executed a settlement agreement on 19 February 2002. *XYZ* paid *Ms. B* $39,000 and $1000 for court costs. The settlement agreement addressed the state and federal claims, and contained a confidentiality agreement.[88]

Ms. R sent a letter to the CO, dated 25 February 2002, requesting payment in the amount of $140,000 for legal expenses and settlement costs relating to a layoff, which was alleged to be retaliation against an employee for filing a sexual harassment charge. The CO now comes to you and asks for help. You contact *Ms. B*, through her counsel, and inquire if she would discuss the sexual harassment allegations. *Ms. B* desperately wants to discuss them, but is concerned about the confidentiality provisions of her settlement agreement. On the advice of her attorney, *Ms. B* indicates that if *XYZ* waives the confidentiality and breach provisions of the settlement agreement, she would be willing to testify about her allegations of sexual harassment. *XYZ* declines to waive the confidentiality provision in the settlement agreement, and thus, the government cannot depose *Ms. B*.[89]

On 3 March 2002, the government advised *XYZ* that for the expenses to be allocable,[90] *XYZ* must demonstrate how the defense and settlement of a wrongful termination lawsuit, predicated on sexual harassment, benefited the government.[91]

On 6 March 2002, *Ms. M*, a government cost and price analyst, requested that the Defense Contract Audit Agency (DCAA) audit *XYZ*'s legal and settlement expenses in relation to this claim. That audit revealed the following expenses:

Legal Fees:	$100,000
Settlement Costs:	39,000
Court Costs:	1000
Total:	$140,000

The DCAA audit revealed that the legal and settlement costs that *XYZ* proposed as a direct charge to the contract were accu-

86. The U.S. Equal Employment Opportunity Commission is an independent federal agency originally created by Congress in 1964 to enforce Title VII of the Civil Rights Act of 1964. The Commission is composed of five commissioners and a general counsel appointed by the President and affirmed by the Senate. The EEOC is also responsible for enforcing the Equal Pay Act of 1963, the Age Discrimination in Employment Act of 1967, Title I and V of the Americans with Disabilities Act of 1990, Sections 501 and 505 of the Rehabilitation Act of 1973, and the Civil Rights Act of 1991. The EEOC also provides oversight and coordination of all federal equal employment opportunity regulations, practices, and policies. Equal Employment Opportunity Commission, *What is the EEOC and How Does It Operate*, *at* http://www.eeoc.gov/facts/qanda.htm (last visited Sept. 30, 2003); *see* Civil Rights Act of 1964, 42 U.S.C. 2000 (2000).

87. FAR, *supra* note 11, at 52.222-26(b)(1).

88. *See* Motion for a Board Order to Compel, Tecom, Inc., at 3, ASBCA No. 53884 (Oct. 7, 2002).

89. *See id.* at 6.

90. The FAR determines allocability as follows:

> A cost is allocable if it is assignable or chargeable to one or more cost objectives on the basis of relative benefits received or other equitable relationship. Subject to the foregoing, a cost is allocable to a Government contract if it—
>
> (a) Is incurred specifically for the contract;
>
> (b) Benefits both the contract and other work, and can be distributed to them in reasonable proportion to the benefits received; or
>
> (c) Is necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown.

FAR, *supra* note 11, at 31.201-4.

91. Caldera v. Northrop Worldwide Aircraft Servs., Inc., 192 F.3d 962 (Fed. Cir. 1999). In this case, the CAFC held that attorneys' fees were not allocable to a contract because they did not "benefit" the government.

> It is established that the contractor must show a benefit to government work from an expenditure that it claims is 'necessary to the overall operation of the [contractor's] business." . . . We can discern no benefit to the government in a contractor's defense of a wrongful termination lawsuit in which the contractor is found to have retaliated against the employees for the employee's refusal to defraud the government.

Id. at 972.

mulated and charged to the G&A expense pool and allocated to all contracts for fiscal years 1997 through 2001. *XYZ* denied that it charged the settlement amount of $40,000 to G&A.[92]

On 4 April 2002, the CO issued a final decision demanding the $100,000 in legal fees that *XYZ* charged to G&A during fiscal years 1997 through 2001. The letter further stated that the government could not reimburse *XYZ* for its settlement costs ($39,000) and court costs ($1000), unless *XYZ* shows that the sexual harassment allegations have "very little likelihood of success."[93]

The government and *XYZ* were clearly at an impasse at the time of their last communication on 26 April 2002. *XYZ* saw the expenses as compensable and the government did not. The president of *XYZ* sent an invoice for the settlement fees to the government. *XYZ* filed a complaint with the ASBCA on 5 August 2002, claiming reimbursement for legal fees and settlement costs associated with the sexual harassment claims of a former employee. The government responded that it would not reimburse *XYZ* until it meets the burden of proof under the case law, the FAR, and the CAS.[94] As the contract attorney, you tell the CO that you will study the issue, and get back to her.

Based on the foregoing analysis, assume the *Boeing II* standard applies in this hypothetical case. Therefore, *XYZ* must prove that *Ms. B*'s lawsuit had "very little likelihood of success" in order to establish that its legal fees are allowable.[95] First, the CO would consider allocability. As CAFC noted, "[a]llocability is an accounting concept involving the relationship between incurred costs and the activities or cost objectives (e.g. contracts) to which those costs are charged."[96] The CAFC further explained that "[p]roper allocation of costs by a contractor is important because it may be necessary for the contractor to allocate costs among several government contracts or between government and non-government activities."[97]

The CAFC added that "[t]he concept of cost allocability concerns whether a particular cost can be recovered from the government in whole or in part. Cost allocability here is to be determined under the CAS, 4 C.F.R. Parts 403, 410."[98] The concept of allocability addresses whether a sufficient nexus exists between the cost and a government contract.[99] Although a cost may be allocable to a contract, the cost is not necessarily allowable. In *Boeing II*, the CAFC agreed that costs might be assignable and allocable under the CAS[100] but not allowable under the FAR.[101]

The FAR makes clear that while the total cost of a contract includes all costs properly allocable to the contract, the allowable costs to the government are limited to those allocable costs that are allowable under the FAR and the applicable agency supplements.[102] The CAS governs if there is a direct conflict between the CAS and the FAR on issues of allocability.[103]

In *Boeing II*, the court held that "[a]llocability is an accounting concept and the CAS does not require that a cost directly benefit the government's interests for the cost to be allocable."[104] The CAFC concluded that the "word 'benefit' is used in allocability provisions to describe the nexus required for accounting purposes between the cost and the contract to which it is allocated."[105]

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92. *See* Motion for a Board Order to Compel, Tecom, Inc., at 4-5, ASBCA No. 53884 (Oct. 7, 2002).

93. Boeing II, 298 F.3d 1274, 1288-89 (Fed. Cir. 2002).

94. *Id.* at 1274. On 29 July 2002, the CAFC established two new and important legal standards for allocability and allowability of costs under government cost-reimbursement contracts. With respect to allocability, the court deviated from its earlier decisions which provided that costs were allocable only if there was some "benefit to the government" for incurring the cost, and that the contractor had to show a benefit to government work from an expenditure of a cost that it claims is necessary to the overall operation of the contractor's business. *Id.* at 1290. The CAFC now held that the costs for attorneys' fees in third-party civil suits may be allowed only if it has been determined that the plaintiffs had "very little likelihood of success on the merits" of prevailing. *Id*. at 1290.

95. *Id*. at 1288-89.

96. *Id*. at 1280.

97. *Id*.

98. *Id*.

99. *Id*. at 1281.

100. *See supra* note 49.

101. *Boeing II*, 298 F.3d at 1285.

102. FAR, *supra* note 11, at 31.201-1(b).

103. *Boeing II*, 298 F.3d at 1283.

104. *Id.* at 1284.

Since *Boeing II*, contractors must allocate the costs between government and non-government contracts. In this case, *Mr. T* began his alleged harassment of *Ms. B* at a commercial construction site. The harassment continued at a government contract site. *XYZ* may have to determine when the harassment began, the effect of *Mr. T*'s actions at each site, and allocate the costs of defending the lawsuits accordingly. The CO will judge whether this allocation is proper. Once the CO answers the allocability question, she must address allowability. Whether *Boeing II* applies or not, will depend on the ASBCA's interpretation of the term "related," a word in FAR section 31.204 that played a central role in *Boeing II*.[106]

With respect to the settlement payment, the Army would "argue that they are 'related' to penalties made unallowable by FAR [section] 31.205-15."[107] As explained, the CAFC's discussion in *Boeing II* "favors a broad application of the 'related' standard."[108] *XYZ* paid *Ms. B* $39,000 to settle her case. Although this payment might be encompassed by the above allowability argument concerning legal fees, there is another basis for finding it unallowable. FAR section 31.205 -15(a) states the following:

> Costs of fines and penalties resulting from violations of, or failure of the contractor to comply with, Federal, State, local, or foreign laws and regulations, are unallowable except when incurred as a result of compliance with specific terms and conditions of the contract or written instructions from the CO.[109]

Practitioners have addressed this issue since *Boeing II*. In the government's brief in support of its Motion to Compel in *Tecom Inc.*,[110] U.S. Army Contract Appeals Division (CAD) attorneys argued that "[a] payment in a settlement of a civil suit is a substitute for the fine or penalty that was at risk in the action filed" by the plaintiff.[111] "Therefore, it is 'related' to the unallowable fines and penalties in FAR [section] 31.205-15 (a),[112] Fines, Penalties, and Mischarging Costs."[113] They reiterated that "[t]here is no 'little likelihood of success' standard in FAR [section] 31.205-15 (a), and that standard should not apply to the settlement payment."[114] Applying this argument to the *XYZ* scenario, the $39,000 plus $1000 should be "unallowable even if the legal fees are determined to be allowable under the little likelihood of success standard in *Boeing*."[115] According to the CAD, this is a reasonable outcome because *XYZ* paid the $39,000 plus $1000 to *Ms. B* to "limit its risk for the alleged wrongdoing and such a payment is undoubtedly 'related' to a penalty."[116]

Concerning the attorneys' fees, the Army argues, "the 'related' standard is broad enough to sweep in non-fraud wrongdoing, such as sexual harassment, pursuant to FAR [section] 31.205-47."[117] The CO must now decide whether *Ms. B*'s

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105. *Id.*

106. FAR, *supra* note 11, at 31.204.

107. Brief for Respondent, Tecom, Inc., at 2, ASBCA No. 53884 (Dec. 4, 2002) (citing *Boeing II*, 298 F.3d at 1285).

108. *Id.*

109. FAR, *supra* note 11, at 31.205-15(a).

110. Tecom, Inc., ASBCA No. 53884 (Oct. 7, 2002). This is a case subsequent to *Boeing II* addressing the allowability of contractor legal costs for defending a third-party civil case.

111. *See supra* note 3, Motion for a Board Order to Compel, Tecom, Inc., at 3, ASBCA No. 53884 (Oct. 7, 2002)

112. The FAR section regarding fines, penalties and mischarging costs provides:

> (a) Costs of fines and penalties resulting from violations of, or failure of the contractor to comply with, Federal, State, local, or foreign laws and regulations, are unallowable except when incurred as a result of compliance with specific terms and conditions of the contract or written instructions from the CO.
>
> (b) Costs incurred in connection with, or related to, the mischarging of costs on Government contracts are unallowable when the costs are caused by, or result from, alteration or destruction of records, or other false or improper charging or recording of costs. Such costs include those incurred to measure or otherwise determine the magnitude of the improper charging, and costs incurred to remedy or correct the mischarging, such as costs to rescreen and reconstruct records.

FAR, *supra* note 11, at 31.205-15.

113. Brief for Respondent, Tecom, Inc., at 12-13, ASBCA No. 53884 (Oct. 7, 2002).

114. *Id.*

115. *Id.*

116. *Id.*

claim had "very little likelihood of success on the merits."[118] If so, the legal costs are allowed. If not, the legal costs are disallowed.

This is where the difficulty arises. The CO would be called upon to decide timeliness issues, such as whether the federal discrimination claim has been timely filed, given that the state court action is pending. Also, she must assess the evidence and decide whether *Ms. B* is likely to prevail before a judge or a jury on her claim. Because there were better witnesses at the commercial site than at the government site, the CO may decide that there is a substantiated harassment claim at the commercial site but not for the harassment allocable to the government contract. Finally, she would have to decide where "success on the merits" would apply.[119] It might apply at: (1) an alternative dispute resolution; (2) before an EEOC administrative judge; (3) before a state court judge; or (4) before a federal court judge or jury.[120]

These issues are challenging even for experienced employment law judges. The COs would certainly find these issues challenging and would likely have difficulty with them; COs are not trained in employment discrimination nor are they trained to determine whether suits are meritorious. Although one can persuasively argue that the new *Boeing II* standard requires COs to make these determinations, they are not well equipped to do so. Additionally, the CO would not be able to adequately assess these issues without a factual basis for the claims. In the *XYZ* scenario, the plaintiff's version of the facts would be unavailable because *Ms. B* is bound by a confidentiality agreement.

The Aftermath of the *Boeing II* Decision

Following *Boeing II*, attorneys with extensive government procurement experience disagreed about the scope of the CAFC's ruling. Practitioners were concerned with the practical effects that an overly broad scope would have on the COs in the field. One attorney stated the following:

> I am concerned that COs will improperly misinterpret *Boeing* [II] to apply the standard from FAR [section] 31.205-47(c)(2) to any third-party civil cases filed against government contractors. As an example, the application of that standard to employment litigation alleging wrongful discharge based on discrimination would create a terrible and very costly problem for contractors. COs will have free rein to second guess settlement decisions, and disallow legal costs if they believe that the plaintiffs had more than a 'very little likelihood of success on the merits.' Such second-guessing is inconsistent with the Government emphasis on alternative dispute resolution, the settlement of litigation, and judicial economy. Further, if *Boeing* is so interpreted by COs, it raises the serious question of what expertise and training do COs possess to determine whether plaintiffs were likely to prevail before a judge or jury on a sex, age, or racial discrimination charge against Government contractors. How are COs and their legal advisors to determine between meritorious suits and suits that lack merit?[121]

Professors Ralph C. Nash[122] and John Cibinic[123] (Nash and Cibinic) have opined that these concerns are misplaced. Their position is that "[w]e do not believe it appropriate for COs, the board of contract appeals, or the courts to extend the 'very little likelihood of success on the merits' standard to any 'third-party civil cases.'"[124] Rather, they believe that *Boeing II* "makes it clear that the key for application of FAR [section] 31.204(c) is the specific disallowance of a type of cost in FAR [section]

117. *Id*. at 1-2.

118. Boeing II, 298 F.3d 1274, 1288-89 (Fed. Cir. 2002).

119. *Id*. at 1288-89.

120. *See generally id.* (explaining that the "regulations suggest that where a private suit is involved an inquiry is necessary to determine whether the plaintiff was likely to prevail").

121. Nash & Cibinic, *supra* note 10, ¶ 45 (quoting an unnamed attorney).

122. Ralph C. Nash, Jr. received an A.B. from Princeton University and a Juris Doctor from The George Washington University. He has written and lectured extensively in the government contracts field. In 1960, he founded the George Washington University's government contracts program, and served as its director from 1960 to 1966 and from 1979 to 1984. He taught at the law school from 1960 to 1993, retiring to become Professor Emeritus. He also is a consultant for law firms, government agencies, and private corporations. JOHN CIBINIC, JR. & RALPH C. NASH, JR., FORMATION OF GOVERNMENT CONTRACTS vii (3d ed. 1998).

123. John Cibinic, Jr. received an A.B. from the University of Pittsburgh and a Juris Doctor from The George Washington University. He has written and lectured extensively in the government procurement field. He taught at the George Washington University Law School from 1963 to 1993, retiring to become a Professor Emeritus. He was Director of the government contracts program from 1966 through 1974. In addition to teaching, he is a consultant for private corporations, law firms, and government agencies. *Id.*

124. Nash & Cibinic, *supra* note 10, ¶ 45.

31.205."[125] They believe the CAFC "found no similarity in the case of suits against boards of directors because FAR [section] 31.205 did not 'address' the costs of defending boards of directors from 'charges that they tolerated inadequate controls concerning possible fraud or similar misconduct.'"[126] Thus, Nash and Cibinic explain that CAFC created a "relatively strict test for determining whether costs are 'similar.' FAR [section] 31.205 must deal specifically with the type of conduct upon which the civil suit is based for the 'similar' test to be invoked. Since FAR [section] 31.205 does not deal with suits against directors, the costs were not similar."[127]

With respect to the *Boeing II* "related" test,[128] Nash and Cibinic do not believe that COs will have to apply this test because the related test also requires coverage in FAR section 31.205.[129] Nash and Cibinic argue that *Boeing II* addresses civil suits involving fraud.[130] They explain that "[s]ince costs relating to fraud against the government are covered in FAR [section] 31.205-47 ('Costs related to legal and other proceedings') and the allegations in this suit included fraud against the Government, the court found the test in that section should be applied to the costs in this case."[131] Based on the fraud analysis, Nash and Cibinic conclude that "[t]he 'very little likelihood of success on the merits' test is not covered by any provision in FAR [section] 31.205 other than FAR [section] 31.205-47(b). Since that provision deals only with fraud against the government, it would be improper to use its test for any other type of cost."[132]

Others, however, disagree with Nash and Cibinic's conclusion that *Boeing II* is limited to fraud cases. For example, the U.S. Army CAD has responded to the position that *Boeing II* does not apply in the employment discrimination context. In its brief in support of a Motion to Compel in *Tecom Inc*.,[133] the Army argued that:

> the wrongdoing involved in the *Citron* litigation was not fraud. The costs in *Boeing* were legal fees associated with settling a shareholders' lawsuit charging that management "breached their fiduciary duties to the corporation by . . . failing to establish internal controls sufficient to insure that the corporation's business was carried on in a lawful manner."[134]

In fact, the parties stipulated that the *Citron* "complaint did not directly allege that the director-defendants participated in, or had prior knowledge of, any of the . . . instances of wrongdoing" described in the complaint.[135] Therefore, breach of fiduciary duty was the true underlying misconduct.[136]

The CAD noted that in *Boeing II*, the CAFC held that under FAR sections 31.204 and 31.205-47, the breach of fiduciary duty was related to "a proceeding brought by a third party under the False Claims Act in which the United States did not intervene."[137] They argued that once the CAFC "found that the costs were 'related,' the *Boeing II* court applied the 'very little likelihood of success' standard for allowability in FAR [section] 31.205-47 (c)(2)."[138] The Army's attorneys reiterated the CAFC's holding that such costs may be allowable if the CO determines that there was "very little likelihood that the third party [plaintiffs] would have been successful on the merits."[139]

A complaint for breach of fiduciary duty is not a claim of fraud.[140] Therefore, the CAD applied the *Boeing II* "related"[141]

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125. *Id.*

126. *Id.*

127. *Id.*

128. Boeing II, 298 F.3d 1274, 1285 (Fed. Cir. 2002).

129. Nash & Cibinic, *supra* note 10, ¶ 45.

130. *Id.*

131. *Id.*

132. *Id.*

133. Brief for Respondent, Tecom, Inc., at 11, ASBCA No. 53884 (Oct 7, 2002) (citing Boeing II, 298 F.3d 1274, 1276-1277 (Fed. Cir. 2002)).

134. *Id.*

135. *Boeing II*, 298 F.3d at 1277.

136. Brief for Respondent, Tecom, Inc., at 11, ASBCA No. 53884 (Oct. 7, 2002) (citing Boeing N. Am., Inc. v. Roche, 298 F.3d 1274, 1276-77 (Fed. Cir. 2002).

137. *Id.* (citing *Boeing II*, 298 F.3d at 1286).

138. *Id.* (citing *Boeing II*, 298 F.3d at 1286-87).

139. *Id.*

standard and reasoned "if a breach of fiduciary duty is 'related' to conduct that violates the False Claim Act, which is fraudulent, there is no reason why other non-fraudulent conduct may not likewise be considered 'related' to FAR [section] 31.205 (c)(2) for the purposes of evaluating allowability."[142]

The Army wrote that "[s]exual harassment is a breach of contract and illegal conduct. However, it, like breach of fiduciary duty, is not fraud . . . . Arguably, sexual harassment is worse behavior than breach of fiduciary duty."[143] They argued that "if breach of fiduciary duty is related to False Claims Act violations for allowability purposes, so is sexual harassment."[144] The Army concluded that "the *Boeing* [II] standard applies in the case of employment discrimination. The contractor must prove that the employee's lawsuit had 'very little likelihood of success' in order to establish that its legal fees are allowable."[145]

The CAD's position is more persuasive than that of Nash and Cibinic for one critical reason. As the government correctly pointed out, "[b]reach of fiduciary duty is not fraud."[146] Much of Nash and Cibinic's analysis centers on the idea that the *Boeing II* costs were fraud-related, and costs relating to fraud against the government are covered under FAR section 31.205-47. Therefore, the CAFC found the test in that section should be applied to the costs.[147] This portion of their analysis, properly understood, significantly weakens their position that *Boeing II* will be narrowly applied. Hence, the Army's conclusion that "if breach of fiduciary duty is related to False Claims Act violations for allowability purposes, so is sexual harassment"[148] appears to be the most accurate statement of the law in this area. The *Boeing II* standard would apply in the case of employment discrimination.[149]

Although Nash and Cibinic suggest that *Boeing II* is limited to fraud cases, there are no reported cases that deal with the interpretation of the language "similar" or "related" in FAR section 31.204. Recently, in the appeal of *Tecom, Inc.*, the Army attempted to secure the testimony of a terminated employee bound by a confidentiality agreement, in order to properly perform the *Boeing II* cost analysis.[150] The ASBCA, however, did not decide the issue in that case, instead holding that it lacked jurisdiction to require the release of any confidentiality agreement.[151] Thus, it appears that contractors, COs, attorneys, and commentators will be left to struggle with these issues until the ASBCA or the federal courts resolve them.

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140. *Id*. at 11.

141. Boeing II, 298 F.3d 1274, 1276-1277 (Fed. Cir. 2002).

142. Brief for Respondent, Tecom, Inc., at 12, ASBCA No. 53884 (Dec. 4, 2002) (citing *Boeing II*, 298 F.3d at 1285).

143. *Id*.

144. *Id*.

145. *Id*.

146. *Id.*

147. *Id*.

148. *Id*.

149. *Id*.

150. Tecom, Inc., ASBCA No. 53884 (Dec. 4, 2002).

151. Opinion and Order on Government's Motion to Compel, Tecom, Inc., at 11, ASBCA No. 53884 (Dec. 4, 2002).