THE ARMY LAWYER

Headquarters, Department of the Army

Department of the Army Pamphlet 27-50-371

April 2004

Articles

Editor, Captain Heather J. Fagan
Adjunct Editor, Lieutenant Colonel Timothy M. Tuckey
Adjunct Editor, Major Carissa D. Gregg
Technical Editor, Charles J. Strong

The Army Lawyer (ISSN 0364-1287, USPS 490-330) is published monthly by The Judge Advocate General's Legal Center and School, Charlottesville, Virginia, for the official use of Army lawyers in the performance of their legal responsibilities. Individual paid subscriptions to *The Army Lawyer* are available for $45.00 each ($63.00 foreign) per year, periodical postage paid at Charlottesville, Virginia, and additional mailing offices (see subscription form on the inside back cover). POSTMASTER: Send any address changes to The Judge Advocate General's Legal Center and School, 600 Massie Road, ATTN: JAGS-ADA-P, Charlottesville, Virginia 22903-1781. The opinions expressed by the authors in the articles do not necessarily reflect the view of The Judge Advocate General or the Department of the Army. Masculine or feminine pronouns appearing in this pamphlet refer to both genders unless the context indicates another use.

The Army Lawyer welcomes articles from all military and civilian authors on topics of interest to military lawyers. Articles should be submitted via electronic mail to charles.strong@hqda.army.mil or on 3 1/2" diskettes to: Editor, *The Army Lawyer*, The Judge Advocate General's Legal Center and School, U.S. Army, 600 Massie Road, ATTN: JAGS-ADA-P, Charlottesville, Virginia 22903-1781. Articles should follow *The Bluebook, A Uniform System of Citation* (17th ed. 2000) and *Military Citation* (TJAGSA, 8th ed. 2003). Manuscripts will be returned on specific request. No compensation can be paid for articles.

The Army Lawyer articles are indexed in the *Index to Legal Periodicals*, the *Current Law Index*, the *Legal Resources Index*, and the *Index to U.S. Government Periodicals*. *The Army Lawyer* is also available in the Judge Advocate General's Corps electronic reference library and can be accessed on the World Wide Web by registered users at http://www.jagcnet.army.mil/ArmyLawyer.

Address changes for official channels distribution: Provide changes to the Editor, *The Army Lawyer*, The Judge Advocate General's Legal Center and School, 600 Massie Road, ATTN: JAGS-ADA-P, Charlottesville, Virginia 22903-1781, telephone 1-800-552-3978, ext. 396 or electronic mail to charles.strong@hqda.army.mil.

Issues may be cited as ARMY LAW., [date], at [page number].

Articles

TJAGLCS Practice Notes

Labor Law Practice Note

Legal Assistance Practice Note

Note from the Field

The Applicability of the Randolph-Sheppard Act to Military Mess Halls

Major Erik L. Christiansen
Student, 52d Judge Advocate Officer Graduate Course
The Judge Advocate General's Legal Center and School, U.S. Army
Charlottesville, Virginia

I can see clearly now the [competition's] gone. I can see all obstacles in my way.[1]

Introduction

The Randolph-Sheppard Act for the Blind (RSA),[2] enacted in 1936, provides blind vendors with a preference for certain federal contracts. Since 1936, Congress has amended the Act several times to strengthen consideration for blind vendors, most importantly in 1974.[3] Recent decisions at the federal district and appellate levels interpreting the RSA in light of the 1974 amendments have further expanded the Act's reach.[4] One such expansion, the application of the Act to military mess hall contracts, has sparked significant controversy, in part, because the blind vendor preference directly conflicts with other procurement preference programs.[5]

This article surveys the current controversy over military mess halls under the RSA. It begins with a brief history of the Act, to include the 1974 amendments that expanded the RSA to include "cafeterias" on "federal property."[6] Next, the article addresses three areas of litigation concerning military mess hall contracts arising from the 1974 amendments. The first area involves whether the RSA applies to military mess halls at all. It discusses agency interpretations and implementation of the 1974 RSA amendments, which read "mess halls" into the RSA's definition of "cafeteria," and the resultant federal cases, *NISH v. Cohen*[7] and *NISH v. Rumsfeld*.[8] The second area of litigation concerns the relationship of the blind vendor priority to other procurement preference programs, including the Javits Wagner O'Day Act,[9] the Historically Underutilized Business Zone (HUBZone) Act,[10] and small business set-asides, as exemplified by *In re Intermark*[11] and *Automated Communications Systems, Inc. v. United States*.[12] The third area of litigation explores the scope of the blind vendor preference. It discusses aspects of competitive range determination, as in *Oklahoma v. Oklahoma Department of Rehabilitative Services*,[13] and the discretion accorded a contracting officer's determination of the applicability of the RSA, analyzed in *Washington State Department of Services for the Blind* (*WSDSB*) *v. United States*.[14] The article concludes with a cursory discussion of future mess hall litigation in light of these federal opinions and the National Defense Authorization Act for Fiscal Year 2004.[15]

---

1. JOHNNY NASH, I CAN SEE CLEARLY NOW, *on* I CAN SEE CLEARLY NOW (Sony 1972).
2. 20 U.S.C. §§ 107-107f (2000).
3. *See generally* Randolph-Sheppard Act Amendments of 1974, Pub. L. No. 93-516, 88 Stat. 1622.
4. *See, e.g.*, NISH v. Cohen, 95 F. Supp. 2d 497 (E.D. Va. 2000), *aff'd*, 247 F.3d 197 (4th Cir. 2001).
5. *See, e.g., id.* at 498 (illustrating conflict with the Javits Wagner O'Day Act).
6. Randolph-Sheppard Act Amendments of 1974, §§ 202, 207, 88 Stat. at 1623, 29.
7. 95 F. Supp. 2d 497 (E.D. Va. 2000), *aff'd*, 247 F.3d 197 (4th Cir. 2001).
8. 188 F. Supp. 2d 1321 (D.N.M. 2002).
9. 41 U.S.C. §§ 46-48c (2000).
10. 15 U.S.C. §§ 631-650.
11. B-290925, 2002 Comp. Gen. LEXIS 167 (Oct. 23, 2002).
12. 49 Fed. Cl. 570 (2001).
13. 1998 U.S. Dist. LEXIS 23041 (W.D. Okla. Jan. 7, 1998).
14. 2003 U.S. Claims LEXIS 381 (Fed. Cl. Dec. 17, 2003).
15. H.R. 1588, 108th Cong. (2003) (enacted).

History of the Randolph-Sheppard Act

Congress enacted the RSA in 1936 to "provid[e] blind persons with remunerative employment, enlarg[e] the economic opportunities of the blind, and stimulat[e] the blind to greater efforts in striving to make themselves self-supporting."[16] To that end, the Act authorized blind vendors to operate vending stands in federal buildings.[17] Due in part to the authority the Act bestowed on agency officials to approve blind vendors' operations,[18] the 1936 Act met with limited success.

Spurred by the "invention of vending machines," Congress reexamined the RSA in 1954.[19] Although the amendments "showed concern for expanding the opportunities of the blind,"[20] such as applying the RSA to federal *properties* (previously *buildings*), the Act maintained discretion with agency officials to implement the Act's provisions "so far as feasible."[21] Consequently, "[in] reality [the 1954 amendments] fell far short of [c]ongressional intent to expand the blind vendor program."[22]

In 1974, Congress again addressed the lack of impetus for the program,[23] responding with amendments that (1) secured the priority of blind vendors on federal properties; and (2) expanded the scope of blind vendor opportunities.[24] The 1974 amendments established a federal-state relationship that effectively replaced the previous "so far as feasible" preference.[25] The amendments mandated the Department of Education (DOE), through the Commissioner of Rehabilitative Services Administration (CRSA), to publish regulations ensuring the *priority* of blind vendors in the "operation of vending facilities on [f]ederal property."[26] The amendments require State Licensing Agencies (SLAs), through their respective chief executives, to "give preference to blind persons who are in need of employment"[27] and to "cooperate with the [CRSA] in carrying out the purpose of the [RSA]."[28]

---

16. Act of June 20, 1936, Pub. L. No. 74-732, § 1, 49 Stat. 1559.

17. *Id.*

18. *See id.*

19. Contract & Fiscal Law Dep't, The Judge Advocate General's School & Legal Center, U.S. Army, 52d Graduate Course Contract Law Deskbook 10-25 (Fall 2003) [hereinafter Contract Law Deskbook] (construing Act of Aug. 3, 1954, Pub. L. No. 83-565, 68 Stat. 663).

20. *Id.*

21. Act of Aug. 3, 1954, § 4, 68 Stat. at 663.

22. Contract Law Deskbook, *supra* note 19, at 10-26. *See also* Randolph-Sheppard Act Amendments of 1974, Pub. L. No. 93-516, § 201(1), 88 Stat. 1622 ("[T]he [blind vendor] program has not developed, and has not been sustained, in the manner and spirit in which the Congress intended at the time of the [RSA's] enactment.").

23. *See generally* Review of Vending Operations on Federally Controlled Property, Comp. Gen. No. B-176886, Sept. 27, 1993, *cited in* Contract Law Deskbook, *supra* note 19, at 10-27.

24. *See* Randolph-Sheppard Act Amendments of 1974, § 202, 88 Stat. at 1623.

25. *See id*. § 203, 88 Stat. at 1623-24 (codified as amended at 20 U.S.C. § 107a (2000)).

26. *Id*. § 202, 88 Stat. at 1623 (codified as amended at 20 U.S.C. § 107(b)).

27. 20 U.S.C. § 107a(b).

28. *Id.* § 107b(1). The 1974 RSA amendments outline how the SLAs get involved in giving priority to blind vendors on federal property. The Act states that "in authorizing the operation of vending facilities on [f]ederal property, priority shall be given to blind persons licensed by a [s]tate agency." *Id.* The Act then directs the Secretary of Education to designate an SLA in each state. "These SLAs license blind persons for the operation of vending facilities on federal property. In issuing licenses, the SLAs are required to give preference to blind persons who need employment." *Id.* §§ 107a(a)(5), (b)(2), *cited in* North Carolina Div. of Servs. for the Blind v. United States, 53 Fed. Cl. 147, 150 (2002). The regulations promulgated by the DOE under the Act then invite the SLAs to respond to solicitations for cafeteria operation contracts:

> [T]o establish the ability of blind vendors to operate a cafeteria in such a manner as to provide food service at comparable cost and . . . quality . . . the appropriate [SLA] shall be invited to respond to solicitations for offers when a cafeteria contract is contemplated by the appropriate . . . agency.

34 C.F.R. § 395.33 (LEXIS 2004).

In addition to strengthening the blind vendor preference, the 1974 amendments expanded the scope of the RSA to include management functions previously considered beyond blind vendor capabilities.[29] This extension included the addition of the operation of cafeterias to the RSA's list of covered "vending facilities."[30] Unfortunately, the 1974 RSA amendments did not define cafeteria, providing an ambiguity as to whether Congress intended military mess halls to fall within the RSA's ambit.

Military Mess Hall Contract Litigation Stemming from the 1974 RSA Amendments

The 1974 amendment's undefined term "cafeteria" and concomitant strengthening of priority for blind vendors has resulted in litigation of military mess hall contracts on several fronts: (1) whether the RSA applies to military mess halls at all;[31] (2) the interrelationship of the RSA preference to other set-aside programs;[32] and (3) the discretion of an agency when administering the RSA preference.[33] The following sections address these areas of litigation.

Application of the RSA to Military Mess Halls

Agency Interpretation and Implementation

As discussed above, the RSA is silent on the definition of the term "cafeteria." The Departments of Education and Defense, however, did define cafeteria in their respective regulations promulgated to implement the RSA's provisions. Both Departments provide a "standard" definition of cafeteria, but neither definition expressly includes or excludes military mess halls.[34]

Given this statutory and regulatory background, in 1993 the Comptroller General, in *U.S. Department of the Air Force—Reconsideration* (*Keesler*),[35] determined that the Air Force properly applied the RSA to a contract for full food services at Keesler Air Force Base. Contractors KCA and Triple P Services protested the solicitation, in part, because "the [RSA] statute and [DOE's] implementing regulations . . . apply only to cafeteria operations, not food services at military dining halls such as the services required [by the Keesler solicitation]."[36] Further, the protestors argued that even if the procurement fell within the DOE's definition of cafeteria, provisions of *Department of Defense* (*DOD*) *Directive 1125.3*, *Vending Facility Pro-*

---

29. *See* Randolph-Sheppard Act Amendments of 1974, § 202, 88 Stat. at 1623; U.S. Dep't of Air Force–Reconsideration, B-250465.6, B-250465.7, B-250783.2, 1993 U.S. Comp. Gen. LEXIS 530, at *16-17 (June 4, 1993) (citing S. REP. NO. 937, at 25 (1974)).

30. *See* 20 U.S.C. § 107e(7). The RSA defines "vending facilities," in full, to mean

> automatic vending machines, cafeterias, snack bars, cart services, shelters, counters, and such other appropriate auxiliary equipment as the Secretary [of Education] may by regulation prescribe as being necessary for the sale of the articles or services described in [20 U.S.C. § 107a(a)(5)] and which may be operated by blind licensees[.]

Id.

31. *See, e.g.*, NISH v. Rumsfeld, 188 F. Supp. 2d 1321 (D.N.M. 2002), *aff'd*, 2003 U.S. App. LEXIS 23290 (10th Cir. Nov. 14, 2003); NISH v. Cohen, 95 F. Supp. 2d 497 (E.D. Va. 2000), *aff'd*, 247 F.3d 197 (4th Cir. 2001); *U.S. Dep't of Air Force—Reconsideration*, 1993 U.S. Comp. Gen. LEXIS 530, at *16-17.

32. *See, e.g.*, Automated Communications Sys., Inc. v. United States, 49 Fed. Cl. 570 (2001); *In re* Intermark, Inc., B-290925, 2002 Comp. Gen. LEXIS 167 (Oct. 23, 2002); *U.S. Dep't of Air Force—Reconsideration*, 1993 U.S. Comp. Gen. LEXIS 530.

33. *See, e.g.*, Southfork Sys. v. United States, 141 F.3d 1124 (Fed. Cir. 1998); Oklahoma v. Oklahoma Dep't of Rehabilitative Servs., 1998 U.S. Dist. LEXIS 23041 (W.D. Okla. Jan. 7, 1998); Washington State Dep't of Servs. for the Blind v. United States, 2003 U.S. Claims LEXIS 381 (Fed. Cl. Dec. 17, 2003); *North Carolina Div. of Servs. for the Blind*, 53 Fed. Cl. at 147.

34. *See* 34 C.F.R. § 395.1(d) (LEXIS 2004) (DOE); 32 C.F.R. subpt. 260.6 (LEXIS 2004) (DOD). The DOE definition provides:

> Cafeteria means a food dispensing facility capable of providing a broad variety of prepared foods and beverages (including hot meals) primarily through the use of a line where the customer serves himself from displayed selections. A cafeteria may be fully automatic or some limited waiter or waitress service may be available and provided within a cafeteria and table or booth seating facilities are always provided.

34 C.F.R. § 395.1(d). The DOD adopts the DOE definition virtually verbatim, then adds the following sentence: "DoD Component food dispensing facilities which conduct cafeteria-type operations during part of their normal operating day and full table-service operations during the remainder of their normal operating day are not 'cafeterias' if they engage primarily in full table-service operations." 32 C.F.R. subpt. 260.6. The DOD uses this same definition for cafeteria in its directive. *See* U.S. DEP'T OF DEFENSE, DIR. 1125.3, VENDING FACILITY PROGRAM FOR THE BLIND ON FEDERAL PROPERTY para. E1.1.1 (7 Apr. 1978) (C1 22 Aug. 1991) [hereinafter DOD DIR. 1125.3].

35. B-250465.6, B-250465.7, B-250783.2, 1993 U.S. Comp. Gen. LEXIS 530 (June 4, 1993).

36. *Id.* at *3. The Air Force initially solicited the contract as an 8(a) small business set-aside. KCA and Triple P, two 8(a) eligible firms, submitted bids by the original bid closing date. Subsequent to bid closing, the Air Force cancelled the original solicitation, re-soliciting the contract on an "unrestricted basis to comply with the [RSA]." *Id*. In addition to their position that the RSA did not apply to the procurement, KCA and Triple P also protested the subservience of the 8(a) program to the RSA. *Id*. This article discusses that aspect of the protest *infra* notes 100-12 and accompanying text.

gram for the Blind on Federal Property,[37] exclude "open messes and military clubs which engage primarily in full table-service operations."[38]

The Comptroller General denied the protest. First, he dismissed the protesters' narrow interpretation of the DOE regulations' definition of criteria. The Comptroller General opined that the DOE's definition of cafeteria, which focuses on the "salient characteristics of such a facility," logically encompassed the services the protesters argued the definition did not cover.[39] Second, upon review of the plain meaning of the RSA, the Act's legislative history, agency regulations, *DOD Directive 1125.3*, and DOD interpretations of its regulations, the Comptroller General determined that nothing in these sources precluded the application of the RSA to the Keesler dining hall procurement.[40] Both the agency charged with the implementation of the RSA program, DOE,[41] and the DOD General Counsel[42] agreed with the Comptroller General's interpretation.

Federal Court Decisions

NISH v. Cohen (NISH I)[43]

Relying on the above agency regulations, DOD directive, and agency head interpretations, a contracting officer at Fort Lee, Virginia, imposed an RSA preference on a military mess hall contract in 1997. The National Institute for the Severely Handicapped (NISH) sued, giving rise to the seminal RSA military mess hall case, *NISH v. Cohen*.[44]

NISH protested that the RSA did not apply to the Fort Lee mess hall procurement on two primary grounds. First, similar to the protester in *Keesler*, NISH argued that appropriated fund military mess halls do not fall within the RSA's definition of "normal" cafeterias. NISH argued that vending facilities, as defined by the RSA, require a point of sale transaction, an ability to set prices, or both.[45] Second, even if mess halls fall within the RSA definition of cafeteria, NISH argued that the RSA is inapplicable to the Fort Lee procurement because the RSA is not a procurement statute. Therefore, setting an RSA preference violates the full and open competition requirements of the Competition in Contracting Act (CICA).[46] Similarly, because the relevant provisions of the Federal Acquisition Regulation (FAR) omit mention of the RSA preference, NISH argued that the RSA is also not exempt from the FAR.[47]

On 25 April 2000, the District Court for the Eastern District of Virginia (EDVA) granted the defendants' (DOE and DOD) cross-motion for summary judgment. The district court determined that the *Chevron* analysis applied to NISH's claims:

> Where a statute is silent or ambiguous regarding a specific issue, a reviewing court considers whether the agency's interpretation is based on a permissible construction of the

37. DOD DIR. 1125.3, *supra* note 34.

38. *U.S. Dep't of Air Force—Reconsideration*, 1993 U.S. Comp. Gen. LEXIS 530, at *11. The protesters also argued that the DOE's regulations, which require the blind vendor to provide the services at a "'comparable cost,' impl[y] that the regulations were intended to apply only where the contractor will have discretion with regard to the cost of food and services." *Id.* at *10 (quoting 34 C.F.R. § 395.33(b)). The protesters argued that the contractor will not have such discretion because the Keesler dining hall caters primarily to customers who purchase meals on a "subsistence-in-kind . . . non-cash basis." *Id.* The Comptroller General quickly dismissed this argument, finding that "reasonable cost" in the regulations refers to the examination of proposals, not the examination of cash prices charged at the facility. *Id.* at *14-15.

39. *Id.* at *11-13.

40. *Id.* at *15-23.

41. Memorandum, Frederick K. Schroeder, Commission of Rehabilitative Services Administration, to the Committee for Purchase (Aug. 14, 1997), *quoted in* NISH v. Cohen, 95 F. Supp. 2d 497, 504 (E.D. Va. 2000) (NISH I) (DOE position).

42. Memorandum, Judith A. Miller, Department of Defense General Counsel, to General Counsels of the Military Departments 4 (Nov. 12, 1998), *quoted in NISH I*, 95 F. Supp. 2d at 504 (DOD position).

43. *NISH I*, 95 F. Supp. 2d at 497, *aff'd*, 247 F.3d 197 (4th Cir. 2001) (NISH II).

44. *Id.* Absent an RSA preference, the dining facility contract award would have been a JWOD procurement. NISH, as the statutory JWOD advocate, therefore challenged the contracting officer's decision to impose an RSA preference. *NISH II*, 247 F.3d at 199 (citing 41 C.F.R. § 51-3.1 (LEXIS 2004)). This articles discusses *NISH*'s treatment of the RSA preference in relation to the JWOD program *infra* notes 82-85 and accompanying text.

45. *NISH II*, 95 F. Supp. at 203.

46. *Id.* at 203-04 (citing the Competition in Contracting Act, 10 U.S.C. § 2304(a)(1) (2000)).

47. *NISH I*, 95 F. Supp. 2d at 504 (citing GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 6.302(b) (July 2003) [hereinafter FAR]). The FAR states that it does not apply "when statutes, such as the following, expressly authorize or require that acquisition be made from a specified source or through another agency." *Id.* at 6.302-5(b). The FAR does not explicitly list the RSA as exempt from the FAR. *See id.* NISH argued this omission meant that the RSA was not exempt from the FAR. *NISH I*, 95 F. Supp. 2d at 504. As discussed *infra* text accompanying notes 56-57, the court opined that the FAR's use of the term "such as the following" clearly indicated that the list of statutes explicitly exempted from the FAR was non-exclusive.

> statute. Accordingly, the agency's interpretation of the statute is afforded great deference by the courts and need not be the very best interpretation—so long as it is reasonable.[48]

Accordingly, the court held that the contracting officer did not act unreasonably when he applied an RSA preference to the dining facility contract.[49] Regarding the definition of cafeteria, "the [c]ourt held that, as a matter of law, addition of the term 'cafeteria' to the [RSA], when viewed in conjunction with corresponding regulations and available case law, supports the [RSA's] coverage of the military mess hall services at Fort Lee, Virginia."[50] The court found that the RSA did not violate the CICA's requirements,[51] but did not specifically address NISH's argument as to what qualified the RSA as a procurement statute.[52]

Reviewing the case de novo in 2001, the Court of Appeals for the Fourth Circuit, relying on the same authority as the district court, affirmed the lower court's grant of summary judgment for the government. Significantly, the Fourth Circuit also answered the question left unanswered by the EDVA, finding that the RSA was a procurement statute within the CICA's broad definition of procurement.[53]

NISH argued that 10 U.S.C. § 2304(a)(1)'s exception to full and open competition for "procurement procedures expressly authorized by statute" applied only to statutory procurement procedures.[54] The Fourth Circuit disagreed, determining that the CICA "broadly defines 'procurement' as including 'all stages of the process for determining a need for property or services and ending with contract completion and closeout,'" and that the RSA provisions "clearly fit this sweeping definition."[55] The Fourth Circuit responded similarly to NISH's claim regarding the applicability of the FAR to the RSA. NISH argued that the FAR's lack of explicit reference to the RSA was evidence that "the [RSA] does not involve government purchases of goods or services."[56] The Fourth Circuit dismissed this claim, determining that the FAR's saving clause at section 6.302-5(b)—"such as the following"—clearly encompassed the RSA.[57]

NISH v. Rumsfeld (Rumsfeld I)[58]

On facts "virtually identical" to *NISH v. Cohen*,[59] NISH sued the government in 2002 for awarding the mess hall contract at Kirtland Air Force Base under the RSA. In *NISH v. Rumsfeld*, NISH raised essentially the same arguments it raised in *Cohen*, and it met with the same results. The District Court for the District of New Mexico granted the defendant's motion for summary judgment.[60] In 2003, the Court of Appeals for the Tenth Circuit affirmed.[61]

---

48. *NISH I*, 95 F. Supp. at 500 (citing Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842 (1984)).

49. *Id.* at 505.

50. *Id.* at 499 (referring to the above-mentioned persuasive authority, *supra* notes 40-42 and accompanying text, and the Comptroller General's decision in *Keesler*).

51. *See id.* at 503-04.

52. Major John Siemietkowski et al., *2000 Contract Year in Review*, ARMY LAW., Jan. 2001, at 92-93. NISH based its argument on 10 U.S.C. § 2304(a)(1) (West 1998), which states in part, "[E]xcept in the case of procurement procedures otherwise expressly authorized by statute, the head of an agency in conduction of a procurement for property or services . . . shall obtain full and open competition . . . ." *Id.* NISH further argued that the Fort Lee procurement violated 10 U.S.C. § 2304(k)(2) of the CICA, which states conditions under which provisions of law may be construed as "requiring a new contract to be awarded to a specified non-[f]ederal [g]overnment entity." *Id.* § 2304(k)(2). The District Court for EDVA found that § 2304(k)(2) was inapplicable to the RSA, but did not address § 2304(a)(1). *See NISH I*, 95 F. Supp. 2d at 503-04.

53. NISH II, 247 F.3d 197, 204 (4th Cir. 2001).

54. *Id.* (quoting 10 U.S.C. § 2304(a)(1)).

55. *Id.* (quoting 10 U.S.C. § 2302(3)(A)).

56. *Id.* at 204 n.7. The court noted that the adoption of a contrary position, "that the [RSA] is not a procurement statute pursuant to CICA[,] would require a misreading and misapplication of both statutes." *Id.* In other words, NISH's rationale would undermine the DOE's mandate to enforce the blind vendor provision as envisioned by the RSA.

57. *Id.* (quoting FAR, *supra* note 47, at 6.302-5(b) (1998)). *See supra* note 47.

58. 188 F. Supp. 2d 1321 (D.N.M. 2002), *aff'd*, 2003 U.S. App. LEXIS 23290 (10th Cir. Nov. 14, 2003) (Rumsfeld II).

59. *Id.* at 1326 n.7. Similar to *NISH v. Cohen*, *NISH v. Rumsfeld* also discusses the interrelationship of the RSA preference in relation to the JWOD program. *See* NISH I, 95 F. Supp. 2d 497 (E.D. Va. 2000), *aff'd*, 247 F.3d 197 (4th Cir. 2001). That aspect of these cases is discussed *infra* notes 79-86.

60. *Rumsfeld I*, 188 F. Supp. 2d at 1321.

61. *Rumsfeld II*, 2003 U.S. App. LEXIS 23290, at *4.

Although the New Mexico district court reached the same results as *NISH v. Cohen*, its logic differs. As in *Cohen*, NISH raised two primary arguments in *Rumsfeld* regarding the applicability of the RSA to military mess halls: (1) that the agency is not entitled to deference, therefore, nothing supports reading mess halls into the term cafeteria; and (2) even if mess halls fall within the definition of cafeteria, the RSA does not apply to the procurement because the RSA is not a procurement statute such that it qualifies as an exception to the CICA's requirement for full and open competition.[62]

In dismissing NISH's arguments, the New Mexico district court began its analysis on the same path as *Cohen*: it determined that the issue concerns an ambiguous statute, thus the correct standard of review for the agency action is *Chevron* deference.[63] When determining whether the agency acted reasonably, however, the *Rumsfeld* district court veered from *Cohen*. In *Cohen*, the district and appellate courts assessed the agency's reasonableness by examining the DOE and DOD RSA regulations and the authorities the agency considered in determining that the RSA applied to the procurement.[64] The New Mexico district court, in contrast, assessed agency reasonableness by looking at "the plain language of CICA and the definition of 'procurement' that applies to military procurement contracts."[65] In other words, the district court conflated NISH's two distinct arguments.

On appeal, the Tenth Circuit bifurcated NISH's arguments, as per *NISH v. Cohen*. Regarding the applicability of the CICA to the RSA, NISH renewed its argument that the "authorization of vending facilities on federal property is not 'procurement' because it does not involve the acquisition of properties or services."[66] The *Rumsfeld* court refused to adopt NISH's narrow definition. Instead, the court adopted the Fourth Circuit's analysis, determining that the CICA broadly defined procurement such that this term encompassed the provisions of the RSA.[67]

Regarding its contention that the agency is not entitled to *Chevron* deference, however, NISH raised several novel arguments on appeal. First, NISH contended that the district court failed to establish the first prong of the *Chevron* test, which requires establishing whether the statute evidences a clear congressional intent. NISH argued that the statute clearly expresses Congress's intent that the RSA definition of vending facility only include "places where a private individual runs a business selling food and services to the public for profit," thus excluding military mess halls.[68] The Tenth Circuit rejected this argument, finding that NISH failed to demonstrate that Congress's true intent differed from "that expressed in the plain meaning of the statute."[69] Second, NISH argued that *Chevron* deference requires a "[clear] textual commitment of authority" and that "the [RSA] does not grant the DOE authority to regulate military mess halls."[70] The court dismissed this argument, stating that it "did not believe the ramifications of bringing military mess halls within the purview of the [RSA] are so apparent that [the court] may impute to Congress an intention not to delegate this authority."[71]

The Relationship of the Blind Vendor Preference to Other Preferences

In addition to challenging the RSA's application to military mess halls, protesters have argued that even if the RSA does apply to such procurements, other set-aside programs have priority over the RSA preference. This section discusses litigation regarding the interrelationship of the RSA preference to the Javits Wagner O'Day Act (JWOD);[72] the Historically Underutilized Business Zone (HUBZone) Act;[73] the Small

62. *Id.* at *3.

63. *Rumsfeld I*, 188 F. Supp. 2d at 1324.

64. *NISH I*, 95 F. Supp. 2d at 505 (E.D. Va. 2000); NISH II, 247 F.3d 197, 202-06 (4th Cir. 2001).

65. *Rumsfeld I*, 188 F. Supp. 2d at 1327.

66. *Rumsfeld II*, 2003 U.S. App. LEXIS 23290, at *25. Essentially, NISH tried to parse the statutory definition of "procurement" according to the entity that ultimately receives the goods or services. NISH argued that "vending facilities provide goods and services to the general public, not to the federal government," *id.*; therefore, the government's contract for vending facilities was not an *acquisition* of goods and services.

67. *Id*. at *26-27 (citing *NISH II*, 247 F.3d at 204 (4th Cir. 2001)).

68. *Id*. at *10-11. Comically, to reach this "clear" expression of congressional intent, NISH implored the court to employ the relatively obscure Latin canons of construction *ejusdem generis* and *noscitur a sociis*. *See id*.; *see also* BLACK'S LAW DICTIONARY 535, 1084 (7th ed. 1999) (defining *ejusdem generis* as Latin for "of the same kind or class" and *noscitur a sociis* as Latin for "it is known by its associates").

69. *Rumsfeld II*, 2003 U.S. App. LEXIS 23290, at *14.

70. *Id.* at *17 (quoting Whitman v. American Trucking, 531 U.S. 457 (2001)).

71. *Id.* at *18.

72. 41 U.S.C. §§ 46-48c (2000).

Business preference; and the Small Disadvantaged Business 8(a) set-aside program.[74] As discussed below, the courts have interpreted the RSA to take precedence over all of these preferences.

Javits Wagner O'Day Act

The JWOD was enacted in 1971 to "provide training and employment opportunities for persons who are blind or have severe disabilities."[75] Under the Act, a committee representing JWOD interests annually publishes a procurement list that "consist[s] of commodities and services that it considers suitable for purchase by the government from qualified nonprofit agencies for the blind and disabled."[76] In general, the JWOD establishes the committee's list as a mandatory procurement source for the federal government.[77] Although both the JWOD and the RSA serve as preferences for the blind, the JWOD focuses on providing the blind and disabled with a "'sheltered' environment" to work, whereas the RSA extends to managerial opportunities.[78]

The *Code of Federal Regulations* designates NISH as the advocate for JWOD interests.[79] In *NISH v. Cohen*, although the mess hall replacement contract at Fort Lee was not yet on the JWOD procurement list, NISH "expressed interest" on behalf of certain non-profit agencies.[80] In *NISH v. Rumsfeld*, the services at the Kirtland dining hall had been on the JWOD procurement list and performed by JWOD contractors for several years.[81] Both cases required reconciliation of the two preferences.

In *NISH v. Cohen*, NISH argued that the JWOD applied to the procurement because the JWOD was an express exception to the CICA's full and open competition requirements, whereas the RSA was not. As discussed previously, this argument failed because the Fourth Circuit adopted a broad definition of procurement that encompassed the RSA.[82] The court, however, discussed the JWOD "absent the limitations imposed by the CICA."[83] The court recognized that both the RSA and JWOD applied to the procurement, but the RSA controlled because "[it] is a 'specific statute closely applicable to the substance of the controversy at hand'": the operation of cafeterias.[84] In comparison, "the JWOD Act is a general procurement statute."[85]

In *NISH v. Rumsfeld*, the Tenth Circuit adopted the Fourth Circuit's rationale. Although the Tenth Circuit recognized that the RSA and JWOD could co-exist under limited circumstances, the court determined it must decide which Act took

73. 15 U.S.C. § 632.

74. *See* 13 C.F.R. § 121.105(a) (LEXIS 2004).

75. NISH II, 247 F.3d 197, 201 (4th Cir. 2001) (citing Barrier Indus. v. Eckard, 584 F.2d 1074, 1076 (D.C. Cir. 1978)).

76. *Id.* (citing 41 U.S.C. § 47(a)(1)).

77. *Id.* (citing 41 U.S.C. § 47(d)).

78. *Id*. In a nutshell, the JWOD defines its preference in terms of "direct labor" performed by blind individuals, whereas the RSA extends the blind vendor preference to all facets of the "operation" of vending facilities, to include supervision and management. *Compare* 41 U.S.C. § 47(b)(3)(C), (b)(5) (JWOD), *with* 20 U.S.C. § 107(a) (RSA).

The JWOD establishes a preference for commodities and services provided by "qualified non-profit agencies for the blind." 41 U.S.C. § 47(a). The JWOD defines a "qualified non-profit agency for the blind" as an agency "which in the production of commodities and in the provision of services . . . employs blind individuals for [not lest than 75%] of *direct labor* required for the production or provision of the commodities or services." *Id.* § 48b(3)(C) (emphasis added). In defining what constitutes "direct labor," the JWOD explicitly excludes "supervision, administration, inspection, or shipping." *Id*. § 48b(5). In comparison, the RSA preference extends to the "operation of vending facilities by licensed blind vendors." 20 U.S.C. § 107(a). The term "operation" includes management and supervisory facets of employment in addition to direct labor. *See NISH II*, 247 F.3d at 201 (stating that the RSA "takes a slightly different tack [from the JWOD] by encouraging blind persons to be entrepreneurial and to run their own businesses"). Further, the RSA preference extends directly to blind persons (licensed by their respective state licensing agencies); unlike the JWOD, the RSA does not employ a "qualified non-profit agency for the blind" as a middle man when exercising the preference. *See* 20 U.S.C. § 107(a).

79. *See* 41 C.F.R. § 51-3.1 (LEXIS 2004).

80. *NISH II*, 247 F.3d at 199.

81. Rumsfeld I, 188 F. Supp. 1321, 1324 (D.N.M. 2002).

82. *See supra* note 55 and accompanying text.

83. *NISH II*, 247 F.3d at 205.

84. *Id.*

85. *Id.*

precedence. The Tenth Circuit found the RSA controls because "it is a general maxim of statutory interpretation that a statute of specific intention takes precedence over one of general intention."[86]

As one commentator observed, "[g]iven that the facts, rationale, and holdings of *NISH v. Cohen* and *NISH v. Rumsfeld* were strikingly similar, RSA and JWOD proponents may have fought their last round of food fights."[87] JWOD proponents, however, effectively moved their food fights from the court room to the floors of Congress. Section 852 of the National Defense Authorization Act (NDAA) for Fiscal Year 2004, signed by President Bush on 24 November 2003, stabilizes certain existing military mess hall contracts, thus preserving the JWOD preference.[88] Entitled "Contracting With Employers of Persons With Disabilities,"[89] Section 852 renders the RSA inapplicable to current JWOD contracts for "the operation of a military mess hall, military troop dining facility, or any similar dining facility operated for the purpose of providing meals to members of the Armed Forces."[90] Notably, JWOD proponents achieved a limited victory: the reprieve applies only to JWOD contracts and the options provided under those contracts "entered into before the date of the enactment of the [NDAA]; and . . . in effect on [that] date."[91] Consequently, the RSA provisions in the 2004 NDAA do not affect contracts entered on the date of enactment of the NDAA and thereafter.[92]

HUBZone Act

The Historically Underutilized Business Zone (HUBZone) Act was passed in 1997 "to provide federal contracting assistance for qualified small business concerns located in historically underutilized business zones in an effort to increase employment opportunities."[93] Among the methods available to assist qualified HUBZone small business concerns (SBCs) is the requirement for "contracting officer[s] to provide HUBZone [SBCs] a price evaluation preference by adding a factor of 10% to all [other] offers."[94]

In *Automated Communications Systems, Inc. v. United States* (2001),[95] ACSI, a HUBZone SBC, protested the application of the RSA blind vendor preference to a full food services procurement at Lackland Air Force Base.[96] ACSI claimed that the government "eliminated the [HUBZone] preference for which ACSI applies by applying the [RSA blind vendor preference] without limitation."[97] Consequently, ACSI demanded that the Air Force waive the RSA preference under the authority of FAR section 1.403.[98]

The Court of Federal Claims (COFC) disagreed with ACSI's premise, determining that the two preferences were not incompatible. Specifically, the COFC agreed with the government that the procurement agency could give both preferences "full effect": the agency could accord all qualified HUBZone SBCs their price evaluation preference, then the agency could apply the RSA blind vendor preference if any SLA proposal fell within the competitive range. Furthermore, the COFC followed the logic of the Fourth and Tenth Circuits: if the prefer-

86. Rumsfeld II, 2003 U.S. App. LEXIS 23290, at *4 (10th Cir. Nov. 14, 2003).

87. Major Tom Modeszto, *RSA Continues to Score Knockouts*, *in* Major Tom Modeszto et al., *Contract and Fiscal Law Developments of 2002—The Year in Review*, ARMY LAW., Jan./Feb. 2003, at 77. Although this comment preceded the appellate court's decision in *NISH v. Rumsfeld*, the Tenth Circuit's decision further strengthens Major Modeszto's observation.

88. H.R. 1588, 108th Cong. (2003) (enacted).

89. The title for the initial Senate version of Section 852 (then Section 368) more explicitly described Congress's motivation for the legislation: "Stability of Certain Existing Military Troop Dining Facilities Contracts." NATIONAL DEFENSE AUTHORIZATION ACT FOR FISCAL YEAR 2004, S. REP. NO. 108-046 (2003).

90. H.R. 1588 § 852(b).

91. *Id.*

92. *See id.*

93. 13 C.F.R. § 126.100 (LEXIS 2004).

94. *Id.* § 19.1307(b).

95. 49 Fed. Cl. 570 (2001).

96. *Id.* at 571.

97. *Id.* at 574.

98. *Id.* at 578. Section 1.403 of the FAR authorizes agency heads to deviate from the FAR subject to the policy restrictions of FAR section 1.402. *See* FAR, *supra* note 47, at 1.402-.403. Because the COFC "conclude[d] that the proposed procurement properly adhered to *DoDD 1125.3* and the RSA, [the court determined] it [was] not necessary to examine the reach of FAR 1.403." *Automated Communications Sys., Inc.*, 49 Fed. Cl. at 578-79.

ences conflicted, the more specific preference, the RSA, would control.[99]

Small Business and Small Disadvantaged Business 8(a) Set-Aside Programs

Congress enacted the Small Business Act[100] to "[p]lace a fair proportion of acquisitions with small business concerns" and to "[p]romote maximum subcontracting opportunit[ies] for small businesses."[101] Section 8(a) of the Act provides additional benefits for those small businesses predominantly owned or operated by socially and economically disadvantaged individuals.[102] For procurements that exceed $100,000, the FAR *mandates* that the contracting officer set aside the acquisition for a small business if "[1] the contracting officer reasonably expects to receive offers from two or more responsible small businesses; and [2] award will be made at a fair market price."[103] For small disadvantaged businesses, the FAR *permits* contracting officers to set aside contracts for eligible 8(a) firms.[104]

In *In re Intermark, Inc.* (2002),[105] the Army initially offered a mess hall services contract at Fort Rucker, Alabama, as a regular small business set-aside. Subsequently, the Alabama SLA expressed interest in the contract. Because the agency determined the SLA was not a small business, and therefore could not compete for the contract as currently solicited, it withdrew the initial solicitation and re-solicited the contract on an unrestricted basis. Intermark, a small business and the incumbent contractor, protested the withdrawal of the initial solicitation. Intermark argued that because the contracting officer had determined that the procurement met the conditions for a small business set-aside, the FAR mandated setting the acquisition aside.[106]

The Comptroller General agreed with Intermark that the agency had no basis to withdraw the small business set-aside.[107] Much to Intermark's chagrin, however, the Comptroller General did not find that the FAR thus mandated awarding the contract to a small business. Instead, the Comptroller General adopted the rationale of *Automated Communications*. He determined (1) that the RSA preference had priority over the small business preference; and (2) that the "solicitation [could] be fashioned in such a way to accommodate both preferences."[108] Accordingly, the Comptroller General opined that the solicitation could encompass a "'cascading' set of priorities . . . whereby competition is limited to small business concerns and the SLA, with the SLA receiving award if . . . within the competitive range . . . ; otherwise, award will be made to an eligible small business."[109]

The Comptroller General distinguished *Intermark* from the earlier Comptroller General decision, *U.S. Department of the Air Force—Reconsideration* (*Keesler*).[110] In *Keesler*, the Air Force withdrew an 8(a) set-aside solicitation "for the purpose of reissuing the solicitation on an unrestricted basis to comply with the [RSA]."[111] The Comptroller General held that the withdrawal of the solicitation in *Keesler* was permissible

---

99. *Automated Communications Sys., Inc*., 49 Fed. Cl. at 577-78.

100. Pub. L. No. 85-836, 72 Stat. 384 (1958) (codified as amended at 15 U.S.C. §§ 631-650 (2000)).

101. CONTRACT LAW DESKBOOK, *supra* note 19, at 10-1 (construing Small Business Act § 2, 72 Stat. at 384).

102. 15 U.S.C. § 637(a); *see* 13 C.F.R. §§ 124.102-.104 (LEXIS 2004).

103. FAR, *supra* note 47, at 19.502-2(b).

104. *Id.* subpt. 19.8.

105. B-290925, 2002 Comp. Gen. LEXIS 167 (Oct. 23, 2002).

106. *Id.* at *3-4.

107. *Id.* at *4.

108. *Id.*

109. *Id.* at *6-7. The COFC's decision in *North Carolina Division of Services for the Blind v. United States* (*NCDSB*), 53 Fed. Cl. 147 (2002), is in accord with the "cascading" priorities in *Intermark*. *NCDSB* involved a full food and attendant services contract for the mess halls at Fort Bragg, North Carolina. *Id*. at 149. The contracting officer determined that the RSA did not apply to the contract and issued the solicitation as a small business set-aside. *Id*. at 154. The North Carolina SLA, NCDSB, submitted a proposal that the contracting officer subsequently determined was outside the competitive range. *Id*. at 153. Thus, Fort Bragg awarded the contract to a small business. *See id*.

Post-award, the NCDSB protested the solicitation, arguing that the contracting officer should have applied the RSA preference. *Id*. at 156. The COFC sided with the government, finding that NCDSB lacked standing: NCDSB was not an "interested party" because even if the Army had applied the RSA preference, NCDSB would not have had a substantial chance to receive award of the contract because it was outside the competitive range. Consequently, the COFC did not need to decide whether the RSA applied to the Fort Bragg procurement. *Id.*

110. B-250465.6, B-250465.7, B-250783.2, 1993 U.S. Comp. Gen. LEXIS 530 (June 4, 1993).

because, in contrast to the regular small business set-aside present in *Intermark*, the 8(a) set-aside was not mandatory.[112] Thus, the agency in *Keesler* had no obligation to set aside the procurement in the first place.

In dicta, the Comptroller General pointed out a problem with the COFC's logic in *Automated Communications*. As the Comptroller General noted, giving HUBZone SBCs their ten-percent evaluation preference could potentially "affect the ability of the SLA proposal to be included in the competitive range."[113] Such circumstances would prevent the contracting agency from giving "full effect" to the RSA preference. The Comptroller General, however, did not address the weakness of his own proposal: it does not distinguish between small and large blind vendor businesses, thus according the former no advantage.

The Scope of the Blind Vendor Preference

In addition to the above areas of litigation, the blind vendor program has also raised disputes regarding the scope of the priority. As discussed previously, the RSA preference is not without limits; the SLA's offer must be within the competitive range. Several cases discussed below explore the definition of competitive range and the contracting officer's discretion when evaluating SLA proposals in the RSA context. Further, the RSA preference only applies to the "operation" of vending facilities. *Washington State Department of Services for the Blind v. United States*[114] teaches that a contracting officer may correctly determine that certain military mess hall contracts, such as dining facility attendant services contracts, fall outside the RSA's penumbra, so long as the contracting officer's decision is not "arbitrary, capricious, or otherwise not in accordance with the law."[115]

Competitive Range

Southfork Systems v. United States[116]

In *Southfork Systems* (1998), Southfork, the incumbent operator of cafeteria services at Lackland Air Force Base, Texas, protested the government's pre-award decision to include the state SLA's proposal within the procurement's competitive range.[117] Among its claims, Southfork argued (1) that the Air Force should have excluded the SLA's proposal because "it failed to satisfy criteria in the [s]olicitation . . . directed to compliance with the RSA"; and (2) that in considering the SLA's proposal, the Air Force "misapplied [the] evaluation criteria in the [s]olicitation."[118] Specifically, Southfork argued that the SLA's proposal, which contemplated the use of a non-blind subcontractor to provide the blind cafeteria manager with training and experience, failed to satisfy how it would "[enlarge] economic opportunities for the blind."[119] Further, Southfork argued that the Air Force did not evaluate the SLA's proposal consistently with other offers because it had rejected another offer that did not meet the solicitation's management experience criteria.[120]

On appeal from the COFC, the Court of Appeals for the Federal Circuit (CAFC) affirmed the COFC's finding "that it could see no defect in the [SLA's] proposal or in the manner in which it was evaluated by the [g]overnment."[121] The CAFC noted the contracting officer's broad discretion when establishing the competitive range and in applying evaluation criteria.[122] Regarding RSA compliance, the CAFC stated that for the Air Force to have excluded the proposal on such grounds, it would have had to "reject out-of hand" the proposition that the employment of a single blind cafeteria manager could enhance the economic opportunities for the blind. "Such a choice," opined the CAFC, "was well within the discretion of the . . . contracting officer."[123] Regarding the consistency of criteria application, the CAFC determined that "the contracting officer had broad discretion to consider each factor [, including management experience,] as part of the totality of the circum-

111. *Id.* at *3.

112. *In re Intermark*, 2002 Comp. Gen. LEXIS 167, at *7.

113. *Id.* at *8 n.2.

114. 2003 U.S. Claims LEXIS 381 (Fed. Cl. Dec. 17, 2003).

115. *Id*. at *55; *see infra* notes 137-40 and accompanying text.

116. 141 F.3d 1124 (Fed. Cir. 1998).

117. *Id.* at 1127.

118. *Id*. at 1132-33.

119. *Id*. at 1138.

120. *Id.*

121. *Id.* at 1135.

stances, . . . [and] Southfork [failed to show] that the contracting officer abused that discretion."[124]

North Carolina Division of Services for the Blind v. United States[125]

In *North Carolina Division of Services for the Blind v. United States* (*NCDSB*) (2002), the contracting officer determined that the proposal from North Carolina's SLA, NCDSB, fell outside the competitive range for a full food and attendant dining services contract at Fort Bragg, North Carolina.[126] In making this determination, the contracting officer established the competitive range in accordance with FAR section 15.306, which provides that "the contracting officer may limit the number of proposals in the competitive range to the greatest number that will permit an efficient competition among the most highly rated proposals."[127] Among its protests, NCDSB argued that the RSA competitive range as defined by DOE's implementing regulations is much broader than the FAR currently provides.[128] According to NCDSB, agencies soliciting a vending facility contract must evaluate proposals in accordance with the definition of competitive range prevailing at the RSA's inception; that is, "a proposal must be regarded as being in the competitive range unless it is so deficient or out of line in price as to preclude further meaningful negotiations."[129]

Adoption of NCDSB's argument would significantly impact the contracting community. The broader the competitive range, the more likely an SLA's offer will fall into that range. Further, if an SLA's offer falls within the competitive range, the DOE's implementing regulations require the contracting agency to award the contract to the SLA.[130] Consequently, under NCDSB's rationale, SLAs may receive award for contracts they would otherwise not receive under application of FAR section 15.306.

The COFC held against NCDSB. Citing Cibinic and Nash's treatise *Formation on Government Contracts*,[131] the COFC recognized that the government's definition of competitive range had narrowed since the enactment of the RSA. The court found, however, that "[t]here is no precedent to support [NCDSB's] argument that the [RSA] regulations require the application of a competitive range definition that is different from that typically used in federal procurement law today [FAR § 15.306(c)(1)]."[132] The COFC, upholding the government's actions, determined that the contracting officer had correctly followed the FAR's provisions.[133]

Oklahoma v. Oklahoma Department of Rehabilitative Services[134]

Southfork and *NCDSB* both illustrate the great discretion contracting officers hold when determining the competitive range for a procurement. In contrast, *Oklahoma Services* (1998) illustrates that contracting officer discretion has its limits. In *Oklahoma Services*, the Oklahoma SLA submitted a proposal for a food services contract at Fort Sill, Oklahoma, that the contracting officer determined was within the competitive range along with five other offerors.[135] Subsequently, "written discussions ensued, and the [SLA and other offerors were]

122. *Id.* at 1138. For a recent GAO opinion describing the contractor's "broad discretion" when determining the competitive range, see Cantu Servs., Inc., Comp. Gen. B-289666.2, B-289666.3, Nov. 1, 2002, 2002 CPD ¶ 189, *described in* Major Steven Patoir, *The RSA's Preference for the Blind Wields a Visible Presence*, *in* Major Kevin Huyser et al., *Contract and Fiscal Law Developments of 2003—The Year in Review*, ARMY LAW., Jan. 2004, at 69-70.

123. *Southfork Sys.*, 141 F.3d at 1138.

124. *Id*. at 1139.

125. 53 Fed. Cl. 147 (2002).

126. *Id.* at 149.

127. FAR, *supra* note 47, at 15.306, *cited in NCDSB*, 53 Fed. Cl. at 166.

128. *NCDSB*, 53 Fed. Cl. at 166 (plaintiff's reply at 8 (quoting CACI Field Servs., Inc. v. United States, 13 Cl. Ct. 718 (1987))).

129. *Id.*

130. 34 C.F.R. § 395.33 (LEXIS 2004). Mandatory award to the SLA is subject to limited exceptions. The contracting officer may award to other than the SLA if he determines that award to the SLA would "adversely affect the interests of the United States" or that "the blind vendor does not have the capacity to operate a cafeteria in such a manner as to provide food service at a comparable cost and of comparable high quality as that available from other providers of cafeteria services." 32 C.F.R. § 260.3(g)(1)(ii) (LEXIS 2004). Such action requires the Secretary of Education's approval. *Id.*

131. JOHN CIBINIC, JR. & RALPH C. NASH, JR., FORMATION OF GOVERNMENT CONTRACTS 869 (3d ed. 1998).

132. *NCDSB*, 53 Fed. Cl. at 167.

133. *Id*.

134. 1998 U.S. Dist. LEXIS 23041 (W.D. Okla. Jan. 7, 1998).

asked to submit [their] best and final offers [BAFO]."[136] The contracting officer evaluated the SLA's BAFO lower than other BAFOs he received. Consequently, the contracting officer removed the SLA's bid from the competitive range because he determined the SLA had no chance of reasonably being awarded the contract.[137]

The District Court for the Western District of Oklahoma granted summary judgment for the SLA, determining that no authority supported the government's removal of the SLA's bid from the competitive range without prior consultation with the DOE.[138] The district court reasoned that the SLA's inclusion within the initial competitive range, and subsequent request for the SLA's BAFO, implied that the SLA's offer had a reasonable chance of receiving award. Consequently, the RSA regulations required the agency to consult with the DOE before removing the SLA from the competitive range.[139]

Application of the RSA to Dining Facility Attendant Services Contracts

In *Washington State Department of Services for the Blind* (*WSDSB*) *v. United States* (2003),[140] Washington's SLA, WSDSB, challenged Fort Lewis's decision not to apply the RSA preference to a dining facilities attendant [DFA] services contract. Under a DFA services contract, "military personnel cook the food in a mess hall, but an outside contractor provides other services, such as washing dishes."[141] In contrast to a full food services contract offered at the same time, the contracting officer determined that the RSA did not apply to the DFA contract.[142]

The issue in *WSDSB* turned on "whether the term 'operation of a vending facility' requires the application of the RSA to a DFA services contract."[143] As an initial matter, the COFC denied WSDSB's assertion that the DOE had primary jurisdiction to resolve this question. The COFC determined that this question was "a matter of statutory interpretation that [fell] within the [COFC's] conventional wisdom."[144] Subsequent to a mind-numbing exposition on the taxonomy of the term "operation,"[145] the COFC held for the government: the "[contracting officer's] interpretation of the term 'operation' of a vending facility' [was] not 'arbitrary, capricious, or otherwise not in accordance with law.'"[146]

Military Mess Hall Litigation in Light of the 2004 NDAA

As previously discussed,[147] Congress addressed the application of the RSA to military mess halls in the 2004 National Defense Authorization Act (NDAA).[148] Section 852 of the Act specifies that certain JWOD contracts are immune from the RSA:

> (a) *Inapplicability of the* [*RSA*]—The [RSA] does not apply to any contract described in subsection (b) for so long as the contract is in

135. *Id.* at *2-3.

136. *Id*. at *11.

137. *Id.* at *4-6. Before eliminating the SLA from the competitive range, the contracting officer asked counsel for advice on the matter. The contracting officer "felt that prior approval from the Secretary of Education was required." *Id*. at *4. The agency's counsel advised the contracting officer that such approval was unnecessary. *Id*. at *3-4. The opinion gives no further detail on counsel's rationale for this "advice."

138. *Id.* at *6.

139. *Id.* at *11.

140. 2003 U.S. Claims LEXIS 381 (Fed. Cl. Dec. 17, 2003).

141. *Id.* at *2.

142. *Id.* at *5 n.4.

143. *Id*. at *20.

144. *Id*. at *19-20. Fort Lewis initially solicited its mess hall contract such that it included both full food and DFA services. Upon request from the WSDSB, the DOE opined that the RSA applied to the solicitation. Consequently, Fort Lewis bifurcated its procurement into a full food services contract and a DFA services contract. The contracting officer determined that the RSA applied to the full food services contract, but not to the DFA services contract. *Id*. at *3-5. The WSDSB sought review again from the DOE for the re-solicitation of the DFA services contract, claiming the DOE had primary jurisdiction, but the COFC denied this claim. *Id*. at *19-20.

145. *See id.* at *55.

146. *Id*. (quoting 5 U.S.C. § 706(2)(A) (2000)).

147. *See supra* notes 88-92 and accompanying text.

148. *See* H.R. 1588, 108th Cong. (2003) (enacted).

effect, including for any period for which the contract is extended pursuant to an option provided in the contract.

(b) [*JWOD*] *Contracts*—Subsection (a) applies to any contract for the operation of a military mess hall, military troop dining facility, or any similar dining facility operated for the purpose of providing meals to members of the Armed Forces that—

(1) was entered into before the date of the enactment of [the 2004 NDAA] with a nonprofit agency for the blind or an agency for the other severely handicapped in compliance with [JWOD § 3] and

(2) is in effect on such date.[149]

By its express provisions, Section 852 provides a narrow window that preserves certain existing JWOD contracts—the Act has no prospective effect.[150]

Perhaps of greater significance, however, are the implications of Section 852 on future military mess hall litigation. As discussed throughout this article, military mess hall litigation has proceeded along three fronts: (1) whether the RSA applies to military mess halls in the first place; (2) the relationship of the RSA to other set-asides; and (3) the scope of the blind vendor preference. Section 852 affects each of these areas.

Foremost, the NDAA for FY 2004 resolved whatever slim doubt remained about the direct application of the RSA to military mess halls following *NISH v. Cohen* and *NISH v. Rumsfeld*.[151] By creating an exemption from the RSA provisions for mess hall contracts, Congress implied the premise that the RSA applies to such contracts. Similarly, by creating an exemption that elevates the JWOD preference over the RSA, Congress implied that absent such an exemption, the RSA preference is superior. This logic extends to the other preferences (e.g., small business, HUBZone) and supports the courts' statutory maxim: when two preferences are applicable, the more specific controls.[152] Consequently, future military mess hall litigation will occur on the remaining area of dispute—the scope of the blind vendor preference.

Conclusion

Given the large values of the contracts involved and the tendency for the RSA preference to unseat the beneficiaries of other procurement preference programs, litigation over military mess hall contracts will continue. In light of the federal opinions and the express and implied provisions of the NDAA for FY 2004,[153] it is clear (1) that the RSA applies to contracts for the operation of military mess halls; and (2) that the RSA is superior to other less specific set-aside programs. Thus, protesters will focus their arguments on the third litigation area discussed above, the scope of the blind vendor preference.

Litigants have probed the RSA scope in disputes concerning (1) various aspects of competitive range; and (2) the applicability of the RSA to dining facility attendant services contracts. According to the above cases, so long as the contracting officer follows the FAR provisions for establishing a competitive range and evaluating proposals, the procurement should not be in jeopardy. In this regard, agencies should read *Southfork Systems*, which reprints the pertinent RSA preference and evaluation criteria in the agency solicitation.[154] Once the contracting officer determines an SLA proposal falls within the competitive range, however, he does not have the discretion to remove that proposal from the range absent the approval of the Secretary of Education.[155]

Finally, *WSDSB* teaches that an agency enjoys some discretion when interpreting what the RSA's provision "operate a vending facility" entails.[156] Agencies that consider *WSDSB* as a green light to exclude DFA services contracts from the RSA, however, should proceed with caution. The case was only at the district court level, and the district court narrowed its holding to the facts of the case.

---

149. *Id.*

150. *See id*.

151. *See supra* note 87 and accompanying text.

152. *See, e.g*., Rumsfeld II, 2003 U.S. App. LEXIS 23290, at *4 (10th Cir. Nov. 14, 2003).

153. *See supra* notes 148-52.

154. *See generally* Southfork Sys. v. United States, 141 F.3d 1124 (Fed. Cir. 1998).

155. Oklahoma v. Oklahoma Dep't of Rehabilitative Servs., 1998 U.S. Dist. LEXIS 23041, at *11 (W.D. Okla. Jan. 7, 1998).

156. *See generally* Washington State Dep't of Servs. for the Blind v. United States, 2003 U.S. Claims LEXIS 381 (Fed. Cl. Dec. 17, 2003).

The Boeing Suspension: Has Increased Consolidation Tied the Department of Defense's Hands?

Major Jennifer S. Zucker[1]

Introduction

> *For the federal government to continue to do business with a private company that has a documented record of defrauding the government and abusing taxpayer money is unconscionable.*
>
> *-Congressman Bob Barr (R-GA), 23 August 2001*

Perhaps the greatest threat to a government contractor following the discovery of an employee's bad act or omission is the possibility of the company's suspension or debarment. The prospect of being barred from future work or the rescission of current contracts is a serious one. When a contractor is suspended or debarred, society often perceives the contractor as corrupt and the consequence as punishment. But suspension and debarment are not imposed for purposes of punishment. Instead, they are administrative remedies that permit agencies to exclude contractors from federal procurements and nonprocurement programs when necessary to protect the government's interest and to ensure compliance with statutory goals.[2] The goal is to maintain the integrity of the procurement system, to spend taxpayers' dollars wisely, and to ensure that contractors act properly.

To these ends, the *Federal Acquisition Regulation* (*FAR*) requires contracting officers to make an affirmative determination of responsibility before any federal purchase or award.[3] Responsibility spans a number of factors including the contractor's record of performance, integrity, and business ethics.[4] Suspension and debarment decisions are merely "the final straw in the examination of responsibility issues,"[5] and focus on whether the contractor acted responsibly and whether it is presently responsible.[6] Such decisions frequently require an agency debarring official to examine such factors as contractor integrity and honesty; the quality and reliability of the items supplied; the risk of harm to the soldier or citizen; the impact of exclusion from future procurements; and other contract-performance related issues. Debarring officials must also determine whether the conduct of a contractor's employee or subcontractor should be imputed to the contractor. Finally, even if a contractor is suspended or debarred, those exclusions may be waived when compelling reasons exist, such as a lack of alternate sources, meeting urgent needs, or national defense requirements.[7]

In July 2003, the Air Force (AF) suspended three of Boeing's Integrated Defense System business units[8] and three of its former employees.[9] The suspensions were based on an AF investigation which concluded that Boeing committed serious violations of the law.[10] According to a Department of Justice

---

1. Judge Advocate, U.S. Army. Presently assigned as a Trial Attorney, Contract Appeals Division, U.S. Army Legal Services Agency, Arlington, Virginia. This article was submitted to partially satisfy the requirements of an LL.M. degree at The George Washington University Law School. The opinions and conclusions represented in this article are solely those of the author, and do not necessarily represent the views of the Department of Defense, the Department of the Army, the Army Judge Advocate General, or any governmental agency.

2. General Servs. Admin. et al., Federal Acquisition Reg. 9.402 (July 2003), *available at* http://www.arnet.gov/far/ [hereinafter FAR] (noting that the on-line version includes amendments from Federal Acquisition Circular (FAC) 19 (Jan. 1, 2004) and FAC 18 (Jan. 12, 2004)).

3. *Id.* at 9.103.

4. *Id.* at 9.104-1.

5. Steven L. Schooner, The Paper Tiger Stirs: Rethinking Suspension and Debarment, Paper Prepared for Delivery Before the George Washington Law School Government Procurement Law Program and the Federal Acquisition Institute Colloquium on Suspension and Debarment: Emerging Issues (Nov. 20, 2003) *in* L. & Pol'y, Nov. 20, 2003, at 3.

6. *See generally* FAR, *supra* note 2, at 9.4.

7. *See* U.S. Dep't of Defense, Defense Federal Acquisition Reg. Supp. 209.405(a)(i)-(iv) (July 2002); *see also* FAR, *supra* note 2, at 9.405, 9.405-1, 9.405-1(b), 9.405-2, 9.406-1(c), 9.407-1(d), 23.506(e) (noting that FAR 9.405-1(b) was amended on 12 Jan. 2004, to require the agency head to make a written determination of compelling reasons before placing orders under existing contracts with contractors that have been debarred, suspended, or proposed for debarment.); *see also* National Aeronautics and Space Administration; Debarment and Suspension–Order Placement and Option Exercise, 67 Fed. Reg. 67,282 (proposed Nov. 4, 2002) (to be codified at 48 C.F.R. pt. 9) (stating that the deletion "of" "or a designee" from the phrase "agency head or designee" does not signify a change in policy, but implements the FAR convention at FAR 1.108(b) that each authority is delegable unless specifically stated otherwise").

8. Press Release, U.S. AF, U.S. AF Announces Boeing EELV Inquiry Results (July 25, 2003), *available at* http://www.af.mil/stories/story.asp?storyID=123005322 [hereinafter AF Press Release, U.S. Air Force Announces Boeing EELV Inquiry Results]. The suspended units were The Boeing Company, Launch Systems; The Boeing Company, Boeing Launch Service; and The Boeing Company, Delta Programs. *Id.*

(DOJ) press release issued in connection with its criminal case: (1) Boeing possessed an extraordinary amount of rival Lockheed Martin Corporation's (Lockheed Martin) proprietary data during the 1998 Evolved Expendable Launch Vehicle (EELV)[11] competition; (2) the data was capable of providing great insight into Lockheed Martin's cost and pricing; and (3) Boeing failed to disclose to the AF the full extent of the data in its possession for approximately four years.[12]

The Boeing suspension sent a message throughout the procurement community that large defense contractors are not immune from suspension or debarment; previously, interest groups had argued that such companies, were in practice, immune.[13] When Boeing's suspension was twice lifted to allow it to receive awards,[14] interest groups then argued that such action seriously eroded any deterrent effect of the AF's suspension.[15] This conclusion is understandable but it is mistaken. The drastic consolidation of the defense industry over the last decade makes it difficult, but not impossible, to impose a suspension or debarment on mega-defense contractors, like Boeing, Lockheed Martin, or Raytheon.[16] When considering such action, agencies must consider not only the traditional mitigating factors,[17] but also the harsh reality that the exclusion may ultimately be waived, by necessity, if there are no other viable sources.

Continued consolidation of the defense industry poses difficult problems for suspension and debarment officials. This article sets forth the basis and procedural requirements for imposing a suspension or debarment, and the factual basis for the AF's suspension of Boeing. Next, this article examines the problem of using the traditional suspension and debarment remedies to exclude large defense contractors, and then discusses a new approach for crafting remedies aimed at developing alternative sources, when agencies foresee continued business dealings with mega-defense contractors.

Suspension and Debarment

Background

Overview of Procurement Regulations

Federal Acquisition Regulation 9.103 requires contracting officers to make a determination of responsibility before making any purchase or award.[18] Some of the standards listed for consideration are unique to the needs of a particular procurement, such as having the necessary production equipment or meeting a required delivery schedule.[19] Other standards apply to all contracts like having "a satisfactory record of integrity and business ethics."[20] When a contracting officer determines that a contractor is "nonresponsible" that determination applies

9. Matt Kelley, *Air Force Retracts $1B Boeing Deal on Federal Law Violations*, TECHNEWS.COM, July 24, 2003 (reporting that those individuals are Kenneth Branch, William Erskine, and Larry Satchell).

10. AF Press Release, U.S. Air Force Announces Boeing EELV Inquiry Results, *supra* note 8.

11. The EELV is not a government-owned weapon system. Under the EELV Program, discussed below, the AF procured developmental contracts for commercially owned rocket systems including launch capabilities, and then awarded separate launch service contracts—the Buy I and Buy II—to send government satellites into space. *See generally* The U.S. Air Force Evolved Expandable Vehicle Launch System Program Office Homepage, *Introduction to EELV Brief*, *available at* http://www.losangeles.af.mil/smc/mv/intro_files/public/eelv_intro_brief.pdf (last visited Mar. 30, 2004) [hereinafter *EELV Brief*].

12. Press Release, DOJ, Two Former Boeing Managers Charged in Plot to Steal Trade Secrets from Lockheed Martin (June 25, 2003), *available at* http://www.usdoj.gov/criminal/cybercrime/branchCharge.htm [hereinafter DOJ Press Release].

13. Danielle Brian, Contractor Debarment and Suspension: A Broken System, Address Prepared for Delivery Before the George Washington Law School Government Procurement Law Program and the Federal Acquisition Institute Colloquium on Suspension and Debarment: Emerging Issues (Nov. 20, 2003) *in* L. & POL'Y (submitted on Nov. 20, 2003), *available at* http://www.pogo.org/p/contracts/ct-031101-debarment.html (criticizing the government's system for debarring and suspending large contractors).

14. *Id*.; *see* Renae Merle, *Boeing Gets Waiver From Air Force*, WASH. POST, Aug. 30, 2003, at E1 [hereinafter Merle, *Boeing Gets Waiver From Air Force*] (reporting on the AF waiver and award to The Boeing Co. of a $56.7 million contract to deploy a Delta II rocket carrying the Global Positioning Satellite (GPS-IIR-10) system); *see also* Renae Merle, *Suspension Doesn't Stop Boeing: The Contract to Build a Spy Satellite Comes After Boeing Was Punished for Breaking Federal Laws in 1998*, WASH. POST, Oct. 1, 2003 [hereinafter Merle, *Suspension Doesn't Stop Boeing*] (reporting on second waiver and award to Boeing of a contract for the launch of a spy satellite).

15. Brian, *supra* note 13.

16. GEN. ACCT. OFF., REP. NO. GAO/NSIAD-98-141, *Defense Industry: Consolidation and Options for Preserving Competition* (Apr. 1, 1998), *available at* http://www.fas.org/man/gao/nsiad98141.htm [hereinafter GAO REP. NO. GAO/NSIAD-98-141] (reporting that as of 1998, these three large firms "receive a substantial portion of what DOD spends annually to acquire its major weapons and other products").

17. *See* FAR, *supra* note 2, at 9.406-1 (discussed below).

18. *Id.* at 9.103.

19. *Id.* at 9.104-1.

only to that particular award.[21] In such cases, the contractor is free to compete for other awards.

By contrast, the sanctions imposed under *FAR Subpart 9.4* that govern suspension, debarment, and ineligibility, exclude the contractor from all federal procurement and nonprocurement programs unless the agency head determines that there is a compelling reason for such action.[22] The *FAR* grants agency heads broad discretion in pursuing their mandate.[23] If more than one agency has an interest in the suspension or debarment decision, the *FAR* recommends that one agency be designated as the lead agency.[24]

In many respects, suspensions are similar to debarments.[25] The main differences between the two lie not in the causes, but in the (1) procedures (suspensions may be imposed without prior notification to the contractor); (2) burden of proof (suspensions may be based on an indictment for criminal or civil violations or on adequate evidence[26] of the same); and (3) period of exclusion (suspensions are temporary, whereas debarments are for fixed periods, generally not to exceed three years).[27]

Causes and Procedures

The *FAR* requires each agency to establish procedures "for the prompt reporting, investigation, and referral to the debarring official of matters appropriate for that official's consideration."[28] But the mere existence of a cause for debarment "does not necessarily require that the contractor be debarred; the seriousness of the contractor's acts or omissions and any remedial measures or mitigating factors should be considered in making the debarment decision."[29] Debarring officials must first consider the following mitigating factors:

> (1) Whether the contractor had effective standards of conduct and internal control systems in place at the time of the activity which constitutes cause for debarment or had adopted such procedures prior to any [g]overnment investigation of the activity cited as a cause for debarment.
>
> (2) Whether the contractor brought the activity cited as a cause for debarment to the attention of the appropriate [g]overnment agency in a timely manner.
>
> (3) Whether the contractor has fully investigated the circumstances surrounding the cause for debarment and, if so, made the result of the investigation available to the debarring official.
>
> (4) Whether the contractor cooperated fully with [g]overnment agencies during the investigation and any court or administrative action.
>
> (5) Whether the contractor has paid or has agreed to pay all criminal, civil, and administrative liability for the improper activity, including any investigative or administrative costs incurred by the [g]overnment, and has made or agreed to make full restitution.

---

20. *Id.*

21. *See generally id.* at 9.103; *see also id.* 9.104-3(d) ("If a small business concern's offer that would otherwise be accepted is to be rejected because of a determination of nonresponsibility, the contracting officer shall refer the matter to the Small Business Administration which will decide whether or not to issue a Certificate of Competency.").

22. When suspended or debarred, "agencies shall not solicit offers from, award contracts to, or consent to subcontracts with these contractors, unless an agency head determines that there is a compelling reason for such action." *Id.* at 9.405. Agency means "any executive department, military department or defense agency, or other agency or independent establishment of the executive branch." *Id.* Examples include the DOD, GSA, Social Security Administration, and the Internal Revenue Service. *Id.* at 9.403.

23. *Id.* at 9.402.

24. *Id.*

25. *Id.* at 9.407-2.

26. Adequate evidence means "information sufficient to support the reasonable belief that a particular act or omission has occurred." *Id.* at 2.101; *see also id.* at 9.403 (stating that an "information or other filing by competent authority charging a criminal offense is given the same effort as an indictment").

27. *Id.* at 9.407-4, 9.406-4. Since the same basic principles apply to both remedies, the discussion below generally refers only to debarments unless further distinction is necessary.

28. *Id.* at 9.406-3(a); *see also id.* at 9.407-3 (requiring agencies to establish procedures for the prompt reporting, investigation, and referral of appropriate matters to the suspending official); *see, e.g.*, U.S. DEP'T OF ARMY, REG. 27-40, LITIGATION ch. 8 (19 Sept. 1994) (effective date 19 Oct. 1994).

29. *See* FAR, *supra* note 2, at 9.406-1(a); *see also id.* at 9.407-1(b)(2) (containing a similar provision governing suspensions).

(6) Whether the contractor has taken appropriate disciplinary action against the individuals responsible for the activity which constitutes cause for debarment.

(7) Whether the contractor has implemented or agreed to implement remedial measures, including any identified by the [g]overnment.

(8) Whether the contractor has instituted or agreed to institute new or revised review and control procedures and ethics training programs.

(9) Whether the contractor has had adequate time to eliminate the circumstances within the contractor's organization that led to the cause for debarment.

(10) Whether the contractor's management recognizes and understands the seriousness of the misconduct giving rise to the cause for debarment and has implemented programs to prevent recurrence.[30]

Officials should also consider these factors (but are not required to) when weighing a possible suspension.[31]

The General Services Administration (GSA) compiles, maintains, and distributes a "List of Parties Excluded from Federal Procurement and Nonprocurement Programs."[32] The list contains the names, addresses, and identities of parties debarred, suspended, proposed for debarment, or declared ineligible by executive agencies (e.g., the Army) or the General Accounting Office (GAO).[33]

Debarment officials may predicate a debarment on criminal convictions or civil judgments for (1) fraud or a criminal offense related to the procurement or performance of a public contract;[34] (2) violations of federal or state antitrust laws;[35] (3) embezzlement, theft, forgery, bribery, falsification or destruction of records, false statements, tax evasion, or receiving stolen property;[36] (4) improperly affixing "Made in America" labels to foreign goods;[37] or (5) offenses indicating a lack of business integrity.[38] Debarment may also be grounded on a serious violation of contract terms or "any other cause of so serious or compelling a nature that it affects the present responsibility of the contractor or subcontractor."[39] To act on the latter, however, the "serious violation" or "other evidence" must be established by a preponderance of the evidence.[40] Further bases for debarment include unfair trade practices, violations of the Immigration and Nationality Act employment provisions, repeated unsatisfactory performance,[41] and violations of the Drug-Free Workplace Act of 1988.[42]

When proposing a debarment, agencies are required to notify contractors, and any specifically-named affiliates, of its reasons.[43] The contractor is then given thirty days to submit, in person, in writing, or through a representative, information and argument in opposition to the debarment.[44] If the action is not based on a criminal conviction or civil judgment, and the con-

30. *See* FAR, *supra* note 2, at 9.406-1.

31. *Id.* at 9.407-1(b)(2) provides in part:

> The existence of a cause for suspension does not necessarily require that the contractor be suspended. The suspending official should consider the seriousness of the contractor's acts or omissions and may, but it is not required to, consider remedial measures or mitigating factors, such as those set forth in 9.406-1(a). A contractor has the burden of promptly presenting to the suspending official evidence of remedial measures or mitigating factors when it has reason to know that a cause for suspension exists.

32. Excluded Parties Listing System, *Excluded Parties Lists Report*, *available at* http://epls.arnet.gov (last visited Apr. 5, 2004) [hereinafter *Lists Report*]; *see* FAR, *supra* note 2, at 9.404.

33. *Lists Report*, *supra* note 32.

34. *See* FAR, *supra* note 2, at 9.406-2(a)(1); *see also* Serv. Scaffold, Inc., Brian Ingber, EPA Case Nos. 86-0096-00, 86-0096-01, 1989 EPADEBAR LEXIS 7 (June 6, 1989) (finding fraudulent acts and conflicts of interest in violation of the Racketeer Influenced Corrupt Organizations Act).

35. *See* FAR, *supra* note 2, at 9.406-2(a)(2); *see also* Carlton Bartula, Case No. 91-0109-01, 1992 EPADEBAR LEXIS 66 (June 3, 1992) (finding bid-rigging and mail fraud in violation in of the Sherman Anti-Trust Act).

36. *See* FAR, *supra* note 2, at 9.406-2(a)(3); *see also* John E. Signorelli, Docket No. 94-C-0054-DB, 1995 HUD BCA LEXIS 8, 9 (Sept. 20, 1995) (reviewing debarment based on contractor's conviction for mail fraud and denying challenge of debarment order); DiCola v. FDA, 77 F.3d 504, 505 (D.C. Cir. 1996).

37. *See* FAR, *supra* note 2, at 9.406-2(a)(4).

38. *See id.* at 9.406-2(a)(5); *see also* Bae v. Shalala, 44 F.3d 489, 491 (7th Cir. 1995) (debarring petitioner based on a felony conviction for providing "an FDA official with an unlawful gratuity in exchange for official acts performed and to be performed by the FDA official"); Melvin Smith, Jet-It Sys., Inc., HUDBCA No. 90-5320-D81, 1992 HUD BCA LEXIS 12, 8 (Oct. 20, 1992) (finding illegal distribution of a controlled substance and failure to disclose knowledge of a kickback scheme).

39. *See* FAR, *supra* note 2, at 9.406-2(c).

tractor's submission raises a genuine of material fact, the official must "[a]fford the contractor an opportunity to appear with counsel, submit documentary evidence, present witnesses, and confront any person the agency presents."[45] Otherwise, the decision may be based on all the information in the administrative record, including contractor submissions.[46]

A Case Study: The Boeing Suspension

Background of the EELV Program

Our nation depends on routine, affordable, and reliable access to space.

-1997 U.S. AF Issues Book, EELV Space Launch Capability[47]

Over the years, the Department of Defense (DOD) has used a number of medium to heavy-lift expendable launch vehicles (e.g., Atlas, Delta, and Titan rockets) to transport satellites into space.[48] In the late 1980s and early 1990s, several attempts were made to reduce the cost of space launch without jeopardizing operability, but those programs proved unsuccessful.[49] Therefore, in 1993, Congress directed the Secretary of Defense to develop a Space Launch Modernization Plan (SLMP) to remedy space launch deficiencies and to reduce program costs.[50] Subsequently, AF Lieutenant General Moorman led the Space Launch Modernization Study (SLMS) with participants from the military, civil, commercial, and intelligence communities.[51] The SLMS produced four viable SLMP options: (1) sustain existing launch systems; (2) evolve current expendable launch systems; (3) develop a new expendable launch system; and (4) develop a new reusable launch system.[52]

On 5 August 1994, President Clinton signed the National Transportation Policy, which designated the DOD as the lead agency for improving and evolving existing launch vehicles, and tasked the DOD with developing an Implementation Plan.[53] Shortly thereafter, Congress appropriated $40 million for the SLMP, and the AF announced its support for Option 2—evolv-

40. *Id.* at 9.406-3(d)(3). Preponderance of the evidence means "proof by information that, compared with that opposing it, leads to the conclusion that the fact at issue is more probably true than not." *Id.* at 2.101. Debarments based on a preponderance of the evidence have been upheld in numerous instances. *See* Austen v. Office of Pers. Mgmt., 2000 U.S. App. LEXIS 493 (Fed. Cir. 2000) (making false statements); Sameena Inc. v. United States Air Force, 147 F.3d 1148, 1151 (9th Cir. 1998) (finding false submissions regarding the contractor's experience and certification regarding debarment); Wellham v. Cheney, 934 F.2d 305, 309 (11th Cir. 1991) (supplying non-conforming goods or materials and submitting fraudulent test reports and certificates of conformance); Titan Constr. Co. v. Weinberger, Civ. No. 85-5533, slip. op. (D. N.J., Feb. 14, 1986), *aff'd per curium*, 802 F.2d 448 (3rd Cir. 1986) (submitting false invoices to obtain progress payments; using foreign construction materials in violation of the Buy American Act); Robinson v. Cheney, 876 F.2d 152, 155 (D.C. Cir. 1989); Glazer Constr. Co., Inc. v. United States, 52 Fed. Cl. 513 (Fed. Cl. 2002) (violating the Davis-Bacon Act); Western Am., Inc., d/b/a Western Adhesives and Theodore A. Newman, Nos. 7655D, 7656D, 1985 GSBCA LEXIS 570 (July 22, 1985) (submitting false certification results); Andreas Boehm Malergrossbetrieb, No. 44017, 2001 ASBCA LEXIS 44, *14 (Mar. 15, 2001) (offering bribes to government officials in violation of the Gratuities Clause); Donald M. DeFranceaux and DRG Funding Group, 1994 HUDBCA LEXIS 2 (Apr. 7, 1994) (breaching fiduciary obligations to shareholders).

41. FAR, *supra* note 2, at 9.406-3(b)(1)(i)(B); *see* IMCO, Inc. v. United States, 33 Fed. Cl. 312, 318 (1995) (finding failure to perform on nine purchase orders); *see also* Immigration and Nationality Act, 8 U.S.C. § 1151 (2000).

42. FAR, *supra* note 2, at 9.406-2(b)(1), (2); *see* Drug-Free Workplace Act of 1988, 41 U.S.C. § 701.

43. *Id.* at 9.406-3.

44. *Id.*

45. *Id.*

46. *Id.*

47. EELV Space Launch Capability, *1997 U.S. Air Force Issues Book, available at* http://www.af.mil/lib/afissues/1997/app_b_20.html (last visited Mar. 30, 2004) [hereinafter *1997 U.S. Air Force Issues Book*].

48. GEN. ACCT. OFF., REP. NO. GAO-03-835R, *Military Space Operations: Common Problems and Their Effects on Satellite and Related Acquisitions* 31 (June 2, 3003) [hereinafter GAO REP. NO. 03-835R].

49. *Id.* Those programs included the "Advanced Launch System (1987-1990), the National Launch System program (1991-1992), and the Spacelifter program (1993)." Lieutenant Colonel Sidney Kimhan III et al., *EELV Program-An Acquisition Reform Success Story, Program Provides a Key to Future Military Success*, PROGRAM MANAGER 86, May/June 1999.

50. National Defense Authorization Act for Fiscal Year 1994, Pub. L. No. 103-160, § 213, 107 Stat. 1600 (1993).

51. Kimhan, *supra* note 49, at 86; *see also EELV Brief supra* note 11, at 7.

52. *Id*.

53. Presidential Decision Directive/National Science and Technology Council-4 (PDD/NSTC-4)), *available at* http://www.fas.org/spp/military/docops/national/launchst.htm (last visited Mar. 30, 2004).

ing current expendable launch systems.[54] The AF chose this option as the best route for ensuring that "satellites reach their target on time, on budget, fully operational, and at twenty-five to fifty percent less cost than current rocket systems."[55]

Acquisition Strategy

The AF employed a "rolling down-select" acquisition strategy which consisted of three phases: Low Cost Concept Validation (LCCV)—four contractors would compete to validate the low-cost concept; Pre-Engineering Manufacturing and Development (Pre-EMD)—two of the four contractors would be selected to compete for the Engineering and Manufacturing Development (EMD) contract; and EMD—one contractor would receive the award.[56] In addition to the EMD contracts, Initial Launch Services (ILS) contracts, known as Buy I, would be awarded in the final phase to the successful contractor for launching government satellites into space between the years 2002-2006.[57]

Because the government was only procuring launch services, and not the associated launch pads, processing facilities, and other control systems, there was a potential for the successful contractor to reap substantial economic benefits by using the EELV to launch commercial satellites into space.[58] Therefore, in November 1997, the EELV program office revamped its acquisition strategy to leverage the rapidly growing commercial launch satellite market.[59] Under the revised strategy, two contractors would be awarded EMD and ILS contracts rather than down-selecting to one, contractors would share the cost of developing a national launch capability, and competition would be maintained throughout the life of the program.[60] The demand for commercial satellite launches has not yet materialized.[61]

In May 1995, Alliant Techsystems, Boeing Defense and Space Group, Lockheed Martin Astronautics, and McDonnell Douglas Aerospace, were each awarded $30 million LCCV contracts and took their proposals through Tailored Preliminary Design Review, which lasted fifteen months.[62] Of the four, Lockheed Martin Astronautics and McDonell Douglas Aerospace (now a wholly owned subsidiary of Boeing) were selected to continue and were each awarded $60 million Pre-EMD contracts and took their designs through Downselect Design Review, which lasted seventeen months.[63] Based on the revised acquisition strategy, simultaneous awards of $500 million EMD contracts were awarded to Lockheed Martin and Boeing on 16 October 1998. Both agreed to pay any additional developmental costs.[64]

Also on 16 October 1998, the AF announced the breakdown of the twenty-eight ILS Buy I awards—Boeing received nineteen Buy I launches, worth $1.38 billion, and Lockheed Martin received nine, worth $650 million.[65] The name of Boeing's launch vehicle is Delta IV and Lockheed Martin's is Atlas V.[66] Since Lockheed Martin only received two West Coast Buy I launches, it asked the AF to re-allocate those launches to Boeing, as it was too costly for Lockheed Martin to upgrade its current facility at Vandenberg AF Base (AFB) for only two launches.[67] Currently, Boeing and Lockheed Martin are the

54. *EELV Brief*, *supra* note 11, at 8; Kimhan, *supra* note 49, at 86.

55. Kimhan, *supra* note 49, at 86; *see also 1997 U.S. Air Force Issues Book*, *supra* note 47.

56. Kimhan, *supra* note 49, at 87; *see also EELV Brief*, *supra* note 11, at 8-9.

57. *EELV Brief*, *supra* note 11, at 8-9.

58. GAO Rep. No. 03-835R, *supra* note 48, at 32; *see also* Kimhan, *supra* note 49, at 86-87.

59. Kimhan, *supra* note 49, at 87.

60. *Id.*

61. *Id.*; *see also* GAO Rep. No. 03-835R, *supra* note 48, at 32; Andrea Shalal-Esa, *Lockheed Invests in West Coast Rocket Launch Site*, Forbes.com, Oct. 28, 2003, *available at* http://www.forbes.com/markets/newswire/2003/10/28/rtr1126280.html [hereinafter Shalal-Esa, *Lockheed Invests in West Coast Rocket Launch Site*] (blaming telecommunications industry collapse for the failure of the commercial satellite market industry); Plunkett Research, Ltd., *Overview of the Telecommunications Industry, at* http://www.plunkettresearch.com/telecommunications/telecom_trends.htm (last visited Mar. 30, 2004) (providing a detailed overview of the telecommunications industry, trends, and statistics).

62. Plunkett Research, Ltd., *supra* note 61; Press Release, Boeing, U.S. Air Force Procures Boeing Delta IV Launches for EELV Program (Oct. 16, 1998), *available at* http://boeing.com/news/release/1998/news_release_981016a.html.

63. *Id.*; *see also EELV Brief*, *supra* note 11.

64. *Id.*

65. *Id.*; *see also* DOJ Press Release, *supra* note 12, at 12 (citing Boeing's lower price and lower risk as largely responsible for Boeing getting the bulk of the launches).

66. *EELV Brief*, *supra* note 11; *see also* DOJ Press Release, *supra* note 12.

only domestic contractors capable of performing launch services.[68]

The Boeing Suspension

On 24 July 2003, the AF suspended three of Boeing's space units and three of its former employees.[69] The suspension followed the indictment of Boeing's former employees for conspiracy, possession of trade secrets, and Procurement Integrity Act violations.[70] The alleged misconduct of Boeing's employees was further aggravated by Boeing's subsequent failure to promptly report its findings to the government.[71]

According to an affidavit submitted in support of the criminal complaint, the misconduct started when William Erskine, a Boeing EELV engineer, recruited and hired Kenneth Branch, a Lockheed Martin EELV scientist and engineer, for the purpose of obtaining the Lockheed Martin EELV proposal.[72] In exchange for delivering the proposal, Branch began working at Boeing in January 1997 "as a senior engineer/scientist earning $77,000 a year, not including overtime."[73]

At the time of Branch's hiring, the AF had not yet announced its revised dual-procurement EMD acquisition strategy, and the atmosphere at Boeing was tense:

> By spring of 1997, the pressure inside Boeing to win the rocket contract was ratcheted up significantly. On March 3, Frank Slazer, director of EELV business development, sent a memo to Larry Satchell, the manager in charge of strategic analysis and marketing at Huntington Beach, calling for "an improved Lockheed Martin EELV competitive assessment." In particular, he encouraged Mr. Satchell and others to "seek out" former Lockheed employees to get "their thoughts and impressions." The memo cautioned nonetheless that "under no circumstances should any proprietary documentation be utilized in your assessment activity."[74]

In mid-June 1999 (approximately seven months after Boeing received the bulk of the Buy I launches), Erskine told another Boeing employee about the "Branch deal."[75] According to Erskine's affidavit, Erskine hired Branch because Branch, "while still working at Lockheed Martin, came to [Erskine] with an 'under-the-table' offer to hand over the entire Lockheed Martin EELV proposal presentation to aid in Erskine's proposal in exchange for a position at Boeing."[76]

Boeing's legal department subsequently commenced an internal investigation on 18 June 1999.[77] Mr. Steve Griffin, a project specialist on the Delta IV rocket program, told Boeing investigators that when he confronted Erskine about the "Branch deal," Erskine replied, "I was hired to win . . . and I was going to do whatever it took to do it."[78] Branch and Erskine were also questioned by a Boeing attorney in 1999 and their offices were searched.[79]

According to an affidavit filed in connection with the criminal case, a variety of documents marked "Lockheed Martin/ Competition Sensitive" were found in Branch and Erskine's offices.[80] Shortly after Boeing's internal investigation, it notified Lockheed Martin[81] and the AF[82] that it had proprietary Lockheed Martin documents in its possession; however, Boeing allegedly failed to disclose the quantity and importance of

67. *See* Justin Ray, *Pentagon Strips 7 Launches From Boeing Delta 4 Rocket*, SPACEFLIGHT NOW, July 24, 2003, *available at* http://spaceflightnow.com/news/n0307/24eelv/.

68. *See generally EELV Brief*, *supra* note 11.

69. AF Press Release, U.S. Air Force Announces Boeing EELV Inquiry Results, *supra* note 8.

70. *Id.*

71. *Id.* (reporting that in June 1999, "Boeing first notified Air Force it has two documents, but says they're not critical").

72. *Id.*

73. Anne Marie Squeo & Andy Pasztor, *U.S. Probes Whether Boeing Misused a Rival's Documents at Issue in Investigations: The Hiring of a Rocket Scientist from Lockheed*, WALL ST. J., May 5, 2003, *reprinted in* NAT'L LEGAL AND POL'Y CTR., *available at* http://www.nlpc.org/cip/030505bg.html (last visited Apr. 22, 2004).

74. *Id.*

75. *See* DOJ Press Release, *supra* note 12.

76. *Id.*

77. Squeo & Pasztor, *supra* note 73.

78. *Id.*

79. *See* DOJ Press Release, *supra* note 12.

these documents.[83] Boeing terminated Branch and Erskine for cause in August 1999.[84]

Boeing's next reported disclosure did not come until March 2002 when it notified the AF that it had a significant number of additional Lockheed Martin documents in its possession. Rather than forwarding the documents, Boeing requested permission to more thoroughly investigate the matter.[85] In April, Boeing notified the AF that it located another two boxes of Lockheed Martin documents, and in July 2002, the AF referred the matter to the DOD Inspector General.[86] In October, Boeing launched the first Delta IV into space.[87]

In March 2003, the AF suspension and debarment official sent a letter to Boeing requesting an explanation for why it had Lockheed Martin's proprietary documents in its possession and also demanded the full disclosure of *all* remaining proprietary documents.[88] In April 2003, approximately four years after the first disclosure, Boeing admitted to having another ten boxes of Lockheed Martin's documents in its possession.[89] According to the DOJ's press release, the following documents were found in the offices of Erskine and Branch in 1999:

> [1] 141 documents, consisting of more than 3,800 pages, which appeared to belong to Lockheed Martin were recovered from the work spaces of Branch and Erskine in June 1999;
>
> [2] 36 of the documents were labeled "Lockheed Martin Proprietary or Competition Sensitive;"
>
> [3] 16 of the documents appeared to be related to the manufacturing cost of Lockheed Martin's EELV and, in the opinion of the USAF EELV staff, possession of these proprietary documents by a competitor could have had a "medium" or moderate chance of affecting the outcome of a competitive bid; and
>
> [4] Seven of the documents appeared to be related to the manufacturing costs of the Lockheed Martin EELV and, in the opinion of the USAF EELV staff, possession of these proprietary documents by a competitor could have had a "high" or significant chance of affecting the outcome of a competitive bid.[90]

On 25 June 2003, the government criminally charged Erskine and Branch with conspiracy, theft of trade secrets, and violating the Procurement Integrity Act.[91] During a 24 July 2003 press conference, Undersecretary of the AF Peter B. Teets, who also serves as Director of the National Reconnaissance Office (NRO), announced that the AF had suspended three of Boeing's space units and reallocated the launches under its existing EELV contract.[92] He further stated that the government "does not tolerate breaches of procurement integrity and [that it will] hold industry accountable for the actions of their employees."[93]

In addition to the suspension, the AF announced its intent to reallocate Buy I launches.[94] Under the reallocation, Boeing's total number of Buy I launches were reduced from nineteen to twelve, and the seven reallocated launches were transferred to

80. *Id.*; *see also* Squeo & Pasztor, *supra* note 73.

81. Caroline Daniel, *Boeing Probe Gets to Grips With Ethics—The Group Hopes It Can Regain the Confidence of the U.S. Air Force*, London Fin. Times, Aug. 25, 2003, *available at* http://www.ibe.org.uk/archivesaugust.htm.

82. Ray, *supra* note 67.

83. *Id.* (reporting that in June 1999, "Boeing first notified Air Force it has two documents, but says they're not critical").

84. *See* DOJ Press Release, *supra* note 12.

85. *See* Ray, *supra* note 67.

86. *Id.*

87. *Id.*

88. *Id.*

89. *Id.*; *see also* William Matthews, *Industrial Espionage "High Level" Boeing Leaders Knew of Spying, U.S. Says*, Defense News, July 21, 2003, at 8 (stating that "Boeing admitted to having more than 37,000 pages of Lockheed documents").

90. *See* DOJ Press Release, *supra* note 12.

91. *Id.*; *see* Procurement Integrity Act, 41 U.S.C. § 423 (2000).

92. DOJ Press Release, *supra* note 12.

93. AF Press Release, U.S. Air Force Announces Boeing EELV Inquiry Results, *supra* note 8.

Lockheed Martin.[95] Further, because the reallocation required Lockheed Martin to have a West Coast launch capability, the AF permitted it to develop its existing facility at Vandenberg AFB.[96] Finally, the AF announced the results of its EELV Buy II decision—it disqualified Boeing from the award of three Buy II launches, and announced its intent to award Lockheed Martin three Buy II launches.[97] The total estimated loss to Boeing was $1 billion in potential revenue.[98]

The Waivers

When Undersecretary Teets first announced the suspension, he also stated that exceptions could be made based on "compelling need[s] in the national interest."[99] Accordingly, on 29 August 2003, the AF waived its suspension and awarded Boeing a $56.7 million cost-plus-award-fee contract to deploy a Delta II rocket carrying the Global Positioning Satellite (GPS) system.[100] The waiver was necessary because Boeing was the only contractor capable of "carrying out the third phase and actually launching the GPS satellite" into space.[101] This was because Boeing already held the Delta II rocket and spacecraft integration contracts.[102]

On 30 September 2003, the AF again waived its suspension of Boeing's space units.[103] This time it justified the waiver on national defense requirements and awarded a single Buy II EELV launch to Boeing for the launch of a NRO satellite; the satellite needed to be launched from Vanderberg AFB and Lockheed Martin had not yet completed upgrading its launch facility.[104] Undersecretary Teets stated, "This is a critical national security mission and since Boeing is the only launch provider that can currently meet the requirements of this mission, we believe it is in the best interest of the country to award Boeing this launch."[105] He was also quoted as saying, "it is my sincere hope that The Boeing Company moves quickly to take meaningful corrective actions so that suspension could be lifted and Boeing could be allowed to compete in future launch competitions."[106]

The AF Suspension: Proper or Not?

Under the *FAR* standard, the AF's suspension of Boeing's space units was proper if the alleged misconduct of Boeing's employees "occurred in connection with the individual's performance of duties . . . or with the contractor's knowledge, approval, or acquiescence."[107] Presently, many of the facts are still not publically available regarding the initial discovery of Lockheed Martin's documents; Boeing's response; and the AF's rationale for its suspension. Therefore, it is difficult to fully analyze the AF's imputation decision. Such an analysis, however, is not important for the purposes of this article. What is important is examining the role of the suspension and debarment officials and how their actions may impact current and future acquisition policy.

---

94. *Id.*

95. *Id.*

96. *Id.* (providing that since the AF used the word "permit" in its press release, it is likely that the some type of monetary assistance was envisioned, such as a lease-back program or through launches); *see also* Shalal-Esa, *Lockheed Invests in West Coast Rocket Launch Site*, *supra* note 61 (reporting that Lockheed Martin will spend about $200 million to upgrade its existing launch facility).

97. *Id.*

98. Merle, *Boeing Gets Waiver From Air Force*, *supra* note 14.

99. *Id.*; *see also* Andrea Shalal-Esa, *U.S. Military Gives $1 Billion in Boeing Work to Lockheed*, July 24, 2003, *at* http://www.cndyorks.gn.apc.org/yspace/articles/boeingsuspended.htm (noting that Mr. Teets also stated that he worked at Lockheed Martin "until October or November 1999, but was unaware of this case, which first came to light in June 1999").

100. *Suspension and Debarment: Air Force Waives Boeing's Suspension, Awards $57 Million Rocket Launch Contract*, BNA's FED. CONTRACTS REP., Sept. 9, 2003, at 1.

101. *Id.*

102. *Id.*

103. Merle, *Suspension Doesn't Stop Boeing*, *supra* note 14.

104. Lockheed's West Coast launch pad was not yet complete. *See* Shalal-Esa, *Lockheed Invests in West Coast Rocket Launch Site*, *supra* note 61.

105. Press Release, U.S. Air Force, Boeing's Delta 4 Rocket Wins NRO Launch Order (Sept. 30, 2003), *available at* http://spaceflightnow.com/news/n0309/30delta4/.

106. *See* Ray, *supra* note 67.

107. FAR, *supra* note 2, at 9.406-5.

Ultimately, the AF's suspension could have driven Boeing out of the launch business, reducing the number of prime contractors in this key defense market to one.[108] This demonstrates that competition will not displace procurement integrity. It also demonstrates that in the consolidated defense industry, suspension, debarment, and waiver decisions go beyond traditional issues of responsibility. They require a careful balancing of procurement integrity, protection of citizens and soldiers, maintaining alternate sources, meeting urgent needs, and national defense requirements.

Suspension–Limited to Embroiled Units

Once the AF decided to suspend Boeing, it had to resolve the problem of how to suspend Boeing without disrupting the military's ability to obtain its critical needs. The answer was a narrowly tailored suspension which excluded only the embroiled units, with little or no impact to Boeing's other military programs. Obviously Boeing does not just supply the military with launch services.[109] "From fighter jets and transport planes to helicopters, satellites, satellite-guided bombs, system integration and satellite launches [Boeing's products and services] are woven into the daily fabric of every service branch."[110] Some would argue that the DOD's dependence on mega-contractors, like Boeing, places them largely beyond the reach of administrative remedies.[111]

In 1997, Congress directed the GAO to report on options for preserving competition in the defense industry.[112] The follow-on report dated 4 March 1998, questioned whether consolidation had gone too far and concluded that many of the defense industry transactions were too recent to study.[113] Nevertheless, the report opined that the "DOD's ability to address the potential adverse effects of consolidation will depend upon its ability to identify problem areas and devise alternative ways to maintain competitive pressures in its acquisition programs."[114]

Fast forward to 2004 and the Boeing EELV episode—consolidation continues to challenge the DOD and its procurement officials. Specifically, officials are faced with the dilemma of what to do when a primary supplier, like Boeing, falls under legal and ethical clouds. The wholesale exclusion of Boeing from federal procurements is not an option,[115] at least not until alternative sources are developed. Oversight appears to be a viable option for the short term—but how much oversight is the government willing to conduct and how much is industry willing to take? The reality is that mega-contractors typically have numerous units spread across various locations, which makes it difficult if not impossible to monitor every aspect of their operation. The good news is that the recent suspension appears to have had a sobering effect on Boeing.

Even before the suspensions were announced, Boeing retained former Senator Warren B. Rudman (R-NH) to conduct a review of Boeing's ethics programs and the handling of competitive information.[116] The week following the imposition of

---

108. Warren Fester & Jeremy Singer, *U.S. Air Force Lowers Boom on Boeing Delta Program*, SPACE.COM, *at* http://www.space.com/missionlaunches/boeing_eelv_030724.html (last visited Mar. 30, 2004).

109. For instance, Boeing Air Force Systems provides such products and services as fighters, bombers, tankers and unmanned aircraft, military satellites and space launch systems, whereas Boeing Army systems provides such products and systems as combat helicopters, heavy-lift helicopters, air-to-ground missiles, and the Joint Tactical Radio System. *See* Boeing, *Integrated Defense Systems*, *available at* http://boeing.com/ids/ids-back/index.html (last visited Mar. 30, 2004) ("Boeing Integrated Defense Systems (IDS) combines weapons and aircraft capabilities, intelligence and surveillance systems, communications architectures and extensive large-scale integration expertise across its eight customer-facing business units.").

110. Matthews, *supra* note 89, at 8.

111. *See generally* Brian, *supra* note 13.

112. GEN. ACCT. OFF., REP. NO. GAO/NSIAD-98-141, *supra* note 16, at 3; *see also* National Defense Authorization Act for Fiscal Year 1998, Pub. L. No. 105-85, § 804, 111 Stat. 1629.

113. GEN. ACCT. OFF., REP. NO. GAO/NSIAD-98-141, *supra* note 16, at 4-5. The GAO recommended that the DOD:

> [1] encourage new companies to enter the defense market through the use of science and technology investment funds; [2] fund alternative technologies to meet the warfighters' needs; [3] devise strategies to compete various approaches and missions, for example, using a missile rather than an aircraft; [4] require major defense contractors to use open-system architectures in designing weapon programs; [5] make subtier competition a specific source-selection criterion and contract requirement; and [6] explore opportunities to meet military needs through greater cooperative efforts with international partners.

Id.

114. *Id*.

115. Schooner, *supra* note 5, at 4 (likening such action to cutting one's nose off to spite one's face).

116. Press Release, Boeing, Boeing Responds to U.S. Air Force Announcement (July 24, 2003), *available at* http://www.boeing.com/news/releases/2003/q3/nr_030724s.html.

its sanctions, Boeing suspended work to ensure that all 78,000 employees in its Integrated Defense Systems business units—from its Chief Executive Officer (CEO) to its clerks, underwent a four-hour ethics refresher course.[117] Additionally, it created an Office of Internal Governance, with its head officer reporting directly to the chairman and CEO.[118]

But Boeing continues to have relapses. Another procurement integrity-related controversy was uncovered in November 2003—this related to a politically contentious refueling tanker project. Consequently, in late November 2003, Boeing announced that it terminated Executive Vice President and Chief Financial Officer, Mike Sears, for recruiting and hiring Darleen Druyun, a high-ranking U.S. AF procurement official, while Druyun was negotiating the tanker deal.[119] Druyun, who had recently left the AF for a position at Boeing as Vice President and Deputy General Manager of Missile Defense Systems, was also terminated for cause and ultimately pleaded guilty to conspiracy.[120] Following the Sears/Druyan incident, Boeing asked Senator Rudman to extend his review to an examination of Boeing's procedures and practices for hiring former government employees.[121] The impact of that relapse did not stop there; a week later Boeing's CEO Philip Condit resigned, citing his early retirement as a way for Boeing to move past its ethical lapses, and to focus on current and future performance.[122]

Boeing is not out of the woods yet—its space units still bear the black mark of suspension; Boeing remains without the $1 billion from the loss of its launch services contract;[123] and it continues to receive negative press over the troubled tanker deal, which has an estimated worth of $17 billion.[124] Recent events cause some to declare that "few companies have paid a higher price for ethical misconduct than Boeing."[125] Just days before this article went to publication, however, the *Wall Street Journal* reported that the AF is about to lift Boeing's suspension.[126]

Mega-Contractors, New Realities, and Different Considerations

The military currently needs mega-defense contractors just as much as these contractors need the military. The relationship in the Boeing context has been likened to a "long-married couple keen to save their union, if only for the sake of their children."[127] And the analogy is fitting because it demonstrates just how tenuous the relationship has become.

---

117. Press Release, Boeing, Boeing Halts Work, Conducts Business Unit-Wide Ethics Training (July 30, 2003), *available at* http://www.boeing.com/news/releases/2003/q3/nr_030730s.html.

118. Press Release, Boeing, Boeing Creates New Office of Internal Governance (Nov. 11, 2003), *available at* http://www.boeing.com/news/releases/2003/q4/nr_031111a.html.

119. Press Release, Boeing, Boeing Dismisses Two Executives for Unethical Conduct (Nov. 24, 2003), *available at* http://www.boeing.com/news/releases/2003/q4/nr_031124a.html.

120. *Id.*; Press Release, Ex-Air Force, Boeing Aide Pleads Guilty (Apr. 20, 2004), *available at* http://www.reuters.com/newsArticle.jhtml?type=businessNews&storyID=4881380&section=news ([“F]ormer U.S. Air Force acquisitions official on Tuesday pleaded guilty to conspiracy for discussing a job with Boeing Co . . . while still overseeing its business dealings with the Air Force.”).

121. *Id.*

122. Press Release, Boeing, Boeing Announces Resignation of Phil Condit; Lew Platt Named Non-Executive Chairman, Harry Stonecipher Named President and CEO (Dec. 1, 2003), *available at* http://www.boeing.com/news/releases/2003/q4/nr_031201a.html.

123. Brian Gregory, *Boeings Profits Plummet* (Oct. 29, 2003), *available at* http://komotv.com/boeing/story.asp?ID=28011; *see also* Steven Pearlstein, *Boeing's Fall From Industry Grace*, WASH. POST, Nov. 30, 2003, *reprinted in* philly.com, *available at* http://www.philly.com/mld/inquirer/news/speacial_packages/sundayreview/7375874.htm.

124. James Wallace, *Ethics Scandal at Boeing Could Delay Vital Tanker Deal*, SEATTLE POST-INTELLIGENCER, Nov. 27, 2003, *available at* http://seattlepi.nwsource.com/business/150185_boeing27.html.

125. Susan Chandler, Melissa Allison & Bruce Japsen, *A Stiff Cost for Boeing's Ethics Lesson*, CHI. TRIB., Dec. 7, 2003, *available at* http://www.chicagotribune.com/business/chi- 0312060348dec07,0,2949969.story?coll=chi-business-hed.

126. Andy Pasztor, *Boeing Will Soon Be Free to Bid for Rocket Work*, WALL ST. J, Apr. 5, 2004, at A3; *see also* FAR, *supra* note 2, at 9.407-4(b). The *FAR* provides:

> If legal proceedings are not initiated within 12 months after the date of the suspension notice, the suspension will be terminated unless an Assistant Attorney General requests its extension, in which case it may be extended for an additional 6 months. In no event may a suspension extend beyond 18 months, unless legal proceedings have been initiated within that period.

FAR, *supra* note 2, at 9.407-4(b).

127. Gopal Ratnam, *Fixing Boeing, Contrition, Better Execution Prescribed*, DEFENSE NEWS, Dec. 8, 2003, at 1.

To illustrate a point, the following chart demonstrates the reduction of prime contractors in the defense market between 1990 and 1998:[128]

Prime Contractors in Defense Market Sectors (1990-98)			
Sector	**Reduction in Contractors**	**1990 Contractors**	**1998 Contractors**
Tactical missiles	13 to 4	Boeing Ford Aerospace General Dynamics Hughes Lockheed Loral LTV Martin Marietta McDonnell Douglas Northrop Raytheon Rockwell Texas Instruments	Boeing Lockheed Martin Northrop Grumman Raytheon
Fixed-wing aircraft	8 to 3	Boeing General Dynamics Grumman Lockheed LTV-Aircraft McDonnell Douglas Northrop Rockwell	Boeing Lockheed Martin Northrop Grumman
Expendable launch vehicles	6 to 2	Boeing General Electric Lockheed Loral Martin Marietta Rockwell	Boeing Lockheed Martin
Satellites	8 to 5	Boeing General Electric Hughes Lockheed Loral Martin Marietta TRW Rockwell	Boeing Lockheed Martin Hughes Loral Space Systems TRW
Surface ships	8 to 5	Avondale Industries Bath Iron Works Bethlehem Steel Ingalls Shipbuilding NASSCO Newport News Shipbuilding Tacoma Tampa	Avondale Industries General Dynamics (Bath Iron Works) Ingalls Shipbuilding NASSCO Newport News Shipbuilding
Tactical wheeled vehicles	6 to 4	AM General Harsco (BMY) GM Canada Oskosh Stewart & Stevenson Teledyne Cont. Motors	AM General GM Canada Oshkosh Stewart & Stevenson
Tracked combat vehicles	3 to 2	FMC General Dynamics Harsco (BMY)	General Dynamics United Defense LP

128. GAO REP. NO. GAO/NSIAD-98-141, *supra* note 16, at 7-9.

Strategic missiles	3 to 2	Boeing Lockheed Martin Marietta	Boeing Lockheed Martin
Torpedoes	3 to 2	Alliant Tech Systems Hughes Westinghouse	Northrop Grumman Raytheon
Rotary wing aircraft	4 to 3	Bell Helicopters Boeing McDonnell Douglas Sikorsky	Bell Helicopters Boeing Sikorsky

Today, the number of defense contractors has been reduced even further, with essentially two prime contractors—Lockheed Martin and Boeing—receiving the largest shares of the DOD's annual contract dollars.[129] The following DOD chart shows the top ten defense contractors for fiscal year (FY) 2003 and the dollar value of the awards received in both FY 2003 and FY 2002:[130]

Rank		Company Name	Awards (Billion $)	
2003	2002		2003	2002
1	1	Lockheed Martin Corp.	21.9	17.0
2	2	The Boeing Co.	17.3	16.6
3	3	Northrop Grumman Corp.	11.1	8.7
4	5	General Dynamics Corp.	8.2	7.0
5	4	Raytheon Co.	7.9	7.0
6	6	United Technologies Corp.	4.5	3.6
7	37	Halliburton Co.	3.9	0.5
8	11	General Electric Co.	2.8	1.6
9	7	Science Applications International Corp.	2.6	2.1
10	21	Computer Sciences Corp.	2.5	0.8

In other words, the top five companies received the following percentage of the DOD's prime contract awards: 49.8% of Research, Development, Test, and Evaluation, 40.6% of Supplies and Equipment, and 15.5% of Other Services and Construction.[131] Even the *temporary* suspension of one of these giants would leave one, at best two, prime contractors capable of providing critical products and services to the DOD.

Although the suspension and debarment provisions do not list the size of the contractor (e.g., small, or large) or the types of products or services being procured (e.g., commercial items or major weapons systems) as factors for consideration, the Boeing suspension demonstrates that these factors are taken into account. By only suspending Boeing's space units, numerous other government programs remain intact.[132] This is because procurement officials cannot afford excluding a mega-contractor like Boeing from government contracts. Exclusion also would run counter to the government's policy of preserving competition as the best way for the government to receive competitive products at competitive prices.[133]

129. Procurement Statistics, DOD, *Table 3, DOD Top 100 Companies and Category of Procurement for Fiscal Year 2003, available at* http://www.dior.whs.mil/peidhome/procstat/P01/fy2003/P01FY03-Top100-table3.pdf (last visited Apr. 21, 2004) [hereinafter Procurement Statistics].

130. Procurement Statistics, DOD, *100 Companies Receiving the Largest Dollar Volume of Prime Contract Awards - Fiscal Year 2003, available at* http://www.dior.whs.mil/peidhome/procstat/P01/fy2003/top100.htm (last visited Mar. 30, 2004).

131. Procurement Statistics, Table 3, *supra* note 129.

132. Boeing's Integrated Defense Systems is responsible for the following government programs: Aerospace Support, Homeland Security and Services, Naval Systems, Air Force Systems, Army Systems, Missile Defense Systems, Space and Intelligence Systems, and NASA Systems. *See* Boeing, *Integrated Defense Systems, available at* http://boeing.com/ids/ids-back/index.html (last visited Mar. 30, 2004).

133. Matthews, *supra* note 89, at 8.

With that in mind, suspension and debarment officials must ensure that their remedies are not illusory. Since these officials are often high-level acquisition professionals, they can accomplish this by tapping into various agency resources once they become aware of facts that may warrant exclusion. One suggestion would be to establish an integrated acquisition team (IAT) comprised of senior-level acquisition officials, budget analysts, legal advisors, and other agency heads (when applicable), to study the impact of a proposed suspension or debarment. Although the time and expense of an IAT would only be warranted in very limited situations, such a team could be instrumental in crafting appropriate remedies and in shaping current and future acquisition policy. Once constituted, the IAT could consider the following:

> (1) Whether the contractor is the only source capable of providing the supplies or services and whether it is economically feasible to develop an alternative source;
>
> (2) Whether there is a subcontractor capable of manufacturing replacement products or performing similar-types services and whether that subcontractor has the capability (perhaps through subsidies) to become a prime contractor;
>
> (3) Making competition from the subcontractors a requirement for future procurements, or a bilateral modification on existing contracts;
>
> (4) Explore opportunities for the government to reverse-engineer products or to perform the service itself;
>
> (5) Explore opportunities to meet military needs through international agreements or by purchasing foreign technologies;[134]
>
> (6) Explore the costs and benefits of subsidizing small and medium concerns with a view towards developing alternate technologies;
>
> (7) Determine whether the prime contractor can perform in an advisory role to a designated sub; and
>
> (8) Consider whether the government can assume a more active role in the administration of and/or perform the contract.

Without considering such factors, agency officials may find themselves reacting to events rather than defining them. Absent a rejuvenated growth in the number of defense contractors, the DOD will continue to face challenges, combining both economic and ethical issues, when contracting with mega-contractors.

Conclusion

The defense-industry oligopoly makes it difficult to suspend or debar mega-defense contractors. Boeing's recent missteps demonstrate that even if a mega-contractor is suspended, the DOD may have to override such decisions because there are no other alternate sources; not enough time to procure an alternative source; or reprocurement may not be economically feasible. The GAO cautioned the DOD in 1998 to devise a way to maintain competitive pressure in its acquisition programs; the Boeing suspension is, in effect, cautioning the DOD again. The government should capitalize on the lessons being learned from Boeing's lapses and reexamine the way it does business, while the focus on procurement integrity remains in the public eye. Until a long-term strategy is established, acquisition officials should take an active role, rather than a reactive one, by imposing remedies aimed at developing alternative resources when mega-contractors mis-act. Progress may be slow, but if the DOD fails to act, it may find itself boxed-in and forced to do business with unethical contractors. The time to act is now.

134. Consider exceptions to the Buy American Act when U.S. Providers are declared ineligible. *See* Buy American Act, 41 U.S.C. § 10a-d (2000).

A Primer: Section 529 Plans, Coverdell Education Savings Accounts (Education IRAs), and Other Tax-Smart Ways to Save for College[1]

Lieutenant Colonel Craig D. Bell, USAR
Chief, Legal Assistance, 10th Legal Support Organization
Partner, McGuireWoods LLP
Richmond, Virginia

Maureen C. Ackerly, Esquire
Partner, McGuireWoods LLP
Richmond, Virginia

Introduction

Benjamin Franklin once observed, "An investment in knowledge always pays the best interest."[2] As legal assistance attorneys, clients frequently ask: What is the best way to save or pay for education, especially college education for children and grandchildren? There really is no one "best" answer or resolution to this question. Many more options are available today than ever before. Traditionally, we have counseled clients on the use of custodial accounts such as the Uniform Gifts to Minors Act (UGMA) or the Uniform Transfers to Minors Act (UTMA).[3] These standby methods are quite appealing now that Congress has lowered the capital-gains tax rate that effectively reduces the tax rate most children will pay on any gains in their stock portfolio to between eight and ten percent.[4]

We have also counseled clients on the use of U.S. Savings Bonds, such as Series EE bonds issued after 1989 and all Series I (inflation adjusted) bonds.[5] For married taxpayers with adjusted incomes of $117,750 or less ($73,500 for single tax return filers), some or all of the interest earned on these bonds is tax-free if used for higher education expenses.[6] Consumers' main complaint about them is their low interest rate.

In addition to the traditional savings techniques discussed above, Congress has recently introduced tax incentives to promote education savings, including prepaid tuition and education investment plans commonly referred to as 529 Plans (after Section 529 of the Internal Revenue Code which governs them), Coverdell Education Savings Accounts (formerly called Education IRAs), Hope Scholarships, and Lifetime Learning Credits.[7] This article focuses on 529 Plans and Coverdell Education Savings Accounts. The appendices provide supplemental statutory guidance.

Background

Increasing Cost of Higher Education

The College Board compiled data from 2001-2002, which shows an increase of 9.6% in college tuition and fees at four-year public institutions, and 5.8% at four-year private institutions, as compared with a 1.2% annual increase in the Consumer Price Index.[8] The increase in tuition and fees from 2000-2001 was 4.4% and 5.2%, respectively.[9] College costs increased an average of 7.7% per year during the period 1971-

1. *See* Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, 115 Stat. 38 (2001) (2001 Act). Unless otherwise noted, all references to "section" or "§" are to the Internal Revenue Code of 1986, as amended, and the regulations and proposed regulations thereunder.

2. SAVING FOR EDUCATION: A LONG-TERM INVESTMENT, A GUIDE TO UNDERSTANDING 529 PLANS 1, INVESTMENT CO. INSTIT. (2002) [hereinafter 529 PLANS].

3. *See* UNIFORM TRANSFERS TO MINORS ACT § 2 (2000); UNIFORM GIFTS TO MINORS ACT § 2 (2000). The National Conference of the Commissioners on Uniform State Laws promulgated the UGMA in 1956. All fifty states and the District of Columbia have adopted some version of the UGMA. HENRY J. LISHER, JR., 846 T.M., GIFTS TO MINORS 16(2) (1997). The UGMA has been revised several times and renamed as the UTMA in 1993. *Id*. at 18. Forty eight states and the District of Columbia have adopted a version of the UTMA. *Id*.

4. I.R.C. § 1(h) (2000).

5. *See* Bureau of the Public Debt, *Series EE/E Savings Bonds*, *available at* http://www.publicdebt.treas.gov/sav/savinvst.htm (last visited Apr. 20, 2004) ("EE Bonds are low-risk savings products that pay interest based on current market rates on Treasury securities. EE Bonds are a safe and secure way to save for the future, whether it's to finance education, supplement retirement income, or give as a gift."); Savingsbonds.com, *Home, available at* www.savingsbonds.com (last visited Apr. 21, 2004); U.S. Dep't of the Treasury, *Treasury Direct, available at* www.treasurydirect.gov (last visited Apr. 21, 2004).

6. I.R.C. § 135(a), (b), (c)(1).

7. *See* 529 PLANS, *supra* note 2.

8. *See 2002 Trends in College Pricing*, *available at* www.collegeboard.org (last visited Apr. 23, 2004) [hereinafter *2002 Trends in College Pricing*]; *News 2000-2001*, *available at* www.collegeboard.org (last visited Apr. 23, 2004) [hereinafter *News 2000-2001*].

2001, in comparison to an average 5.1% annual increase in the Consumer Price Index over the same period.[10] From 1989 to 1999, college costs increased at more than twice the rate of the Consumer Price Index (5.6% versus 2.3%).[11]

The economic importance of higher education has also increased. United States Census Bureau statistics show the annual income for a person with a college degree is more than eighty percent higher than for a high school graduate.[12]

In 2020, the College Board projects average college costs for four years of tuition and fees, books and supplies, room and board, transportation and other expenses, as $271,698 for private institutions, and $123,487 for public institutions.[13] Using present costs of actual institutions and projecting to 2020 (assuming five percent inflation rate in college costs), the "in-state" cost for four years of attendance at SUNY-Albany (a four-year public college) will be $130,272, the "out-of-state" costs for Michigan State University (a four-year public college) will be $204,676, and the cost for Columbia University (a four-year private college) will be $358,547.[14]

Predominant Financial Concern

According to the College Savings Plans Network, a non-profit affiliate of the National Association of State Treasurers, public opinion polls indicate the greatest financial concern of most American families has shifted from the ability to save sufficient retirement assets to the ability to pay for children's college education.[15]

In August 1995, the United States General Accounting Office (GAO) published a report on state tuition programs in existence at that time.[16] According to the GAO report:

> When asked on Alabama's program application how they would save for college costs without the tuition prepayment program, about 52% of purchasers in 1991-1994 checked "savings account," about 17% checked "savings bonds," about 15% checked "life insurance," and only about 6% checked "stocks." With passbook savings accounts currently offering less than 3%, it appears that a large percentage of Alabama's participants would be putting their money in investments that would be expected to provide a lower return than the anticipated rate of tuition inflation, about 7-8% per year.[17]

According to an Alliance/Harris College Savings Poll (August 2001), families expect to save only $20,000 for college costs, but expect to pay more than $80,000.[18]

Traditional Education Savings Techniques

Traditional education savings techniques include gifts to a student or for the student's benefit, and tuition payments made directly to the educational organization. Gifts of up to $11,000 per year or $22,000 if the donor is married[19] to a beneficiary outright, a custodial account for a beneficiary, or certain types of trusts for a beneficiary, qualify for an annual exclusion from gift tax.[20] They are treated as nontaxable gifts" for purposes of generation-skipping transfer (GST) tax.[21]

---

9. *2002 Trends in College Pricing*, *supra* note 8; *News 2000-2001*, *supra* note 8.

10. *2002 Trends in College Pricing*, *supra* note 8; *News 2000-2001*, *supra* note 8.

11. *See* THE COLLEGE BOARD, INDEPENDENT COLLEGE 500 INDEX (1999), *available at* www.benico.com (last visited Apr. 21, 2004).

12. *See 2002 Trends in College Pricing*, *supra* note 8.

13. *See id.* (assuming five percent inflation rate in college costs).

14. U.S. News Online, *What Will College Cost for Your Child?*, *available at* www.benico.com (last visited Apr. 12, 2004).

15. *See* College Savings Plans Network (CSPN), *About CSPN*, *available at* http://www.collegesavings.org/ (last visited Apr. 21, 2004).

16. U.S. General Accounting Office, *College Savings: Information on State Tuition Prepayment Programs*, Aug.1995, *available at* www.gao.gov/archive/1995/he95131.pdf (last visited Mar. 9, 2004).

17. *Id.*

18. Alliance/Harris College Savings Poll (Aug. 2001), *available at* www.benico.com (last visited Apr. 12, 2004) [hereinafter Alliance/Harris College Savings Poll].

19. The married couple may elect to "split gifts" with his or her spouse for gift tax purposes under Internal Revenue Code (IRC or Code) Section 2513. I.R.C. § 2513 (2000).

20. *Id.* §§ 2503(b), 2642(c).

21. *Id.*

Qualified Transfers for Educational Expenses

In addition to the gift tax and GST tax annual exclusions, certain qualified transfers for educational expenses are exempt from gift tax and GST tax.[22] A qualified transfer is a tuition payment made directly to a qualified educational institution for the education and training of an individual, but does not include amounts paid for books, supplies, dormitory fees, board, or other expenses which do not constitute direct tuition costs.[23]

There is no limit on the amount of a qualified transfer, and qualified transfers may be made in conjunction with other education savings techniques (e.g., annual exclusion gifts and contributions to 529 Plans and Coverdell Education Savings Accounts).[24] A qualified transfer is exempt from gift tax and GST tax without regard to the relationship between the payor and the student.[25]

The Internal Revenue Service (IRS) has ruled that a donor may make qualified transfers to prepay multiple years of a student's tuition.[26] Such prepayment allows a donor who may not live to make future tuition payments to confer substantial tax-free benefits on a beneficiary currently, while reducing the donor's taxable estate.

Current Status

Currently, all fifty states and the District of Columbia have 529 Plans in operation or development.[27] Over 1.5 million students have been enrolled in 529 Plans, with contributions representing more than $9.5 billion dedicated for future college costs.[28] Cerulli Associates, a financial consulting firm, has predicted that assets in 529 Plans will grow to more than $50 billion by 2006.[29] According to Salomon Smith Barney's research on public awareness of college savings vehicles, eighty-five percent of investors know about U.S. Savings Bonds, fifty-two percent know of Education IRAs (now Coverdell Education Savings Accounts), but just thirty percent know about 529 Plans.[30]

Prepaid Tuition Plans and Education Investment Plans

Code Section 529 authorizes two types of qualified tuition programs (QTPs): prepaid tuition plans and education investment plans.[31] Under the prepaid tuition plan, a contributor purchases tuition credits or certificates on behalf of a designated beneficiary, which entitles the beneficiary to the waiver or payment of qualified higher education expenses.[32] Prepaid tuition plans are designed to hedge against inflation, and enable a contributor to lock-in tomorrow's tuition at today's prices.

Under the education investment plan, a contributor deposits amounts in a separate investment account established for the purpose of meeting the qualified higher education expenses of the designated beneficiary.[33] Once deposited in the account, the contributions are invested in the market (typically, in mutual funds). Investments within these plans are subject to market fluctuations, and do not offer a guaranteed return.

---

22. *Id.* §§ 2503(e), 2611(b)(1).

23. Treas. Reg. § 25.2503-6(b)(2) (2000).

24. *See id.*

25. *Id.* § 25.2503-6(a).

26. Tech. Adv. Mem. 199941013 (July 9, 1999). In this Technical Advice Memorandum, the IRS ruled that a grandmother's non-refundable payments made directly to a preparatory school for several years of her grandchildren's tuition qualified for exclusion from gift tax treatment. *Id.*; *see* Treas. Reg. § 25.2503.

27. Savingforcollege.com, *Internet Guide to Coverdell ESA*, *available at* http://www.savingforcollege.com/ (last visited Apr. 21, 2004) [hereinafter *Internet Guide to Coverdell ESA*].

28. Jane J. Kim, *Choosing a College-Savings Plan*, WALL ST. J., Sept. 24, 2003, at D2.

29. *College Savings Plans: The Race Is On*, N.Y. TIMES, Jan. 13, 2002, at B6.

30. John Waggoner, *529 Adds Up to College Savings*, USA TODAY, Sept. 6, 2000, at B1. According to an Alliance/Harris College Savings Poll (Aug. 2001), only twenty-five percent of families polled were aware of 529 Plans. *See* Alliance/Harris College Savings Poll, *supra* note 18. Sixty-two percent, however, said they would invest in a 529 Plan once they understood the features and benefits. *Id.*

31. I.R.C. § 529 (2000).

32. *Id.* § 529(b)(1)(A)(i).

33. *Id.* § 529(b)(1)(A)(ii).

QTP Requirements

To receive tax-favored treatment, a QTP must meet the following criteria: (1) cash contributions only; (2) separate accounting; (3) no investment direction permitted; (4) no pledging of interest as security; (5) prohibition on excess contributions; (6) prepaid tuition plan sponsors no longer limited to states; and (7) reporting.[34]

First, tuition purchases and investment account contributions may be made in cash only.[35] A QTP may not accept stock or other property. Consequently, a contributor (including the custodian of an UTMA or UGMA account) may need to liquidate investments and pay capital gains tax before making a QTP contribution. Second, the program must maintain a separate accounting for each designated beneficiary.[36] Third, no contributor or designated beneficiary may directly or indirectly direct the investment of any contribution to the program or the earnings thereon.[37] For education investment plans, contributors typically may select among different investment strategies designed by the plan on creation of the account. This limited, initial "direction" is specifically permitted under the proposed regulations.[38]

Fourth, no interest in the program or portion thereof may be pledged as collateral or otherwise used as security for a loan.[39] Fifth, a program must contain adequate safeguards to prevent contributions on behalf of a beneficiary in excess of those reasonably necessary to provide for the qualified higher education expenses of the beneficiary.[40] The Proposed Regulations pro vide a safe harbor whereby a QTP will satisfy this requirement if it bars any additional contributions to an account once the account reaches a specified account balance limit applicable to all accounts of designated beneficiaries with the same expected year of enrollment. The total contributions may not exceed the amount determined by actuarial estimates that is necessary to pay the beneficiary's tuition, required fees, and room and board expenses for five years of undergraduate enrollment at the highest cost institution allowed by the QTP.[41]

Lastly, each QTP or its designee must submit reports to the IRS and designated beneficiaries with respect to contributions, distributions, and such other matters as the IRS may require.[42]

---

34. *See id.*

35. *Id.* § 529(b)(2).

36. *Id.* § 529(b)(3).

37. *Id.* § 529(b)(4).

38. Prop. Treas. Reg. § 1.529-2(g), 63 Fed. Reg. 45,019 (Aug. 24, 1998). In Notice 2001-55, issued 7 September 2001, the IRS recognized that there are a number of situations that might warrant a change in the investment strategy with respect to a 529 Plan account. I.R.S. Notice 2001-55, 2001-2 C.B. 299. Notice 2001-55 provides that the IRS expects that final regulations under Section 529 will provide that a 529 Plan does not violate Code Section 529(b)(4) if it permits a change in the investment strategy selected for a 529 Plan account once per calendar year and upon a change in the designated beneficiary of the account. *Id.* The IRS expects that final regulations will also provide that, to qualify under this special rule, a Plan must (1) allow participants to select only from among broad-based investment strategies designed exclusively by the Plan; and (2) establish procedures and maintain appropriate records to prevent a change in investment options from occurring more frequently than under the foregoing circumstances. *Id.*

In response to the rapid growth and sophistication of 529 Plans, in Notice 2001-55, the IRS recognized that there are a number of situations that might warrant a change in the investment strategy with respect to a 529 Plan account. I.R.S. Notice 2001-55, 2001-2 C.B. 299. According to Notice 2001-55, the IRS expects that final regulations under Section 529 will provide that a 529 Plan does not violate Section 529(b)(4) if it permits a change in the investment strategy selected for a 529 Plan account once per calendar year and upon a change in the designated beneficiary of the account. *Id.*

Notice 2001-55 further states that the IRS expects final regulations will provide that, to qualify under this special rule, a Plan must (1) allow participants to select only from among broad-based investment strategies designed exclusively by the Plan; and (2) establish procedures and maintain appropriate records to prevent a change in investment options from occurring more frequently than under the foregoing circumstances. *Id.*

39. I.R.C. § 529(b)(5).

40. *Id.* § 529(b)(6).

41. § 1.529-2(i)(2), 63 Fed. Reg. at 45,024. In practice, most QTPs impose a cap on contributions between $100,000 and $250,000. Before the 2001 Act, QTPs could be established and maintained only by a state or a state agency or instrumentality. The 2001 Act authorizes private institutions to establish and maintain prepaid tuition plans, but retains the "state only" limitation on education investment plans. To qualify its program as a QTP, a private institution must hold program contributions in a qualified trust and receive an IRS ruling or determination that the program meets the applicable requirements of a QTP. I.R.C. § 529(b)(1).

Qualified Tuition Plans Exempt from Federal Income Tax

A QTP is exempt from federal income tax, but is subject to the same rules as charitable organizations regarding taxation of unrelated business income.[43] As a result, earnings on QTP contributions compound income tax-free within the plans.

Qualified Distributions Exempt from Federal Income Tax

Qualified Distributions Excluded from Gross Income

In-Kind Distributions

In-kind distributions which, if paid for by the distributee, would constitute payment of a qualified higher education expense, are excluded from gross income.[44] Consequently, a beneficiary will not be subject to income tax upon the eventual use of purchased credit hours under a prepaid tuition program.

Cash Distributions

If aggregate cash distributions in a given year do not exceed the beneficiary's qualified higher education expenses in such year, no amount is included in the beneficiary's gross income.[45] If aggregate cash distributions exceed qualified higher education expenses, the amount includible in gross income is equal to the aggregate distribution amount reduced by an amount bearing the same ratio to such amount as the beneficiary's qualified higher education expenses bear to the aggregate distribution amount.[46]

Benefits Treated as Distributions

Any benefit furnished to a designated beneficiary under a QTP is treated as a distribution to the beneficiary for purposes of determining income tax liability.[47]

Coordination with HOPE and Lifetime Learning Credits

The amount of qualified higher education expenses to which QTP distributions may be applied is reduced by the amount of such expenses that were taken into account in determining the HOPE and Lifetime Learning credits allowed under section 25A of the Code.[48]

Coordination with Coverdell Education Savings Accounts

If in any year aggregate distributions on behalf of a beneficiary from any QTP and Coverdell Education Savings Account exceed the beneficiary's total qualified higher education expenses, expenses will be allocated between such distributions for purposes of determining the income tax treatment of the distributions.[49]

Nonqualified Distributions Taxed under Annuity Rules

Nonqualified distributions (those not used to pay qualified higher education expenses) are included in the distributee's income and taxed under the annuity rules of Code Section 72.[50]

---

42. *Id.* § 529(d). *See* § 1.529-4, 63 Fed. Reg. at 45,025. Proposed Regulations require a 529 Plan to report on Form 1099-G, Certain Government Payments, the earnings portion of any distribution made during the year, together with other information such as the name, address and tax identification number of the distributee. *Id.* The 529 Plan must furnish a statement to the distributee on or before 31 January of the year following the calendar year in which the distribution is made. In addition, a 529 Plan must file Form 1099-G on or before 28 February of the year following the calendar year in which the distribution is made. Notice 2001-81, 2 C.B. 617. Notice 2001-81 provides that these reporting requirements continue in effect for distributions made in 2001. Notice 2001-81 further provides that in light of the expansion of Code Section 529 under the 2001 Act to include prepaid tuition programs established and maintained by one or more eligible educational institutions (which may be private institutions), the IRS will issue a new form, Form 1099-Q, for taxable years beginning after 31 December 2001. *Id.* A copy of Form 1099-Q is available for downloading from the IRS website. Dep't. of the Treasury, *Internal Revue Service*, *available at* www.irs.gov (last visited Apr. 21, 2004).

43. I.R.C. § 529(a).

44. *Id.* § 529(c)(3)(B)(i).

45. *Id.* § 529(c)(3)(B).

46. *Id.* § 529(c)(3)(B)(ii).

47. *Id.* § 529(c)(3)(B)(iv).

48. *Id.* § 529(c)(3)(B)(v).

49. *Id.* § 529(c)(3)(B)(vi).

Change in Beneficiaries

Rollovers

A QTP distribution is not included in taxable income to the extent it is transferred within sixty days of distribution to:

(1) another QTP for the same beneficiary; [51] or

(2) a QTP for another designated beneficiary who is a member of the family of the original designated beneficiary.[52]

Limit on Same Beneficiary Rollovers

A tax-free rollover may be made to an account for the same beneficiary only once within a twelve-month period.[53] If a rollover occurs within twelve months of a prior rollover for the same beneficiary, the rollover will be taxed to the beneficiary as a nonqualified distribution.

Change in Designated Beneficiaries

A change in the designated beneficiary of a QTP is not treated as a nonqualified distribution if the new beneficiary is a member of the family of the original beneficiary.[54]

Aggregation of Accounts

For purposes of calculating taxable income for nonqualified distributions, all QTPs of which an individual is the designated beneficiary are aggregated and treated as a single QTP and all distributions are treated as single distribution.[55]

Valuation Date

For purposes of calculating taxable income for nonqualified distributions, the value of a QTP account, income earned on the account, and investment in the account are computed as of the close of the calendar year in which the taxable year begins.[56]

Illustration of Tax Savings

529 Plan Accounts versus Taxable Accounts

Assuming a one-time lump sum investment of $50,000, an eight percent annual return and a combined federal and state tax rate of thirty-five percent, after eighteen years a taxable account will grow to $124,524. A 529 Plan account which is not subject to federal or state tax will grow to $199,801, a difference of $75,277.[57]

---

50. *Id.* § 529(c)(3).

(1) Applying the annuity rules, distributions are divided into two portions: (1) contributions (return of investment), and (2) earnings. *Id.* § 7 (2)(e)(2)(B), (9). Earnings allocable to an account are determined by subtracting the investment in the account (total contributions) from the balance of the account. Prop. Treas. Reg. § 1.529-3(b), 63 Fed. Reg. 45,019 (Aug. 24, 1998).

(2) The earnings portion of the distribution is included in the gross income of the distributee. *Id.* § 1.529-3(a). The portion of the distribution that consists of original contributions is not subject to tax.

(3) The earnings portion is taxed as ordinary income, irrespective of whether part or all of the earnings are attributable to capital gains.

(4) There is some uncertainty as to whether earnings on a nonqualified distribution are included in the income of the designated beneficiary or the account owner (e.g., who is deemed to be the "distributee"). The Proposed Regulations provide that "*Distributee* means the designated beneficiary or the account owner who receives or is treated as receiving a distribution from a [QTP]." *Id.* § 1.529-1(c). An example included in the proposed regulations indicates that nonqualified distributions made to the designated beneficiary will be taxed to such beneficiary. *Id.* § 1.529-3(b)(3), example 2(ii). In practice, however, certain QTPs may prohibit nonqualified distributions to anyone other than the account owner.

51. I.R.C. § 529(c)(3)(C)(i)(I).

52. *Id.* § 529(c)(3)(C)(i)(II).

53. *Id.* § 529(c)(3)(C)(iii).

54. *Id.* § 529(c)(3)(C)(ii).

55. *Id.* § 529(c)(3)(D)(i)-(ii).

56. *Id.* § 529(c)(3)(D)(iii).

57. This figure is based on the authors' computation.

Effect of 2001 Act on 529 Plan Savings

Assume grandparents contribute $100,000 to an education investment QTP for a newborn grandchild, and the assets grow at an annual rate of ten percent. When the grandchild reaches age eighteen, the account balance is $555,991. Assuming the average 7.7% annual inflation rate for college costs, the account balance would greatly exceed the approximately $82,500 per year for tuition, fees, books, room and board at a four-year private college. Assuming the account earnings would have been subject to tax on distribution at the grandchild's rate of fifteen percent under the 529 Plan rules before the 2001 Act, the 2001 Act exemption from federal income tax represents a savings of $83,200. Any QTP assets not used to pay the grandchild's education expenses could be withdrawn (subject to income tax on the earnings and a ten percent penalty), or rolled over to a QTP account for another grandchild or other family member.[58]

State Income Taxation

Most states' tax treatment of income parallels federal tax treatment.[59] Consequently, in most states, qualified distributions from 529 Plans are exempt from state income tax. Even before the 2001 Act, certain states (e.g., Virginia) exempted from state income tax qualified distributions from their state's QTPs.[60] Certain states allow an up-front income tax deduction for contributions to their state's QTPs. For example, Virginia allows an income tax deduction of $2,000 per QTP account per year, with an unlimited carry forward until the full amount has been deducted. If a contributor is age seventy or above, the $2,000 annual deduction cap does not apply and the contributor may deduct the entire contribution amount in the year made.[61]

Gift Tax Treatment of 529 Plans

Contributions Treated as Completed, Present Interest Gifts

For gift and generation-skipping transfer tax purposes, any contribution to a QTP on behalf of a designated beneficiary is treated as a completed gift to such beneficiary which is not a future interest in property.[62]

Treatment of Excess Contributions: Five-Year Averaging Election

If a contributor's aggregate contributions during a calendar year exceed the annual exclusion amount for gift tax purposes under Code Section 2503(b), the contributor may elect to take the aggregate amount into account ratably over the five-year period beginning with such calendar year.[63] Thus, in 2004, an individual may contribute up to $55,000, and a married couple who elect to split gifts for gift tax purposes under Code Section 2513 may contribute up to $110,000, per QTP beneficiary in one year free of gift tax or GST tax.

The following is a list of practical examples:

Example 1:

In 2004, grandmother, a widow, contributes $25,000 to a QTP account for grandchild. Because grandmother's 2004 contribution exceeds the $11,000 annual exclusion amount, she elects to take the $25,000 into account ratably from 2004 to 2008. As a result, grandmother is treated as having made completed gifts of $5,000 in each of 2004, 2005, 2006, 2007, and 2008. Note that grandmother cannot elect to treat her 2004 excess contribution as a completed gift of $11,000 in each of 2004 and 2005, and a completed gift of $3,000 in 2006.

Example 2:

In 2004, grandmother contributes $75,000 to a QTP account for grandchild. Grandmother is treated as having made a completed gift of $31,000 in 2004 ($11,000 of which qualifies for the annual exclusion from gift tax and GST tax, and $20,000 of which does not), and completed gifts of $11,000 in each of 2005, 2006, 2007, and 2008.

---

58. *See* I.R.C. § 529(c); § 1.529-3, 63 Fed. Reg. at 45,025.

59. *See* RIA, ALL STATES TAX GUIDE para.15-110 (2003) (referring to chart).

60. *See, e.g.*, VA. CODE. ANN. § 58.1-322 (LEXIS 2004).

61. *Id.* § 58.1-322D7.

62. I.R.C. § 529(c)(2)(A)(i). A QTP contribution is treated as a completed gift even though the contributor retains the right to revoke the gift and revest the contribution in himself or change the beneficiary of the account to a new beneficiary by direct change or rollover. *Id.* Because the contribution is treated as a "present interest" gift, it qualifies for the annual exclusion from gift tax under Code Section 2503(b) and exclusion from generation-skipping transfer tax under Code Section 2642(c)(2). Treas. Reg. §§ 25.2503(b), 2642(c)(2) (2000).

Whereas Code Section 529, as originally enacted, excluded QTP contributions from gift tax and GST tax treatment as Code Section 2503(e) qualified transfers for educational expenses, in 1998, the statute was amended to provide that contributions do not constitute Code Section 2503(e) qualified transfers, but rather, constitute completed gifts of present interests qualifying for the annual exclusion from gift tax and exclusion from generation-skipping transfer tax. I.R.C. § 529(c)(2)(A)(ii).

63. *Id.* § 529(c)(2)(B).

Example 3:

Assume the same facts set forth in Example 1, except that in 2005, grandmother makes an additional contribution to the QTP account of $11,000 (the amount of the annual exclusion in 2005). Grandmother is treated as having made an additional completed gift of $11,000 in 2005, $6,000 of which qualifies for the annual exclusion ($11,000 - $5,000 from 2004 contribution treated as completed gift for 2003), and $5,000 of which constitutes a taxable gift (to which unified credit and GST exemption may be applied, or if none is available, upon which gift tax and GST tax must be paid).

Example 4:

Assume grandmother contributed $50,000 to a 529 Plan in 2001, when the annual exclusion amount was $10,000. Grandmother elected to take the $50,000 in account ratably from 2001 to 2005, so that grandmother is treated as having made completed gifts of $10,000 in each of years 2001-2005. In 2002, the annual exclusion amount was adjusted for inflation to $11,000. Can grandmother contribute an additional $4,000 in 2002 to take advantage of the additional $1,000 of annual exclusion in 2002-2005? No, according to the Proposed Regulations. The proposed regulations indicate that beginning in 2002, grandmother can contribute an additional $1,000 per year each 1 January.[64]

Treatment of Distributions

General Rule

In general, a distribution from a QTP is not treated as a taxable gift for gift tax or generation-skipping transfer tax purposes.[65]

Special Rules for Rollovers or Change of Beneficiaries

If New Beneficiary Is in Same or Older Generation as Original Beneficiary

A change in the designated beneficiary of a QTP (or a rollover to a QTP account of a new beneficiary) is not treated as a transfer for gift tax or GST tax purposes if the new beneficiary is in the same generation or a generation above the old beneficiary (as determined in accordance with the GST tax rules).[66]

If New Beneficiary Is in Younger Generation Than Original Beneficiary

A change in the designated beneficiary of a QTP (or a rollover to a QTP account of a new beneficiary) is treated as a transfer for gift tax and GST tax purposes if the new beneficiary is in a generation below the old beneficiary (as determined in accordance with the GST tax rules).[67]

Gift by Original Beneficiary

If upon a rollover or change in account beneficiary the new beneficiary is in a generation below the old beneficiary, the transfer is treated as a taxable gift from the original beneficiary to the new beneficiary. The transfer is also subject to GST tax if the new beneficiary is two or more generations below the generation of the original beneficiary.[68]

Original Beneficiary May Apply Own Annual Exclusion

The original beneficiary may apply his or her annual exclusion for gift tax purposes, including the five-year averaging election, to shield the deemed gift from gift tax.[69]

Phantom Gift

These rules effectively allow a beneficiary to be subject to gift tax and GST tax based on the independent act of the account owner, of which act the beneficiary may have no knowledge.

Estate Tax Treatment of 529 Plans

Contributor's Estate

General Rule: No Inclusion in Estate

In general, no amount is includible in the gross estate of a contributor by reason of an interest in a QTP.[70] This is so even though the contributor retains the right to revoke the gift and

64. *See* Prop. Treas. Reg. § 1.529-5(b)(2), 63 Fed. Reg. 45,019 (Aug. 24, 1998).

65. I.R.C. § 529(c)(5)(A).

66. Prop. Treas. Reg. § 1.529-5(b)(3)(i), 63 Fed. Reg. 45,019 (Aug. 24, 1998).

67. I.R.C. § 529(c)(5)(B).

68. § 1.529-5(b)(3)(ii), 63 Fed. Reg. at 45,025.

69. *Id.* § 1.529-5(b)(3)(ii).

revest the account in the contributor and the right to change the beneficiary to a new beneficiary selected by the contributor.[71]

Exception When Contributor Elects Five-Year Averaging for Excess Contributions

When a contributor elects to take excess contributions into account ratably over a five-year period and dies before the close of the five-year period, the contributor's gross estate will include the portion of such contributions allocable to the periods after the contributor's date of death.[72]

Beneficiary's Estate

The statute provides that amounts distributed on account of the death of the designated beneficiary are included in the beneficiary's gross estate.[73] The Proposed Regulations provide "[t]he gross estate of the designated beneficiary of a [QTP] includes the value of any interest in the [QTP]."[74] Although the Proposed Regulations do not define a designated beneficiary's "interest" in a QTP, IRS personnel have indicated that the likely interpretation would be that the entire QTP balance would be included in the designated beneficiary's estate at death.[75]

Planning Considerations

Advantages of 529 Plans

Qualified Distributions Fully Exempt from Income Tax

Before the 2001 Act, 529 Plans offered a significant tax benefit by deferring income tax on contribution earnings (which benefit was offset in part by conversion of capital gains to ordinary income). The 2001 Act, however, exempts 529 Plan earnings from federal income tax altogether if funds are used for qualified higher education expenses.[76] This full exemption will generally provide a superior return to traditional, taxable education savings techniques such as gifts to the student outright or to a custodial account or trust for the student. Further, a contributor may donate up to five times the annual exclusion amount in the year of contribution without incurring gift tax or generation-skipping tax, thereby increasing tax-free compounding. This election is not available for traditional education savings techniques.[77]

Account Owner May Reacquire Funds

Another benefit is that the account owner may reacquire the 529 Plan funds at any time for any reason, subject to income tax and an additional ten percent tax on the earnings portion of nonqualified distributions. Unlike traditional gifts, this retained control by the donor does not cause inclusion of the 529 Plan account in the donor's estate at death.[78]

Beneficiary Does Not Control Funds

Unlike traditional gifts outright or to custodial accounts, the beneficiary of a 529 Plan account generally has no control over accounts for his or her benefit. Rather, the account owner has control over distributions and may reacquire the funds or change the beneficiary at any time (e.g., if the beneficiary chooses to join the circus rather than attend college).[79]

---

70. I.R.C. § 529(c)(4)(A).

71. § 1.529 cmt., para. [29], 63 Fed. Reg. at 45,024.

72. I.R.C. § 529(c)(4)(B); § 1.529-5(d)(2), 63 Fed. Reg. at 45,025.

Example:

In 2003, grandmother, a widow, contributes $20,000 to a QTP account for grandchild, and elects to take the $20,000 into account ratably from 2003 to 2007. As a result, grandmother is treated as having made completed gifts of $4,000 in each of 2003, 2004, 2005, 2006, and 2007. Grandmother dies on 1 January 2005. $8,000 (the amount attributable to 2006 and 2007) is includible in grandmother's gross estate. Note, however, that none of the post-contribution earnings or appreciation attributable to the $8,000 is included in grandmother's gross estate.

73. I.R.C. § 529(c)(4)(B).

74. § 1.529-5(d)(3), 63 Fed. Reg. at 45,025.

75. *See* SUSAN T. BART & PETER S. GORDON, PLANNING FOR COLLEGE: TAX AND OTHER CONSIDERATIONS D-26 (Mar. 2001) (noting this was written material for the ACTEC Seminar (citing Telephone Interview with Susan Hurwitz, Internal Revenue Service (16 Aug. 1999))).

76. *Id.* § 529(c)(1).

77. *Id.* § 529(c)(2).

78. *Id.* § 529(c)(3); § 1.529, cmt. [29], 63 Fed. Reg. at 45,024.

79. *See* I.R.C. §§ 529(b)(4), (c)(3)(C); § 1.529-2(g), 63 Fed. Reg. at 45,024.

No Income Restrictions and High Contribution Limits

Unlike Coverdell ESAs, which will be discussed in the following section, there are no restrictions on a contributor's ability to participate in 529 Plans based on the contributor's adjusted gross income. In addition, contribution limits are substantially higher than Coverdell ESAs.[80]

May Be Used in Conjunction with Other Education Savings Techniques

A contributor may take advantage of 529 Plans in conjunction with qualified transfers of tuition payments under Code Section 2503(e), contributions to Coverdell ESAs, and other education credits.[81]

Disadvantages of 529 Plans

Lack of Investment Control

The account owner and beneficiary are prohibited from exerting investment control over 529 Plan accounts.[82] However, because an account owner may select an investment strategy upon creation of the account, and because most 529 Plan sponsors allow contributions irrespective of residency, a contributor may "shop" among the various 529 Plans and investment options offered nationwide.

Most QTP sponsors retain professional money managers or offer popular mutual funds.[83] Current QTP investment managers include TIAA-CREF, Merrill Lynch, Fidelity, Vanguard, T. Rowe Price, Salomon Smith Barney, and Morgan Stanley Dean Witter.[84]

Each QTP generally offers multiple investment products and portfolios. For example: (1) Arizona's education investment program offers a "high tech" portfolio;[85] (2) California's education investment program offers a "socially responsible" portfolio;[86] and (3) many QTPs offer "age-based portfolios," with accounts for younger beneficiaries invested largely in equities, shifting to fixed income as the beneficiary approaches college-age.[87]

Contributors may hedge their bets by investing in multiple accounts (either with the same sponsor or different sponsors) with different investment strategies. To the extent a contributor is dissatisfied with investment performance after a contribution has been made, the contributor may make a tax-free qualified rollover to a new QTP account offering a different investment strategy. This "escape hatch" was made easier by the 2001 Act's authorization of a "same beneficiary rollover" once per twelve-month period.[88]

Importantly, in Notice 2001-55,[89] issued 7 September 2001, the IRS recognized that there are a number of situations that might warrant a change in the investment strategy with respect to a 529 Plan account. Notice 2001-55 provides that the IRS expects that final regulations under Code Section 529 will provide that a 529 Plan does not violate Code Section 529(b)(4) if it permits a change in the investment strategy selected for a 529 Plan account once per calendar year and upon a change in the designated beneficiary of the account. The IRS expects that final regulations will also provide that, to qualify under this special rule, a Plan must (1) allow participants to select only from among broad-based investment strategies designed exclusively by the Plan; and (2) establish procedures and maintain appropriate records to prevent a change in investment options from occurring more frequently than under the foregoing circumstances.[90]

---

80. *See* I.R.C. § 529.

81. *See* I.R.C. §§ 529(c)(2), 529(c)(3)(B)(v), 529(c)(3)(B)(vi).

82. I.R.C. § 529(b)(4).

83. 529 PLANS, *supra* note 2, at 5.

84. *Id.*

85. *See* Arizona Family College Savings Program, *Frequently Asked Questions About the College Savings Bank Arizona Family College Savings Program*, *available at* http://arizona.collegesavings.com/azfaqs.shtml (last visited Apr. 21, 2004).

86. *See* Golden State Scholar Share, *College Savings Trust*, *available at* www.scholarshare.com (last visited Apr. 21, 2004) ("California has created The Golden State ScholarShare College Savings Trust. ScholarShare, a new '529' college savings program based on the Internal Revenue Code section that created qualified tuition programs, is designed to help California families and others save in order to meet the increasing costs of higher education.").

87. *See* Virginia College Savings Plan, *available at* www.529Virginia.com (last visited Apr. 21, 2004) (under construction) (outlining Virginia's VEST program regarding age-based evolving portfolios) [hereinafter Virginia College Savings Plan].

88. I.R.C. § 529(c)(3)(c)(iii).

89. 2 C.B. 299 (2001).

90. *Id.*

Excess Funds

To the extent a beneficiary does not use all of the 529 Plan account funds for qualified higher education expenses, the earnings portion of the excess funds will be subject to income tax and an additional ten percent federal tax. The account owner may avoid these consequences, however, by changing the 529 Plan beneficiary or making a qualified rollover to another 529 Plan.[91]

Tax Consequences to Beneficiary

If a beneficiary dies while funds are held in any 529 Plan for his or her benefit, the account balance will be included in the beneficiary's taxable estate, even though the beneficiary had no control over the funds or may have no knowledge of the account's existence. Moreover, a beneficiary may be subject to adverse gift tax and GST tax consequences based upon the account owner's independent acts (such as a rollover to a new account for a beneficiary unrelated to or in a generation below the original beneficiary).[92]

Considerations in Selecting a 529 Plan

Importantly, although the federal statute provides generally applicable guidelines and requirements, individual QTPs may contain additional and varied restrictions. In fact, existing QTPs differ significantly. *It is essential to compare and confirm the terms of a particular QTP before investing. Located at Appendix B is a 529 Plan "checklist" that may serve as a good due diligence tool for the Legal Assistance Officer who is counseling a client on the legal and tax aspects of selecting a QTP or comparing alternative QTPs so the client will understand the terms and options afforded by a QTP before making any investment into a QTP.*

Coverdell Education Savings Accounts (Formerly, "Education IRAs")

In 1997, Congress introduced the Education IRA, governed by new Code Section 530 of the Internal Revenue Code, effective for tax years beginning 1 January 1998.[93] On 26 July 2001, President Bush signed a bill formally renaming Education IRAs "Coverdell Education Savings Accounts" (Coverdell ESAs).[94] As with 529 Plans, a Coverdell ESA is exempt from federal income tax, but is subject to the same rules as a charitable organization regarding taxation of unrelated business income.[95] A Coverdell ESA is a trust created or organized in the United States (and designated as a Coverdell ESA at the time created or organized) exclusively for the purpose of paying the qualified education expenses of an individual who is the designated beneficiary of the trust.[96]

The written instrument creating the trust must meet the following requirements. Contributions to a Coverdell ESA must be in cash; accepted before the date on which the designated beneficiary reaches age 18; and when added to other contributions for the taxable year (except in the case of rollover contributions), limited to $2,000.[97] The trustee must be a bank or other person who satisfactorily demonstrates to the IRS that it will administer the trust consistent with the requirements of Code Section 530 or who has demonstrated the same with respect to a retirement IRA.[98] No part of the trust assets may be invested in life insurance contracts.[99] The trust assets may not be commingled with other property except in a common trust fund or common investment fund.[100] Any account balance must be distributed to the designated beneficiary within thirty days of the earlier of the beneficiary's death, or the beneficiary's thirtieth birthday. There are no age limitations, however, with respect to any designated beneficiary with special needs.[101] The trustee of a Coverdell ESA (or custodian of a qualified custodial account) must make such reports to the Internal Revenue

91. I.R.C. § 529(c)(3)(A), (B), (C).

92. *Id.* § 529(c)(4), (5).

93. Pub. L. No. 107-16, 115 Stat. 38 (1997).

94. Pub. L. No. 107-22, 115 Stat. 196 (2001) (renaming the Education IRAs in memory of the late Senator Paul Coverdell (R-Ga.), a backer of Education IRAs, who died in 2000 as a result of an intracerebral hemorrhage).

95. I.R.C. § 530(a).

96. *Id.* § 530. A custodial account may be treated as a Coverdell ESA trust if the assets of the account are held by a bank or another person who meets the definition of a qualified trustee under Code Section 530(b)(1)(B), and if the custodial account would otherwise qualify as a Coverdell ESA. *Id.*

97. *Id.* § 530(b)(1)(A), (iii).

98. *Id.* § 530(b)(1)(B).

99. *Id.* § 530(b)(1)(C).

100. *Id.* § 530(b)(1)(D).

101. *Id.* § 530(b)(1)(E).

Service and the designated beneficiary as are required by regulations with respect to contributions and distributions.[102]

Income Phase-Out

When the contributor's "modified adjusted gross income" (e.g., adjusted gross income adding back certain foreign income) exceeds $95,000, the amount he or she may contribute to a Coverdell ESA is progressively reduced, and no contribution may be made by a single filer whose modified adjusted gross income exceeds $110,000.[103] The contribution limit for a married contributor filing jointly is reduced when modified adjusted gross income exceeds $190,000 and is fully phased out when modified adjusted gross income exceeds $220,000 (exactly two times the limits for a single filer).[104]

Income Tax Treatment of Coverdell ESA Earnings and Distributions

As with 529 Plans, a Coverdell ESA is exempt from federal income tax, but is subject to the same rules as a charitable organization regarding taxation of unrelated business income.[105] If the aggregate distributions from a Coverdell ESA during a tax year do not exceed the designated beneficiary's qualified education expenses for such year, no amount of the distributions shall be included in the beneficiary's gross income.[106] If the aggregate distributions from a Coverdell ESA during a tax year exceed the designated beneficiary's qualified education expenses for such year, a proportionate amount of the distribution shall be included in the beneficiary's gross income and taxed under the annuity rules under Code Section 72.[107]

Income Tax Treatment of Coverdell ESA Earnings and Distributions

Coordination with Hope and Lifetime Learning Credits

The total amount of qualified education expenses with respect to an individual will be reduced by the amount of such expenses taken into account in determining the Hope or Lifetime Learning credit allowed to the individual.[108] An individual taxpayer may claim the Hope Scholarship credit for payments made to an eligible education institution (e.g., college or vocational school tuition and fees) for qualified tuition and related expenses of an eligible student during the first two years of that student's post-secondary education.[109] The Hope Scholarship credit equals 100 percent of the first $1,000 of tuition and related expenses and fifty percent of the next $1,000 for a maximum annual credit of $1,500 per student.[110]

An individual taxpayer may claim the Lifetime Learning credit for qualified tuition and related expenses paid. The credit amount is equal to twenty percent of the first $10,000 of qualifying tuition and related expenses for a maximum credit of $2,000.[111] Unlike the Hope Scholarship credit, the Lifetime Learning credit is calculated per taxpayer (not per student).[112] However, if a taxpayer elects for a taxable year the Hope Scholarship credit with respect to a student's tuition or related expenses, the Lifetime Learning credit is not available with respect to that same student.[113] The taxpayer may, however, claim the Lifetime Learning credit in the same taxable year with respect to other students. In other words, qualified tuition and related expenses with respect to one student's education cannot be allocated between the two tax credits. Both credits are subject to Phase-Out rules. The allowable amount of the credits is phased out ratably for taxpayers with modified adjusted gross income between $41,000 and $51,000 ($82,000 and $102,000 for joint tax returns).[114] These income ranges are indexed for inflation.[115]

---

102. *Id.* § 530(h).

103. *Id.* § 530(c)(1) (noting the 2001 Act revised the modified adjusted gross income rules to remove the marriage penalty).

104. *Id.*

105. *Id.* § 530(a).

106. *Id.* § 530(d)(2)(A).

107. *Id.* § 530(d)(2)(B).

108. *Id.* § 530(d)(2)(C)(i).

109. *Id.* § 25A(b)(2)(C).

110. *Id.* §§ 25A(b)(1)(A), (B), 25A(h)(1)(A) (inflation adjustment).

111. *Id.* § 25A(c)(1); Treas. Reg. § 1.25A-4(a)(1) (2002).

112. I.R.C. § 25A(c)(1).

113. *Id.* § 25A(c)(2)(A); § 1.25A-4(a)(3).

Coordination with Qualified Tuition Programs

If aggregate distributions to a beneficiary for which the Coverdell ESA provision and the 529 Plan provisions both apply exceed the beneficiary's total qualified education expenses for the tax year, the taxpayer must allocate such expenses among such distributions for purposes of determining taxable income.[116]

Additional Tax on Nonqualified Distributions

General Rule

When a beneficiary receives a Coverdell ESA distribution that is not used for qualified education expenses (and the earnings portion thereof is thus included in the beneficiary's gross income), an additional tax of ten percent is imposed on such amount.[117]

Exceptions

The ten percent additional tax on earnings does not apply if the distribution is made on account of: (1) the beneficiary's death; (2) the beneficiary's disability; (3) the beneficiary's receipt of a scholarship (to the extent of such scholarship)[118] or (4) the distribution of an excess contribution (and earnings thereon), if the distribution is made before the prescribed date (before the 2001 Act, the deadline was April 15 of the following tax year; the 2001 Act extended this date to sixth months after the end of the tax year).[119]

Rollover Contributions

A distribution from a Coverdell ESA will not be included in the designated beneficiary's gross income to the extent such distribution is paid, within sixty days of the distribution, into another Coverdell ESA for the benefit of the same beneficiary or a member of the family of such beneficiary who has not reached age thirty.[120]

Change in Beneficiary

A change in beneficiary of a Coverdell ESA is not treated as a nonqualified distribution if the new beneficiary is a member of the family of the old beneficiary and has not reached age thirty.[121]

Estate and Gift Tax Treatment of Coverdell ESAs

The same gift tax and estate tax rules applicable to 529 Plans apply to Coverdell ESAs.[122]

Considerations in Selecting a 529 Plan

First, although most states allow nonresidents to participate in their QTPs, states may offer certain tax benefits (such as income tax deductions for contributions, matching contributions or scholarships, exemption from state financial aid consideration, or guaranteed returns) to residents only.[123] Some state-sponsored QTPs may require the contributor or beneficiary to be a resident of their state. Residency requirements are more often associated with state-sponsored prepaid tuition plans than state-sponsored education investment plans.[124] Each QTP is managed and invested differently and has its own costs and fees. Investments are typically managed by the program

114. I.R.C. § 25A(d)(1), (2); § 1.25A-1(c)(1).

115. I.R.C. § 25A(h)(2); *see* Rev. Proc. 2002-70, 2002-2 C.B. 845.

116. I.R.C. § 530(d)(2)(C)(ii).

117. *Id.* § 530(d)(4)(A).

118. *Id.* § 530(4)(B).

119. *Id.* § 530(d)(4)(C).

120. *Id.* § 530(d)(5). For purposes of a Coverdell ESA, the phrase "member of the family" of the designated beneficiary has the same definition as in Code Section 529(e)(2). *Id.* § 530(d)(5). A tax-free rollover of a Coverdell ESA may only be made if no rollover has been made within the prior twelve months. *Id.*

121. *Id.* § 530(d)(6).

122. *Id.* § 530(4).

123. *See, e.g.*, VA. CODE ANN. § 58.1-322(D)(7) (LEXIS 2004). This section enables a contribution to be deducted from Virginia taxable income in the amount of the contribution up to $2,000. If age seventy or older, there is no ceiling on the amount of the contribution that can be deducted. *Id*.

124. *See Internet Guide to Coverdell ESA*, *supra* note 27 (containing a state-by-state listing of 529 plan requirements).

sponsor or a professional money manager. Most programs offer the contributor numerous investment options or portfolios upon creation of an account. Contributors should review portfolios offered, past investment performance, and fees.[125] Different QTPs have set different minimum and maximum contribution amounts. As of 1 January 2002, the maximum contribution limit for a Virginia QTP is $250,000.[126] Some QTPs may allow contributions to an account by an account owner only. Certain plans may impose additional restrictions on an account owner's ability to obtain qualified or nonqualified withdrawals and/or subject nonqualified distributions to penalties in addition to the ten percent federal tax.[127] Next, certain plans may restrict the number of times an account owner may change designated beneficiaries or rollover accounts, or restrict an account owner's ability to rollover an account to a different QTP. Also, certain plans may restrict transfers of account ownership during the account owner's lifetime and at death, and have different default provisions in the event a successor account is not designated on a plan form. Some plans may guarantee a fixed (often conservative) rate of return.

Advantages of Coverdell ESAs

Qualified Distributions Exempt from Income Tax

As with 529 Plans, earnings within a Coverdell ESA compound income-tax free, and distributions used for qualified education expenses are exempt from income tax.[128]

Covers Elementary and Secondary School Expenses

The 2001 Act expanded the scope of education expenses to which Coverdell ESA funds may be applied to include elementary and secondary school (kindergarten through grade 12) expenses, as well as higher education expenses. 529 Plans cover higher education expenses only.[129]

Contributor Retains Investment Control

A contributor to a Coverdell ESA may select as custodian any bank, mutual fund company, or other financial institution that can serve as custodian of a traditional IRA, and may invest in any qualifying investments available through the sponsoring institution (e.g., stocks, bonds, mutual funds, certificates of deposit). This allows greater investment control than 529 Plans.

Disadvantages of Coverdell ESAs

Low Contribution Limit

The $2,000 contribution amount still offers limited relief against education costs.[130] In addition, annual maintenance fees affect the investment return on a smaller account balance more significantly.

Contributor Income Phase-out

When the contributor's adjusted gross income exceeds a certain amount ($95,000 for contributors filing singly, $190,000 for a married contributor filing jointly), the maximum contribution amount is reduced, and no contribution may be made by a contributor whose adjusted gross income exceeds a certain amount ($110,000 for contributors filing singly, $220,000 for married contributors filing jointly).[131] Thus, this option is not available to certain individuals.

Beneficiary Age Restrictions

Except with respect to special needs beneficiaries, contributions may only be made for beneficiaries under the age of eighteen.[132]

---

125. Fees for managing the account range from 0.5% to 2% a year, depending on the QTP. Investment performance varies among the programs and portfolios offered. According to a survey conducted by the *Business Week* magazine, Arizona's technology fund, launched in September 2000, lost 48.2% of its value by 31 December 2000, while Louisiana's lone bond fund reported a steady 6.51% gain for 2000, and the 2000 return for Kansas's age-based portfolios ranged from 2.2% to 11.9%. Almost all other programs gained or lost between 8%. *See* Business Week Online, *College Savings Plans Come of Age*, *available at* www.businessweek.com (last visited Mar. 12, 2001).

126. *See* Virginia College Savings Plan, *supra* note 82 (providing Virginia's official program description, including the maximum contribution level of $250,000 per beneficiary).

127. *See Internet Guide to Coverdell ESA*, *supra* note 27 (containing a state-by-state listing of any restrictions, penalties, and other requirements for each state's college savings plan).

128. I.R.C. § 530(a) (2000).

129. I.R.C. § 529(e)(3).

130. I.R.C. § 530(b)(1).

131. I.R.C. § 530(c).

132. I.R.C. § 530(b)(1)(A)(ii).

Irrevocable Gift

Unlike 529 Plans, where the contributor retains the power to reacquire the account funds, a contribution to a Coverdell ESA is treated as an irrevocable gift, and will pass to the beneficiary if not used for educational expenses.[133]

Planning Opportunities

Parents (or Grandparents) with Modest Wealth

For parents with modest wealth, contributions to 529 Plans for their children will provide: (1) tax-free compounding of earnings and superior investment performance as compared with other taxable investment vehicles (such as parents' savings accounts or custodial accounts for children); (2) retained control over when and to whom distributions will be made; (3) retained ability to reacquire funds if desired; and (4) a disciplined savings approach for college costs. Parents whose income falls below the statutory limits may also wish to contribute to Coverdell ESAs to cover primary and secondary school expenses, such as tutoring or purchase of a family computer.

Grandparents with Substantial Wealth

For grandparents with substantial wealth who are comfortable making irrevocable gifts, paying (or prepaying) grandchildren's tuition directly to educational institutions—which payments are excluded from gift tax and GST tax treatment under Code Section 2503(e) and Code Section 2611(b)(1)—will provide tax-free benefits to the grandchildren and reduce the grandparent's estate.[134] In addition to these tuition payments, the grandparent could use his or her annual exclusion amount either to establish a 529 Plan (to pay higher educational expenses other than tuition) or to make other "tax-leveraged" gifts to grandchildren.

Transfer of Funds from Custodial Account

Many QTPs allow transfers of funds from a UGMA or UTMA custodial account to a QTP account for the same beneficiary.[135] Because all contributions must be in cash, any securities or other non-cash property held in the custodial account must first be sold, which may incur taxable income or gain. The transfer of assets from a custodial account to a 529 Plan account should be treated as an investment by the custodian (no gift tax or GST tax consequences). The 529 Plan account remains subject to applicable UGMA/UTMA statute. Any assets refunded from the 529 Plan account are held subject to the UGMA/UTMA statute. The custodian, as account owner of the QTP account, will not have the usual power to change the designated beneficiary, and the designated beneficiary will become the owner of the QTP account when the beneficiary reaches 18 (or 21, depending on the terms of the custodial account).[136]

Trusts as 529 Plan Account Owners

Many 529 Plans now permit trusts to open accounts.[137] In this situation, the Trustee is the account owner, and the trust beneficiary designated by the Trustee is the account beneficiary. Whether a trustee may transfer trust assets to a 529 Plan account will depend on the terms of the trust agreement and applicable fiduciary state law.

Trusts permitting distributions for the beneficiary's education should allow consideration of investment in a 529 Plan account. With respect to existing trusts, the trustee must determine whether the fiduciary investment powers permit investment in a 529 Plan account. Newly drafted trusts could specifically authorize investment in 529 Plan accounts. The trustee must assess the income tax cost of liquidating trust assets to make a 529 Plan contribution versus the income tax benefits of a 529 Plan account.

133. I.R.C. § 530(d)(3), (6).

134. I.R.C. §§ 529(d)(4), (5); Prop. Treas. Reg. § 1.529-5, 63 Fed. Reg. 45,019 (Aug. 24, 1998).

135. Prop. Treas. Reg. § 1.529-2(d)(iv) authorizes QTPs to accept rollovers. Legal assistance attorneys will need to review the actual state QTP to see if such a state sponsored QTP permits a transfer from an existing UGMA or UTMA account. *See* § 1.529-1(c), 63 Fed. Reg. at 45,024 (defining a person to include a trust).

136. Legal assistance attorneys should review the applicable state's implementation of the applicable UGMA/UTMA statute and such state's QTP requirements.

137. *See* I.R.C. § 529(b)(1); § 1.529-1(c), 63 Fed. Reg. at 45,024 (including a trust within the meaning of a "person"). Additionally, attorneys should consult the actual requirements of the particular state QTP under consideration.

The transfer of assets from a trust account to a 529 Plan account should be treated as an investment by the custodian (no gift tax or GST tax consequences). Whether the trustee (as account owner) may change account beneficiary will depend on the terms of the trust agreement (for example, whether the trust has multiple beneficiaries).[138]

If the donor makes gifts to the trust (rather than directly to the 529 Plan account), the gifts may not qualify for the annual exclusion (absent withdrawal rights in the trust), and the gifts will not qualify for the special five-year averaging election.[139]

If trust beneficiary dies while assets remain in 529 Plan account, assets will be included in beneficiary's estate. Use of a trustee as account owner avoids problems related to succession of account ownership in the event of a donor's incapacity or death.[140]

Spendthrift provisions in the trust agreement may provide additional creditor protection.[141]

If the donor is the account owner, a nonqualified withdrawal returns the account assets to the donor's estate (unless the Plan allows a distribution to the beneficiary). If a trustee is the account owner, a nonqualified withdrawal returns the account assets to the trust, outside of the donor's estate, to be administered under the terms of the trust.[142]

Remember to Aggregate Gifts

Although an individual may take advantage of multiple education savings techniques, he or she must remember to aggregate contributions for gift tax purposes.[143]

Plan for Successor Account Ownership in Event of Incapacity or Death

Estate planning questionnaires should now include the question: "Are you the Account Owner under a qualified tuition program (529 Plan) or other education savings account?," and provisions should be made for the designation of one or more contingent account owners in the event the client becomes incapacitated or dies before all funds are distributed from the account.[144]

---

138. I.R.C. § 529.

139. *Id.*

140. *Id.*

141. *Id.*

142. *Id.* § 529(c)(4).

143. *Id.* § 529(c)(2); Prop. Treas. Reg. § 1.529-2(i), 63 Fed. Reg. 45,019 (Aug. 24, 1998). For instance, if in 2002, a parent contributes $10,000 to a 529 Plan account for a child, contributes $2,000 to a Coverdell ESA for a child, and makes an additional $5,000 outright gift (or deemed gift, for example, through a premium payment on insurance held by a *Crummey* trust) to a child, the parent will be deemed to have made a gift of $17,000 to the child, $11,000 of which qualifies for the annual exclusion, and $7,000 of which is taxable (or against which the unified credit must be applied).

144. Note the following in planning for successor account ownership in the event of incapacity or death:

a. Some 529 Plans specifically authorize an account owner's attorney-in-fact under a durable power of attorney to act on the account owner's behalf.

b. Durable powers of attorney may be drafted to expressly authorize actions with regard to 529 Plan accounts (including power to make or revoke gifts), as well as any desired limitations on such actions.

c. Many 529 Plans allow or require the original account owner to list a contingent successor account owner in the event of the original account owner's death. The designation of a successor account owner is made either on a plan document or in the account owner's will.

d. If the 529 Plan account does not provide for the designation of a successor account owner, or if no successor account owner is named or able to act, the terms of the plan will determine who becomes the account owner at the original account owner's death (e.g., the original account owner's estate or spouse, or the beneficiary (or beneficiary's guardian)).

e. If the original account owner's estate becomes the successor account owner, potential problems arise:

(i) Absent a contrary direction in the account owner's will, does the personal representative have a fiduciary duty to withdraw the account assets and maximize the estate assets for the probate beneficiaries?

(ii) If the account assets are withdrawn, to whom do they pass?

(iii) May the personal representative designate a successor account owner?

Conclusion

As the foregoing materials and references suggest, there are a variety of programs available for parents, grandparents, and other contributors to establish a plan which will monetarily enable a child to attend an institution of higher learning.[145] The qualified tuition plans authorized under Internal Revenue Code section 529 are extremely expansive and complex. The legal assistance attorney will be required to become intimately familiar with the terms of the various state-and-private-institution sponsored 529 plans to properly advise his clients. There are many resources available to help the legal assistance attorney to accomplish this undertaking.

145. For example, the Virginia College Savings Plan website provides information on Virginia sponsored QTPs. Virginia is regarded by many tax and financial industry experts as offering the most flexible and sophisticated 529 Plans to the general public. Virginia College Savings Plan, *available at* www.529Virginia.com (under construction) (last visited Apr. 21, 2004).

The College Savings Plan Network, an affiliate of the National Association of State Treasurers, serves as "a clearinghouse for information among college savings programs." Its website includes Frequently Asked Questions, links to each established college savings program, and a summary of the tax advantages (e.g., availability of a state income tax deduction for contributions and state income tax exemption for earnings), age restrictions and portability (e.g., whether certain benefits may be applied to out-of-state schools and whether rollovers permitted) of each program. College Savings Plans Network (CSPN), *About CSPN*, *available at* http://www.collegesavings.org/ (last visited Apr. 21, 2004) ("In 1991, the College Savings Plans Network formed as an affiliate to the National Association of State Treasurers . . . to make higher education more attainable . . . .").

The website, http://www.savingforcollege.com/, founded by college savings plan expert and certified public accountant Joseph F. Hurley, provides legislative updates, links to current articles and college savings programs, and comparisons of programs and investment returns. *Internet Guide to Coverdell ESA*, *supra* note 27.

The College Board website, http://www.collegeboard.com/splash offers calculators, scholarship searches, and other useful facts. The College Board, *Connect to College Success*, *available at* http://www.collegeboard.com/splash (last visited Apr. 21, 2004).

Appendix A

529 Plan Definitions and Special Rules

Designated Beneficiary[146]

> The term "designated beneficiary" means -
>
> (A) the individual designated at the commencement of participation in the QTP as the beneficiary of amounts paid (or to be paid) to the QTP,[147]
>
> (B) in the case of a change of beneficiaries. . . the individual who is the new beneficiary [of the QTP],[148] and
>
> (C) in the case of an interest in a [QTP] purchased by a State or local government . . . [or a Code Section 501(c)(3) charitable organization] as part of a scholarship program operated by such government or organization, the individual receiving such interest as a scholarship.[149]

The designated beneficiary need not be related to the contributor, and under most QTPs the designated beneficiary may be the contributor.[150] Unlike Coverdell Education Savings Accounts, there are no statutory age restrictions on the designated beneficiary of a QTP.[151]

Member of the Family

To qualify for a tax-free change of beneficiary or account rollover, the new beneficiary must be a "member of the family" of the original beneficiary.[152] The term "member of the family" includes:

> (1) A son or daughter, or a descendant of either;
>
> (2) A stepson or daughter;
>
> (3) A brother, sister, stepbrother or stepsister;
>
> (4) The father or mother, or an ancestor of either;
>
> (5) A stepfather or stepmother;
>
> (6) A son or daughter of a brother or sister;
>
> (7) A brother or sister of the father or mother;
>
> (8) A son-in-law, daughter-in-law, mother-in-law, father-in-law, brother-in-law, or sister-in-law;

146. I.R.C. § 529(e)(1).

147. *Id.* § 529(e)(1)(B).

148. *Id.* § 529(e)(1)(C).

149. *Id.* § 529(e)(1).

150. *See id.*

151. *See id.*

152. *Id.* § 529(e)(2); Prop. Treas. Reg. § 1.529-1(c), 63 Fed. Reg. 45,019 (Aug. 24, 1998).

(9) The spouse of the designated beneficiary or the spouse of any individual described in clauses (1) through (8).[153]

(10) My first cousin of an individual described in clauses (1) through (8) above.[154]

Qualified Higher Education Expenses

The term "qualified higher education expenses" includes:

(1) "[T]uition, fees, books, supplies, and equipment required for the enrollment or attendance of a designated beneficiary at an eligible educational institution."[155]

(2) Room and board for students who attend school at least half-time, subject to certain dollar limitations for students living at home or off-campus.[156]

(3) Expenses incurred by a special needs beneficiary for certain services.[157]

(4) There are no dollar limitations on room and board expenses. Room and board expenses are limited by (i) the allowance for room and board included in the student's cost of attendance as established by the educational institution, or (ii) the actual invoice amount charged to the student residing in on-campus housing, if greater.[158]

Eligible Educational Institution

The term "eligible educational institution" is defined as "an institution which is described in section 481 of the Higher Education Act of 1965 (20 U.S.C. § 1088) . . . and which is eligible to participate in a program under title IV of such Act."[159] This definition includes any accredited college, university, vocational school, or other postsecondary educational institution eligible to participate in student aid programs administered by the Department of Education.

When Contributions Deemed Made

A contribution will be deemed made on the last day of a donor's tax year if the contribution is made before the due date of the donor's income tax return (not including extensions).[160]

Account Owner

The Proposed Regulations define "account owner" as the individual "entitled to select or change the designated beneficiary of an account, to designate any person other than the designated beneficiary to whom funds may be paid from the account, or to receive distributions from the account if no such other person is designated."[161] Many QTPs permit persons other than the account owner to make contributions to an account.

153. Pub. L. No. 105-206, § 6004(c)(3), 112 Stat. 685 (1998).

154. I.R.C. § 529(e)(2)(D).

155. *Id.* § 529(e)(3)(A).

156. *Id.* § 529(e)(3)(B).

157. *Id.* § 529(e)(3)(A)(ii).

158. *Id.* § 529(e)(3)(B)(ii).

159. *Id.* § 529(e)(5).

160. *Id.* § 530(b)(5).

Some QTPs allow the account owner to transfer ownership of the QTP during the account owner's lifetime, and many allow a transfer of ownership at the account owner's death by operation of law (under a successor account owner designation on the QTP application) or under the account owner's will.

Neither Code Section 529 nor the proposed regulations address the gift tax or generation-skipping transfer tax consequences of a change in account ownership.[162]

Certain QTPs permit an agent designated under the account owner's durable power of attorney to act if the account owner is incapacitated. If a particular plan expressly permits an attorney-in-fact to act or does not specifically address the issue, an account owner may wish to include language in the account owner's power of attorney specifically authorizing his or her attorney-in-fact to take actions with respect to a QTP.[163]

An account owner must examine the terms of the particular QTP carefully to determine successor ownership at the account owner's death. For example, under certain QTPs, if no successor account owner is designated on the QTP forms, the beneficiary may become the account owner at the age of majority notwithstanding a contrary direction in the original account owner's will.

161. Prop. Treas. Reg. § 1.529-1(c), 63 Fed. Reg. 45,019 (Aug. 24, 1998).

162. *See id.*; I.R.C. § 529.

163. *See* Timothy Guare, *To What Extent May An Attorney-in-Fact Deal with a Qualified State Tuition Program Account Created by a Principal?*, 139 TRUSTS & ESTATES 33 (Sept. 2000).

Appendix B[164]

Selecting a 529 Plan: "Checklist"

Use this checklist to compare the features of different 529 plans. All of this information is readily available from the offering documents each plan provides.

__Who may open the account?

__Is there any limit on who qualifies as an eligible beneficiary?

__Are there any age requirements for the account owner or beneficiary?

__Can I change the account beneficiary? If so, are there any fees assessed by the plan for the change?

__Is the plan available to residents in my state?

__At which colleges, universities, or vocational schools may withdrawals be used? For example, if the 529 plan is a prepaid tuition plan there may be limits on the institutions whose tuition is covered in full.

__Do I have to name a specific school when buying a prepaid tuition plan? If the plan is school-specific, what happens if the student decides to attend a different school or isn't admitted by the school?

__Are prepaid tuition benefits guaranteed by the state?

__How are prepaid plan benefits indexed to tuition inflation? Are they guaranteed to equal actual tuition increases, the state average increase, or a projected increase?

__Does the plan impose any minimum contribution requirements?

__What has been the performance of the various investment options offered by the plan?

__Does my state offer any tax advantages for either contributions made to the account or withdrawals from the account?

__Is there a limit on how often I can invest in the account or on how much I can annually invest in the account?

__What is the maximum amount that I can invest in the account over the life of the account?

__What expenses are covered by plan withdrawals?

__What is the plan's refund policy?

__Are there any special incentives for state residents?

__What fees are associated with my account?

__Is there an account minimum I must maintain to avoid certain fees?

__Can I buy the plan directly from the state or plan sponsor, or must it be purchased through a broker-dealer?

__If I purchase the plan through a broker-dealer, will the broker-dealer impose any additional fees in connection with opening the account?

__Can I change how my money is invested?

__If I consult with a financial advisor, what relationship, if any, does that adviser have with the plan he or she is recommending?

__What investment options are offered by the plan?

__What are the risks associated with each of the investment options?

__Are any of the investment options "age-based" such that the portfolio will be automatically adjusted as the beneficiary gets older?

__Does the plan limit how soon I can begin taking withdrawals from the account?

__Does the plan impose any penalties for withdrawals from the account or impose any account termination fees?

__What customer service does the plan provide (toll-free phone numbers, online account information, regular bulletins or mailings)?

__What happens to existing investments and future investments if the investment manager is changed by the state?

__What if my child does not pursue a post-secondary education?

164. This checklist was compiled from a guide book published in 2002 by The Investment Company Institute, *Saving for Education; A Long-Term Investment, A Guide to Understanding 529 Plans*. You may download a free edition of this guide at the CSPN's website, an affiliate of the National Association of State Treasurers. *See* 529 PLANS, *supra* note 2, at 1.

Labor Law Practice Note

Major John N. Ohlweiler
The Judge Advocate General's Legal Center & School

Equal Employment Opportunity Settlement Negotiations: Does the Union Have A Right to Attend?

A bargaining unit employee filed a formal Equal Employment Opportunity (EEO) complaint alleging several instances of discrimination based on race and sex. During the processing of the complaint, the Department of Defense (DOD) Office of Complaint Investigations (OCI) recommended the parties engage in alternative dispute resolution to discuss a possible settlement. Both parties voluntarily agreed and subsequently reached a settlement regarding the complaint. The union has now filed an Unfair Labor Practice (ULP) claiming that the EEO settlement negotiation was a formal discussion that required the agency to give the union notice and an opportunity to attend. Has the agency committed a ULP?

Introduction

Under the Federal Service Labor-Management Relations Statute (FSLMRS),[1] an agency must give the exclusive representative of an appropriate bargaining unit the opportunity to be represented at any formal discussion between one or more agency representatives and one or more employees in the bargaining unit, or their representatives, concerning any grievance or any personnel policy or practices or other general condition of employment.[2] The purpose of this representational right is to grant the union a meaningful opportunity to participate in any discussions pertaining to the workplace in order to protect and represent the institutional interests of the bargaining unit.[3]

On its face, it is unclear whether this representational right includes union presence at EEO settlement negotiations between the agency and a member-of-the-bargaining-unit-complainant.[4] Arguably, the presence of a third-party-union-representative at such a negotiation might hinder an already difficult process, especially when the complainant does not want a union representative to participate.[5] Nevertheless, if EEO complaints are grievances, and if the settlement negotiation occurs under formal circumstances, then the union's independent right to representation entitles it to a participatory presence at the discussion.

Discussion

The Federal Labor Relations Authority (FLRA) has long asserted that EEO settlement negotiations are formal discussions of grievances under the FSLMRS.[6] The EEOC, however, clearly views the presence of unrequested-third-parties as unnecessary and as a potential impediment to complaint resolu-

1. 5 U.S.C. §§ 7101-7135 (2000).

2. *Id.* § 7114(a)(2).

3. Legislative History of the Federal Service Labor-Management Relations Statute, Title VII of the Civil Service Reform Act of 1978, at 957 (1979). "The union's presence at a formal discussion concerning general working conditions as envisioned by Congress in enacting the Statute was intended to improve the quality of the discussion and allow unions to protect their institutional rights to be the employees' sole representative." Memorandum, Joe Swerdzewski, General Counsel, to Regional Directors, subject: Guidance on Meetings Under the Federal Service Labor-Management Relations Statute–Rights & Obligations and Strategies to Avoid Conflict pt. II.A. (25 Jan. 2001), *available at* http://www.flra.gov/gc/guidance/gc_meet_start.html.

4. Throughout this note, the term negotiation is used interchangeably with mediation, discussion, and alternate dispute resolution. Where the term complainant is used, it always refers to an employee who is also a member of the bargaining unit. Finally, all references to EEO complaints mean formal complaints, filed under 29 C.F.R. § 1614.106, unless otherwise specifically stated. 29 C.F.R. § 1614.106 (2003).

5. "The inclusion of a third party with broader interests and concerns could have a negative impact on this system of reaching individualized settlement of complaints." United States Dep't of Def., Def. Contract Mgmt. Agency, East Indianapolis, Indiana, 59 FLRA 207 (2003) (DCMA) (providing Administrative Law Judge Devaney's opinion describing the argument of the government). *See also* U.S. Dep't of Air Force, 436th Airlift Wing, Dover Air Force Base, Dover, Delaware, 57 FLRA 304 (2001) (Dover I) (stating that the FLRA rejected the hypothetical argument that "union representation (at the EEO mediation) might chill candid discussions").

6. *See* IRS Fresno Serv. Ctr., Fresno, California, 7 FLRA 371 (1981). In this case, the FLRA first held that discussions related to EEO complaints were grievances under the FSLMRS. *Id.* The Ninth Circuit, however, reversed that holding two years later. IRS, Fresno Serv. Ctr. v. FLRA, 706 F.2d 1019 (9th Cir. 1983) (Fresno II) (holding that an EEO pre-complaint conciliation conference is not a formal discussion and does not concern a grievance). In view of the Ninth Circuit's reversal, the FLRA "reexamined" the meaning of grievance and subsequently decided that complaints brought under an alternate statutory appeal procedures (such as EEO) were not grievances under the FSLMRS. Bureau of Gov't Fin. Operations, Headquarters and Nat'l Treasury Employees Union, 15 FLRA 423 (1984) (NTEU I). The Court of Appeals for the District of Columbia, however, subsequently reversed that decision. NTEU v. FLRA, 774 F.2d 1181 (D.C. Cir. 1985) (NTEU II). Since then, the FLRA has consistently held that complaints under a statutory appeals procedure are grievances within the meaning of the FSLMRS. *See* U.S. Dep't of Justice, Bureau of Prisons, Fed. Correctional Inst. (Ray Brook, New York), 29 FLRA 584, 589-90 (1987) (describing the evolution of the FLRA's position on statutory appeals as grievances within the meaning of the FSLMRS), *aff'd sub nom.*, Am. Fed'n of Gov't Employees, Local 3882 v. FLRA, 865 F.2d 1283 (D.C. Cir. 1989) (affirming the FLRA's decision that a grievance within the meaning of section 7114(a)(2)(A) can encompass a statutory appeal); *see also* 5 U.S.C. § 7114(a)(2)(A).

tion. Its position is that "any activity conducted in connection with an agency's ADR program during the EEO process would not be a formal discussion within the meaning of the [FSLMRS]." [7]

In 1999, the Ninth Circuit resolved the apparent conflict holding that EEO settlement discussions were not grievances under the FSLMRS, and therefore did not require notice and an opportunity for union representation.[8] Subsequently, in 2003, the Court of Appeals for the District of Columbia (D.C.) specifically disagreed with the Ninth Circuit and held that EEO settlement negotiations are grievances under the FSLMRS and that the exclusive representative has an independent right to attend to protect the union's interests.[9] In *United States Department of the Air Force, Luke Air Force Base, Arizona* (*Luke III*),[10] the FLRA resolved[11] the conflict between the D.C. and Ninth Circuit. The FLRA held that EEO settlement negotiations are grievances and therefore trigger the notice provisions of the FSLMRS if they occur under formal circumstances.[12]

In *Luke III*, the Air Force conducted three EEO settlement mediations with the complaining employee, without informing the union.[13] The union alleged that these mediation sessions were formal discussions of grievances which triggered their right to notice and an opportunity to attend.[14] In deciding the case, the FLRA focused on three issues: (1) whether an EEO settlement negotiation is formal within the meaning of the FSLMRS; (2) whether the EEO complaint is considered a grievance within the meaning of the FSLMRS; and (3) whether potential union participation undermines the EEOC's exclusive authority to resolve complaints of discrimination.

Whether an EEO Settlement Negotiation Is Formal Under the FSLMRS

In order for the union's representational right to be triggered, the FSLMRS requires: (i) a discussion; (ii) which is formal; (iii) between a representative of the agency and a unit employee; and (iv) which concerns any grievance or any personnel policy or practice or other general condition of employment.[15] In *Luke III*, the FLRA considered the first three elements together, as part of their formality analysis.

In determining whether a discussion is sufficiently formal to trigger the union's representational right, the FLRA considers the totality of the circumstances, to include:

> (1) the status of the individual who held the discussions; (2) whether any other management representatives attended; (3) the site of the discussions; (4) how the meeting for the discussions were called; (5) the length of the discussions; (6) whether a formal agenda was established; and (7) the manner in which the discussions were conducted.[16]

---

7. Federal Sector Equal Employment Opportunity, 64 Fed. Reg. 37,645 (July 12, 1999) (final rule); *see also* 42 U.S.C. § 2000e-4 (stating the authority for enforcing the Civil Rights Act resides with the EEOC); 29 C.F.R. §§ 1614.108(b) (stating agencies are encouraged to settle disputes early using alternate dispute resolution techniques),1614.109(e) (finding attendance at EEOC hearings is limited to those with direct knowledge relating to the complaint); UNITED STATE EQUAL EMPLOYMENT OPPORTUNITY COMM'N MGMT. DIR. 110 ch. 3, sec. I (1999) [hereinafter EEOC MGMT. DIR. 110] (requiring federal agencies to establish an ADR program for EEO complaints and stating that confidentiality is an essential component of such a system; also stating that pre-and post-complaint information "cannot be disclosed to a union unless the complaining party elects union representation or gives his written consent").

8. Luke Air Force Base v. FLRA, 208 F.3d 221 (9th Cir. 1999) (Luke II), *reported in full at* 1999 U.S. App. LEXIS 34569.

9. Dep't of the Air Force, 436th Airlift Wing, Dover Air Force Base v. FLRA, 316 F.3d 280 (D.C. Cir. 2003) (Dover II). *Dover II* provided for one exception to union representation. *See infra* notes 44-48 and accompanying text.

10. 58 FLRA 528 (2003).

11. *See infra* notes 32-34 and accompanying text (discussing the authority of the FLRA to resolve a conflict between circuits).

12. *Luke III*, 58 FLRA at 528.

13. *Id*. at 528-29.

14. *Id*. The union claim alleged a violation of 5 U.S.C. § 7116(a)(1), (8) (2000).

15. 5 U.S.C. § 7114(a)(2)(A).

16. *Luke III*, 58 FLRA at 532. *See also* Gen. Servs. Admin., Region 9 and Am. Fed'n of Gov't Employees, Council 236, 48 FLRA 1348, 1355 (1994) (listing the same seven illustrative indicia of formality) (GSA). "These factors are illustrative, and other factors may be identified and applied as appropriate in a particular case." Luke Air Force Base and Am.Fed'n of Gov't Employees, Local 1547, 54 FLRA 716, 724 (1998) (Luke I) (referencing F.E. Warren Air Force Base, Cheyenne, Wyoming, 52 FLRA 149, 157 (1996)).

Using this list of illustrative factors, the Air Force argued against formality in *Luke III*, claiming that no management representatives directly participated in the negotiation, that there was no formal agenda, and that the sessions were voluntary.[17] The FLRA rejected these arguments and found the EEO mediation sessions to be sufficiently formal to trigger the union's representational rights.

To start, the FLRA completely rejected the argument that there was no direct management exchange with the complaining employee.[18] The FLRA stated that when the mediator served as a go-between for the parties, the employee and management were "engaged in responding to each other's settlement position, and that they were no less engaged than if they had been speaking face-to-face."[19] Regarding the agency's assertion that there was no formal agenda for the negotiations, the FLRA stated that the agenda requirement was satisfied because the mediation sessions were "planned in advance and had . . . clearly-defined objectives and procedures that were communicated [between] all the participants."[20] Finally, while the FLRA acknowledged that the voluntary nature of the mediation sessions mitigated against formality, they specifically found this fact alone insufficient to overcome the other indicia of formality.[21]

The FLRA's analysis in *Luke III* indicates an extremely open approach to determining formality. Under this approach, the FLRA will consider virtually any EEO mediation as formal.[22] Accordingly, while each situation must still be analyzed separately for the indicia of formality, agency counsel are advised to exercise extreme caution before asserting that an EEO settlement negotiation is not sufficiently formal to satisfy the FSLMRS.

Whether the EEO Complaint Is a Grievance Under the FSLMRS

Although the FLRA in *Luke III* found the EEO mediation to be sufficiently formal to satisfy the FSLMRS, the mediation must still concern a grievance or other condition of employment to trigger the union's representational right. Ultimately, the most significant aspect of the decision in *Luke III* was the FLRA's unequivocal statement that EEO settlement negotiations are grievances within the meaning of the FSLMRS.

The FSLMRS defines a grievance as:

> any complaint . . . (A) by any employee concerning any matter relating to the employment of the employee . . . [or concerning either:] (i) the effect or interpretation, or claim of breach, of a [collective bargaining agreement]; or (ii) any claimed violation, misinterpretation, or misapplication of any law, rule, or regulation affecting conditions of employment.[23]

In addressing whether or not a complaint filed under the agency's EEO process fits this definition of grievance, the FLRA in *Luke III* compared the conflicting opinions of the Ninth and D.C. Circuits.

In *Luke II*, a case involving facts similar to those in *Luke III*,[24] the Ninth Circuit found that the term grievance was meant to cover those complaints filed under the collective bargaining agreement's negotiated grievance procedure, not complaints filed under alternate statutory mechanisms.[25] More specifically, the Ninth Circuit stated that the union's representational

17. *Luke III*, 58 FLRA at 530.

18. The Air Force argument was premised on the fact that their management representative was rarely in the same room with the employee and that "the mediator primarily held separate meetings with the parties in which she relayed their respective positions." *Id.* at 533.

19. *Id.* The FLRA specifically avoided the question of whether or not the mediator was a management representative. *Id.*; *see also Luke I*, 54 FLRA at 724-25 (finding it unnecessary to address the air force assertion that the OCI investigator was not a management representative).

20. *Luke III*, 58 FLRA at 533. The FLRA also stated that since the meetings took place away from the employee's work area and in the agency attorney's office, this supported a finding of formality. *Id.* at 532-33.

21. *Id*. at 533.

22. Even in *Luke II*, the Ninth Circuit let stand that aspect of the FLRA's decision which found the EEO negotiations between the complainant and management to be sufficiently formal to satisfy the FSLMRS. Luke II, 208 F.3d 221 (9th Cir. 1999), *reported in full at* 1999 U.S. App. LEXIS 34569.

23. 5 U.S.C. § 7103(a)(9) (2000). The General Counsel has issued guidance stating that informal EEO complaints are not considered grievances under the FSLMRS. *Id.* § 7114(a)(2)(A). Informal EEO complaint meetings, however, might nevertheless constitute formal discussions if the indicia of formality are present and the negotiations concern a personal policy or practice or general condition of employment. *See* Memorandum, Joe Swerdzewski, FLRA General Counsel, to Regional Directors, subject: Guidance on Applying the Requirements of the Federal Service Labor-Management Relations Statute to Processing Equal Employment Opportunity Complaints and Bargaining Over Equal Employment Opportunity Matters (26 Jan. 1999), *available at* http://www.access.gpo.gov/flra/gc/gc_eeo1.html. The General Counsel is currently revising this Guidance. *See* Fresno II, 706 F.2d 1019, 1024 (D.C. Cir. 1983) (holding that a negotiation related to an informal EEO complaint is not a grievance under the FSLMRS).

24. Although *Luke II* and *Luke III* arose at the same Air Force base, they each involved different EEO complainants. *See Luke III*, 58 FLRA at 528; *Luke II*, 1999 U.S. App. LEXIS 34569, at *1.

right was not triggered because the EEO process was "discrete and separate from the grievance process to which 5 U.S.C. [§] . . . 7114 [is] directed."[26] Conversely, four years later in *Dover II*, the Court of Appeals for the District of Columbia specifically rejected this argument and reached the exact opposite conclusion.[27] In *Dover II*, noting that the language of the FSLMRS was extremely broad, the court found that including EEO settlement discussions within the definition of grievance represented "a natural reading of the broad statutory language."[28]

After analyzing both cases, the *Luke III* FLRA adopted the D.C. Circuit's broad interpretation of the FSLMRS's definition of grievance. In reaching its decision, the FLRA relied on the express language, the legislative history, and the intended purpose of the representational rights guaranteed by the FSLMRS.[29] The FLRA found that all three of these factors wholly and absolutely supported the conclusion that EEO settlement negotiations are grievances which trigger representational rights under the FSLMRS. Unlike *Luke III*'s formality analysis, which at least left open the possibility of circumstances when an EEO mediation might not be sufficiently formal,[30] the holding that EEO settlement negotiations are grievances left no room for distinguishing circumstances.[31]

Although *Luke III* arose within the jurisdictional area of the Ninth Circuit, the FLRA's decision was not limited by Ninth Circuit precedent. While it may seem strange that the FLRA could essentially ignore a Court of Appeals decision for the area in which a case arose, the FLRA has specifically noted that the case law of a single circuit does not bind the Authority.[32] The Supreme Court has stated that the FLRA is entitled to "considerable deference when it exercises its special function of applying the general provisions of the [FSLMRS] to the complexities of federal labor relations."[33] Accordingly, in *Luke III*, the FLRA acknowledged, and then specifically (and respectfully) disagreed with the Ninth Circuit's precedent, adopting its own reasoning in finding that EEO settlement discussions are grievances under the FSLMRS.

Since the decision in *Luke III*, the FLRA has twice reaffirmed its position that EEO settlement discussions are grievances which trigger the representational rights of the FSLMRS, to include a second case arising in the jurisdictional area of the Ninth Circuit.[34]

Whether Potential Union Participation Undermines the EEOC's Exclusive Authority to Resolve Complaints of Discrimination

Finally, the *Luke III* decision also addressed the argument that the union's representational right at EEO settlement discussions inappropriately intrudes on the exclusive authority of the EEOC to resolve complaints of discrimination.[35] While this argument represents in part a collateral attack on the formality and grievance elements of the FSLMRS,[36] it is primarily an

25. The Ninth Circuit specifically noted that the collective bargaining agreement at issue explicitly excluded discrimination claims from the negotiated grievance procedure. *Luke II*, 1999 U.S. App. LEXIS 34569, at *5.

26. *Id.*; *see* 5 U.S.C. § 7114.

27. Dover II, 316 F.3d 280, 284-85 (9th Cir. 1999) (citing NTEU II, 774 F.2d 1181 (D.C. Cir. 1985)) (holding that FSLMRS grievances include those filed under alternate statutory procedures, to include the MSPB). The conflict between the Ninth and D.C. Circuits on this issue actually dates back to 1985 when, in *NTEU II*, the D.C. Circuit rejected the Ninth Circuit's argument in *Fresno II*. *See NTEU II*, 774 F.2d at 1181; Fresno II, 706 F.2d 1019 (9th Cir. 1983) (finding no representational right to participate in an EEO precomplaint conciliation conference). Due to some distinguishing facts between these earlier cases, the recent conflicting cases are far more significant.

28. *Dover II*, 316 F.3d at 285 (referencing Dover I, 57 FLRA 304, 309 (2001)).

29. *Luke III*, 58 FLRA at 533.

30. Albeit a slim possibility. *See supra* notes 15-22 and accompanying text.

31. The decision, however, did articulate one possible means by which a union could be excluded from participation. *See infra* notes 44-48 and accompanying text.

32. *See* Headquarters, National Aeronautics and Space Administration, Washington, D.C. and National Aeronautics and Space Administration, Office of the Inspector General, Washington, D.C., 50 FLRA 601, 612-14 (1995), *enforced*, 120 F.3d 1208 (11th Cir. 1997), *aff'd*, 527 U.S. 229 (1999) (stating that the FLRA declined to follow the D.C. Circuit's interpretation of the FSLMRS as it pertains to representatives of an agency).

33. Nat'l Fed'n of Fed. Employees, Local 1309 v. Dep't of the Interior, 526 U.S. 86, 99 (1999). All of the federal circuits have held that a decision of the FLRA may be set aside only if it is "arbitrary, capricious, and abuse of discretion, or otherwise not in accordance with law." Dep't of Veterans Affairs Med. Ctr. v. FLRA, 16 F.3d 1526, 1529 (9th Cir. 1994). *See, e.g.*, Tinker AFB v. FLRA, 321 F.3d 1242 (10th Cir. 2002) (establishing the rule that the circuit will only overturn a decision of the FLRA if it is arbitrary, capricious, or an abuse of discretion); Dep't of Health and Human Srvs. v. FLRA, 844 F.2d 1087, 1090 (4th Cir. 1988) (en banc) (holding that FLRA decisions must be enforced unless they are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law").

34. *See* United States Dep't of the Air Force, Luke Air Force Base, Ariz., 59 FLRA No. 5 (2003) (Luke IV) (finding a ULP when the agency did not provide the union with notice and an opportunity to attend an EEO settlement discussion based on the holding that EEO settlement discussions are formal discussions under the FSLMRS); United States Dep't of Def., Def. Contract Mgmt. Agency, East Indianapolis, Indiana, 59 FLRA No. 34 (2003) (finding a ULP when the agency did not provide the union with notice and an opportunity to attend an EEO settlement discussion based on the holding that EEO settlement discussions are formal discussions under the FSLMRS).

argument about the complaining employees' confidentiality concerns.

The EEOC regulations state that only parties with direct knowledge relating to the complaint may attend EEO hearings.[37] In *Luke III*, the FLRA acknowledged this provision, but stated that since it did not specifically exclude unions, it was not dispositive on the issue of union participation in an otherwise formal discussion.[38] In fact, the FLRA argued that union participation was specifically authorized because the union's institutional interests made them a "party" or a "nonparty participant" under other applicable regulations.[39]

Regarding the argument that union participation might threaten the confidentiality concerns of the complaining employee, the FLRA noted that this was a purely hypothetical concern under the facts of *Luke III*.[40] While the FLRA acknowledged the requirement to maintain confidentiality at EEO proceedings,[41] it questioned the proposition that union participation would automatically violate this confidentiality, asserting that unions are often required to maintain confidentiality within their representational duties. The FLRA suggested that a confidentiality agreement could easily bind the union before participating in an EEO settlement mediation.[42]

Finally, although the FLRA did not address the argument that the union's third-party-presence at an EEO settlement negotiation might hinder the ability to reach an accommodation, it is unlikely that the FLRA would accept such an argument. The purpose of the union's representational right is not to make discussions easier. Rather, the purpose is to protect the institutional interests of the union. More importantly, however, union participation does not necessarily prevent the complainant and the agency from signing a settlement agreement with which the union might disagree.[43]

Direct Conflict Exception

Although *Luke III* unequivocally held that EEO settlement discussions are grievances that trigger the union's representational rights, the FLRA acknowledged one circumstance in which a union might be excluded from participation in a negotiation. Acquiescing in part to the argument that there are potential confidentiality issues associated with some discrimination complaints, the FLRA stated that when there is a "direct conflict" between the union's right to participate in formal discussions and the employee's rights as a victim of discrimination, an "appropriate resolution is required."[44]

---

35. 42 U.S.C. § 2000e-4 (2000) (noting the authority for enforcing the Civil Rights Act resides with the EEOC); 29 C.F.R. 1614.109(e) (2003) (stating attendance at EEOC hearings are limited to those with direct knowledge relating to the complaint).

36. *See supra* notes 15–22 and accompanying text.

37. 29 C.F.R. 1614.109(e) (stating attendance at EEOC hearings is limited to those with direct knowledge relating to the complaint).

38. Luke III, 58 FLRA 528, 534 (2003).

39. *Id.* (citing Dover II, 316 F.3d 280, 310 (9th Cir. 1999) (referencing the Administrative Dispute Resolution Act (ADRA), 5 U.S.C. §§ 571-583). Although unstated, the FLRA would probably extend this argument and assert that the union's institutional interests presume direct knowledge relevant to all grievances.

40. *Luke III*, 58 FLRA at 535. In fact, in *Luke III*, the complaining employee willingly discussed her complaint with the union vice president upon meeting him unexpectedly in the hallway during a break in the mediation. *Id.*

41. 5 U.S.C. § 574 (requiring confidentiality in all alternate dispute resolution proceedings); 29 C.F.R. § 1614.108(b) (stating agencies are encouraged to settle disputes early using alternate dispute resolution techniques); *see also* Federal Sector Alternative Dispute Resolution Fact Sheet (Apr. 17, 2002) ("Fairness requires voluntariness, neutrality, confidentiality, and enforceability."), *available at* http://www.eeoc.gov/federal/adr/facts.html (last visited Apr. 8, 2004); EEO MGMT. DIR. 110, *supra* note 7 (requiring federal agencies to establish an ADR program for EEO complaints and stating the confidentiality is an essential component of such a system).

42. Such confidentiality agreements could either be signed on a case-by-case basis for each EEO mediation, or could be included in the collective bargaining agreement. The consequences of the union refusing to sign a confidentiality agreement raises the possibility of a "direct conflict" which might justify their exclusions from the EEO discussion. *See infra* notes 44-48 and accompanying text.

43. If the settlement involves a change to a condition of employment, the union might have an alternate means of stopping the settlement agreement. *See infra* note 48 and accompanying text.

44. *Luke III*, 58 FLRA at 535 (quoting Dover I, 57 FLRA 304, 309 (2001) (citing NTEU II, 774 F.2d 1181, 1189 n.12 (D.C. Cir. 1985)). In *NTEU II*, the Court of Appeals for the District of Columbia stated that:

> Congress has explicitly decided that a conflict between the rights of identifiable victims of discrimination and the interests of the bargaining unit must be resolved in favor of the former. Title VII of the Civil Rights Act of 1964 . . . provides that the right of an aggrieved employee to complete relief takes priority over the general interests of the bargaining unit . . . a *direct* conflict between the rights of an exclusive representative under § 7114(a)(2)(A) and the *rights* of an employee victim of discrimination should also presumably be resolved in favor of the latter.

774 F.2d at 1189 n.12 (emphasis in original).

Determining what facts are necessary to establish a direct conflict is not clear. The concurring opinion in *Luke III* describes one possibility—when the "employee unequivocally requests that the exclusive representative not be present at a mediation session of a formal [EEO] complaint . . . the rights of the employee should presumably prevail."[45] The D.C. Circuit used this same example to describe a circumstance when it might support excluding the union from an EEO mediation.[46]

Agencies have raised a direct conflict type argument in numerous cases during the last several years. In every case in which it was raised, however, the FLRA has dismissed the argument based on the fact that the conflict issues raised by the agency were always hypothetical. Labor counselors are therefore advised to gather and consider all evidence of a direct conflict between the employee's discrimination complaint and the union's right to representation, to include a determination of the complaining-employee's personal preference regarding the union's presence.[47]

Even if there is a direct conflict which precludes union participation in the EEO settlement negotiations, the union may nevertheless be entitled to notice and an opportunity to bargain if the resulting EEO settlement agreement includes a proposed change to a condition of employment.[48] Therefore, labor counselors are well advised to consider this possibility if they determine exclusion from the EEO settlement negotiation is appropriate under the direct conflict exception.

Proposed Legislation and the National Security Personnel System

The National Defense Authorization Act (Authorization Act) for 2004 almost resolved the conflict of whether or not an EEO settlement negotiation is a formal discussion under the FSLMRS. One version of the proposed Authorization Act specifically sought to reverse the FLRA's position on this issue and legislated that "discussions related to [EEO] complaints are not formal discussions."[49] Although this provision was not contained in the final version of the bill, the Authorization Act contains another provision which might still reverse the FLRA's position on EEO settlement negotiations within the DOD.

The Authorization Act directs the Secretary of Defense to create a new human resources management system for DOD civilians, known as the National Security Personnel System (NSPS).[50] On 6 February 2004, the DOD published an Outline of Proposed Labor Relations System Concepts (NSPS Concepts).[51] Among numerous other changes, the NSPS Concepts included a proposal that no portion of the EEO process will be considered a formal discussion. While the NSPS Concepts have not yet been published for implementation, and while they are still subject to a great deal of union opposition,[52] DOD attorneys would be well-advised to stay abreast of the possibility of change in this area.[53]

---

45. *Luke III*, 58 FLRA at 538 (Member Armendariz, concurring).

46. Dover II, 316 F.3d 280, 287 (D.C. Cir. 2003) ("We do not foreclose the possibility that an employee's objection to the union presence could create a 'direct' conflict that should be resolved in favor of the employee.").

47. The agency must learn the employee's preference without violating the FSLMRS.

48. 5 U.S.C. §§ 7102(2), 7103(a)(14), 7114(b)(2) (2000). Labor counselors should be aware that previous FLRA cases seem to suggest that the union's right to representation at EEO settlement discussions could also be premised on the fact that "discussions of EEO settlement agreements . . . . [are] conditions of employment." Marine Corps Logistics Base, Barstow, California and Am. Fed'n of Gov't Employees, Local 1482, 52 FLRA 1039, 1043 (1997).

49. S. 747, sec. 1103(b) (seeking to amend subpara. (A), sec. 7114(a)(2)).

50. Pub. L. No. 108-136, § 1101, 117 Stat. 1618 (2003) (codified at 5 U.S.C. § 9902). In creating this new civilian personnel system, the law permits the DOD to waive certain laws and regulations that currently apply to civilian employees. The purpose of the NSPS is to allow flexibility in managing civilian employees while insuring compliance with the principles of the merit system and collective bargaining while also giving the DOD flexibility to accomplish its mission of national security.

51. *See* NSPS, *NSPS Labor Relations System, available at* http://www.cpms.osd.mil/nsps/lrs_dod.html (last visited Apr. 12, 2004) (outlining "concepts that the [] (DOD) has developed as part of the beginning of the collaborative process of designing and building a new labor management relations system for DOD employees).

52. *See* Stephen Barr, *Unions Ask Help of Congress on Pentagon's New Civil Service System*, WASH. POST, Mar. 3, 2004, at B2; *Federal Unions Unite to Fight Union Busting Labor Relations Plan at DOD*, FED. EMPLOYEE (NFFE Newsletter), Feb. 2004, at 1; Tia Kauffman, *DOD Personnel Plan Under Fire from Lawmakers, Union*, FED. TIMES, Mar. 8, 2004, at 13; Shawn Zeller, *Senator Blasts Defense Personnel Overhaul Design Process*, GOV'T EXECUTIVE MAG., Mar. 2, 2004.

53. *See* Shawn Zeller, *Pentagon Slows Schedule for Rolling Out New Personnel System*, GOV'T EXECUTIVE MAG., Apr. 14, 2004 (noting that the new labor relations system will be implemented in November 2004). The Department of Homeland Security (DHS) recently proposed rules to "establish a new human resources management system within DHS." Department of Homeland Security Human Resources Management System, 69 Fed. Reg. 8030 (Feb. 20, 2004). Among other things, the DHS regulations specifically exclude all discussions regarding EEO complaints from the definition of formal discussions. *Id*. Practitioners should note that even if the exclusive representative no longer has the representational right to notice and an opportunity to attend discussions regarding EEO complaints, they might still have the right to bargain regarding any change to conditions of employment contained within an EEO settlement agreement. Astute labor counselors will insure that implementation of an EEO settlement agreement that requires a change in a condition of employment will be contingent on the agency fulfilling their statutory duty to bargain with the union.

Conclusion

Until and unless the NSPS is implemented, Army labor counselors should act with caution regarding EEO settlement negotiations. This is crucial because the FLRA requires notice and an opportunity to participate in any EEO settlement negotiation. Even installations located in the Ninth Circuit cannot rely on the *Luke II* decision because that circuit's case law does not bind the FLRA.[54] The FLRA will undoubtedly continue to sanction agencies which do not give the union notice and an opportunity to attend EEO settlement negotiations.

Unless a labor counselor has good facts supporting a direct conflict between the union's representational right and the employee's EEO rights, they should treat EEO settlement negotiations as formal discussions and give the union notice and an opportunity to attend.[55]

54. *See supra* notes 32–33 and accompanying text.

55. Rather than dealing with this conflict when it arises, labor counselors should consider addressing union participation in EEO Settlement Negotiations in the Collective Bargaining Agreement.

Legal Assistance Practice Note

The National "Do-Not-Call" Registry and Other Recent Changes to the Federal Trade Commission's Telemarketing Sales Rule

Major Carissa D. Gregg
The Judge Advocate General's Legal Center & School

Introduction

As *Sergeant Smith* is sitting down for dinner, he hears his phone ring. The telemarketer warns *Sergeant Smith* that if he does not purchase credit card loss protection insurance, he may be liable for all unauthorized charges on his credit card. The telemarketer explains to *Sergeant Smith* that in this computer age, hackers can access his computer and charge massive amounts on his credit card account. The insurance is only a few dollars per month. *Sergeant Smith* buys the insurance to avoid the risk of paying thousands of dollars for someone else's charges. Now, *Sergeant Smith* regrets his hasty decision. Can the law provide him with any relief?

The answer is *yes*. In January 2003, Congress passed the Telemarketing and Consumer Fraud and Abuse Prevention Act[1] which significantly amended the Telemarketing Sales Rule (TSR).[2] Among these amendments, the TSR now requires that when a telemarketer attempts to sell any type of credit card loss protection insurance, the telemarketer must explain to the consumer that the consumer's maximum liability for unauthorized use of his credit card is fifty dollars.[3] Further, the amendments require a telemarketer to provide the consumer's telephone caller identification service with the telemarketer's phone number and, if possible, the telemarketer's company name.[4]

Along with these special protections, the Telemarketing and Consumer Fraud and Abuse Prevention Act amended the TSR in numerous other ways to prevent telemarketing fraud and to thwart the majority of telemarketers from contacting consumers altogether. This note highlights those changes. First, it discusses the "do-not-call" registry, to include exceptions to the registry. Next it covers special protections for certain types of calls. The note then explores unique rules for charity telemarketers, followed by a discussion of the added protections to the unauthorized billing rules. Finally, the note discusses enforcement of the TSR.

The Do-Not-Call Registry

The most far-reaching change stemming from the 2003 amendments to the TSR is the creation of a national do-not-call registry. If a consumer registers[5] his phone number on the FTC's do-not-call list, then a telemarketer cannot call that number[6] unless the telemarketer has express written permission from the consumer to place such calls[7] or the telemarketer and the consumer have an established business relationship.[8] These protections last five years from the original date the phone number is registered.[9] Further, before they make any calls, the TSR

1. 15 U.S.C. §§ 6101-6108 (2000).

2. 16 C.F.R. § 310 (2003). The FTC issued the initial TSR in 1995. *Id.*

3. *Id.* subpt. 310.3(a)(vi).

4. *Id*. subpt. 310.4(a)(7). The TSR allows telemarketers to substitute the name of the seller or charitable organization that they represent if they have an employee who answers the phone number during regular business hours. *Id.*

5. Fifteen states shared their information with the national registry. Consequently, consumers who registered on their respective state's do-not-call list before 26 June 2003 did not have to re-register their numbers on the national list. These states include Alabama, Arkansas, California, Colorado, Connecticut, Florida, Georgia, Kansas, Kentucky, Maine, Massachusetts, Minnesota, New York, North Dakota, and Oklahoma. Federal Trade Commission, *FTC Q&A: The National Do Not Call Registry, available at* http://www.ftc.gov (last visited Mar. 9, 2004) [hereinafter *FTC Q&A*].

6. Even if a consumer does not register his number on the do-not-call list, the FTC amendments still provide a consumer with relief from unwanted calls. A consumer may stop a telemarketer from calling again on behalf of a particular seller if the consumer simply tells the telemarketer that he does not wish to receive calls on behalf of that seller. 16 C.F.R. subpt. 310.4(b)(iii)(B)(i).

7. *Id.* subpt. 310.4(b)(iii)(A). The written agreement must have (1) the consumer's signature; (2) the number the consumer is allowing the telemarketer to call; and (3) the identity of the specific party the consumer is authorizing to call him. *Id*.

8. *Id.* subpt. 310.4(b)(iii)(B)(ii). The TSR defines an "established business relationship" as a relationship between the consumer and seller based on a

> purchase, rental, or lease of the seller's goods or services or a financial transaction between the consumer and seller, within eighteen months immediately proceeding the date of the telemarketing call; or the consumer's inquiry or application regarding a product or service offered by the seller within three months immediately preceding the date of the telemarketing call.

Id.

9. *FTC Q&A*, *supra* note 5. A consumer can verify the date of registration on the FTC's Do-Not-Call Web Site, http://www.donotcall.gov, by clicking on the button "verify registration." *See id*.; *The National Do Not Call Registry, available at* http://www.donotcall.gov (last visited Apr. 12, 2004) [hereinafter *Do Not Call*].

requires telemarketers to access and research the FTC registry for each area code they plan to access.[10]

The national do-not-call registry has been a great success story for the FTC.[11] Between 27 June and 31 December 2003, over fifty-five million consumers registered their phone numbers on the do-not-call list.[12] From 11 October through the end of 2003, consumers lodged only a little over 150,000 complaints[13] of violations of the do-not-call registry.[14]

Unfortunately for consumers, registration on the do-not-call list will not block every telemarketer. For example, a telemarketer calling on behalf of a charity may still contact a consumer until the consumer informs the telemarketer that he does not wish to receive a telephone call on behalf of that charitable organization.[15] Furthermore, as discussed in the following sections, certain entities and calls are exempt from FTC jurisdiction.

Entities Exempt from FTC Jurisdiction

Certain businesses are specifically exempt from the FTC's jurisdiction; therefore, the TSR does not apply to them. These businesses are:

(a) banks, federal credit unions, and federal savings and loans;[16]

(b) common carriers such as long distance telephone companies and airlines;[17] and

(c) non-profit organizations,[18] which could include non-profit credit counseling or credit repair companies.[19]

Thus, these businesses may contact a consumer despite a request for them to stop.

Calls Exempt from the TSR

In addition to certain businesses, the TSR is also inapplicable to certain types of telephone calls.[20] These include:

(a) unsolicited calls from the consumer to the seller;[21]

(b) consumer calls to place catalog orders;[22]

(c) business-to-business calls, unless dealing with office or cleaning supplies;[23] and

(d) calls made in response to general media advertising or direct mail advertising, unless the advertisements relates to business opportunities, credit card loss protection, credit

10. 16 C.F.R. subpt. 310.8. The FTC's fee may range from a minimum of $25 to a maximum fee is $7,375 for each accessed area code. *Id.*

11. According to a Harris Interactive Survey released 13 February 2004, fifty-seven percent of U.S. adults have registered for the do-not-call list; ninety-two percent of those registered stated that they have received fewer telemarketer calls since they registered on the do-not-call registry; and twenty-five percent of those registered say they have received no telemarketing calls since registering. FTC for the Consumer, *Compliance with Do Not Call Registry Exceptional, Over 55 Million Telephone Numbers Registered -- Only 150,000 Complaints in 2003*, *available at* http://www.ftc.gov/opa/2004/02/dncstats0204.htm (last visited Apr. 18, 2004).

12. *Do Not Call*, *supra* note 9 (stating that by the end of 2003, the FTC registered 55,849,898 consumer numbers).

13. A consumer can file a complaint against a telemarketer for violating the do-not-call registry by accessing the FTC's Do-Not-Call web-site. *Id.*

14. *Id.* Eighty-one percent of the complaints were made on the website www.donotcall.gov; nineteen percent of the complaints were made at the toll free number 1-888-382-1222. The states with the highest number of complaints were California, with 22,584 complaints; Florida had 17,845 complaints; and Texas had 10,832 complaints. *Id.*

15. 16 C.F.R. subpt. 310.4(b)(iii)(B)(i).

16. FTC, *Complying with the Telemarketing Sales Rule*, *available at* http://www.ftc.gov/bcp/conline/pubs/buspubs/tsrcomp.htm (last visited Apr. 18, 2004) [hereinafter *Complying with the TSR*].

17. *Id.*

18. *Id.* Non-profit organizations are defined as those entities not organized to carry on business for their own, or their members' profit. *Id.*

19. 16 C.F.R. subpt. 310.3(a)(vi).

20. *Id.* subpt. 310.6(b).

21. *Id.* subpt. 310.6(b)(3). The call is exempt from the TSR unless "upselling" occurs. *See infra* text accompanying note 25.

22. *Id.* subpt. 310.6(b)(5).

23. *Id.* subpt. 310.6(b)(7).

repair advance fee loans, or investment opportunities.[24]

Although the TSR normally does not apply to these calls, if the telemarketer attempts to "upsell" the consumer during the telephone call, the TSR *will* apply.[25] Upselling is when a telemarketer or seller attempts to sell additional goods or services during a single phone call after they complete the initial transaction.[26] For example, if a consumer calls a skin products salesman to order wrinkle cream and, after completing the sale, the seller's employee attempts to sell the consumer diet pills and body lotion, then the TSR would apply to the diet pill and body lotion sales.

Partially Exempt Calls

Certain other calls are only required to follow particular provisions of the TSR. Such phone calls include:

(a) calls relating to the sale of 900 number pay per call services;[27]

(b) calls relating to the sale of franchises or certain business opportunities;[28] and

(c) calls that require a face-to-face presentation to complete the sale.[29]

When making one of these calls, the seller must follow the following provisions of the TSR:

(a) they cannot call numbers on the do-not-call registry or interfere with a consumer's right to register on the list;

(b) they cannot call before 0800 and after 2100 hours;

(c) they cannot abandon calls;[30]

(d) they must still transmit caller identification information; and

(e) they must not annoy, abuse, harass, threaten, intimidate, or use obscene language to the person called.[31]

Special Protection Telemarketing Requirements

As mentioned in the opening scenario, the TSR requires telemarketers to disclose the Fair Credit Billing Act's (FCBA)[32] fifty dollar limit on unauthorized credit card use when trying to sell a credit card loss protection plan.[33] Additionally, if the telemarketer's offer includes a negative option feature,[34] the telemarketer must disclose the following to the consumer:

(a) that the consumer's account will be charged unless the consumer takes an affirmative step to avoid the charges;

(b) the date the account will be charged; and

(c) the specific steps the consumer must take to prevent the charges.[35]

---

24. *Id*. subpt. 310.6(b)(5)-(6).

25. *Id*. subpt. 310.2(dd).

26. *Id*.

27. *Id*. subpt. 310.6(b)(1). These sales are subject to the Telephone Disclosure and Dispute Resolution Act of 1992. *Id.* pt. 308.

28. *Id.* subpt. 310.6(b)(2). The FTC rule, "Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures" regulates these sales. *Id*. pt. 436.

29. *Id*. subpt. 310.6(b)(3).

30. Telemarketers often use automatic dialers to call multiple consumers at once. As a result, a telemarketer may hang up on a consumer when the telemarketer has more than one party on the line—this is known as "abandoning calls." *See Complying with the TSR*, *supra* note 16.

31. 16 C.F.R. subpt. 310.6(b).

32. 15 U.S.C.S. § 1643 (LEXIS 2004). This mandatory information ensures that the consumer can make a well-informed decision on whether the plan is worth the cost.

33. 16 C.F.R. subpt. 310.3(a)(vi).

34. A negative option feature is when the seller interprets the consumer's silence as an acceptance of the offer. An example is the "free trial offer" in which a business sends a consumer a product or service for a trial period at no charge. If the consumer does not affirmatively cancel it, he will have to pay for it. The "book of the month club" is another common example. The plan requires the consumer to make a timely rejection of the offer or the consumer is bound to pay for it. *See Complying with the TSR*, *supra* note 16.

Charity Rules

As previously discussed, the TSR requires telemarketers calling on behalf of charities to disclose the charitable organization's identity and that the purpose of the call is to solicit a charitable contribution.[36] The amended TSR further states that it is a deceptive act or practice if a telemarketer acting on behalf of a charity misrepresents:

> (a) the nature, purpose or mission of the charity;[37]
>
> (b) that the contribution is tax deductible in whole or part;[38]
>
> (c) the purpose for which the contribution will be used;[39]
>
> (d) the percentage of the contribution that will go to the charity;[40]
>
> (e) any material aspect of a prize promotion;[41] or
>
> (f) either the charity's or the telemarketer's affiliation with any person or government agency.[42]

Additional Protections to Restrict Unauthorized Billing

The new TSR provisions specifically list unauthorized billing as an abusive practice.[43] Additionally, the TSR expands previous consumer protections established by the FCBA[44] and the Electronic Funds Transfer Act (EFTA).[45] The TSR protects those transactions that fall outside of the protections of the FCBA and EFTA, such as demand drafts, by requiring telemarketers to obtain express, verifiable authorization from the consumer before billing the consumer.[46]

Submitting billing information for payment without the consumer's express verifiable authorization is also a deceptive business practice or act.[47] The TSR requires that

> (a) the customer's express written authorization have the consumer's signature;[48]
>
> (b) oral authorization must be audio-recorded and show clear evidence of the consumer's authorization of the payment of goods and must show the consumer received the following information:[49]
>
> > (1) the number of payments, if more than one;[50]

35. 16 C.F.R. subpt. 310.3(a)(vii).

36. *Id*. subpt. 310.4(e) (requiring the telemarketer to disclose this information in a truthful, prompt, clear, and concise manner).

37. *Id*. subpt. 310.3(d)(1).

38. *Id*. subpt. 310.3(d)(2).

39. *Id*. subpt. 310.3(d)(3).

40. *Id*. subpt. 310.3(d)(4).

41. *Id.* § 310.3(d)(5). This includes "the odds of being able to receive a prize; the nature and value of the prize; or that the charitable contribution is required to win a prize or to participate in a prize promotion." *Id.*

42. *Id*. subpt. 310.3(d)(6).

43. *Id*. subpt. 310.4(a)(6).

44. 15 U.S.C.S. § 1666 (LEXIS 2004). The FCBA applies to all open-end credit accounts—the most important are consumer credit cards. *See id.*

45. *Id.* § 1693a-r. The EFTA applies to point of sale transfers, automated teller machine transfers, direct deposits or withdrawals, transfers initiated by telephone, and debit card use. The EFTA applies to a consumer's account with a financial institution. *See id*.

46. 16 C.F. R. subpt. 310.4(w). "Pre-acquired account information" is any information that allows the telemarketer to charge the consumer's account without obtaining the information directly from the consumer during that particular telemarketing transaction. *Id.*

47. *Id*. subpt. 310.3(a)(3).

48. *Id*. subpt. 310.3(a)(3)(i). The signature can be electronic or digital. *See id*.

49. *Id*. subpt. 310.3(a)(3)(ii).

50. *Id*. subpt. 310.3(a)(3)(ii)(A) (payments, debits, or charges).

(2) the date the payments will be submitted for payment;[51]

(3) the amount of payment;[52]

(4) the consumer's name;[53]

(5) the consumer's billing information;[54]

(6) a telephone number the consumer can contact during normal business hours with any questions;[55] and

(7) the date of the oral authorization;[56] and

(c) the telemarketer may also send written confirmation of the sale or donation via first class mail with all the information in (1)-(7) above clearly listed along with the information on how to obtain a refund before the consumer submits anything for payment.[57]

If the telemarketer has pre-acquired account information[58] and a free-to-pay conversion[59] feature, the telemarketer must:

(a) obtain from the consumer at least the last four digits of the account to be charged;

(b) obtain from the consumer his express agreement to be charged using that account; and

(c) make an audio recording of the entire transaction.[60]

For all situations other than a free-to-pay conversion, if the telemarketer has pre-acquired information, he is required to:

(a) at a minimum, identify the account to be charged in an understandable way to the consumer; and

(b) obtain from the consumer his express agreement to be charged using the account described.[61]

Enforcement

Violators of the TSR face civil penalties up to $11,000 per count.[62] Unfortunately, the Telemarketing and Consumer Fraud and Abuse Prevention Act only allows for a private cause of action if the plaintiff's damages exceed $50,000.[63] The FTC has the authority to enforce the TSR. State attorneys general, however, are authorized to file suit in federal court for injunctive relief, damages, restitution, and other relief.[64] The Federal Communications Commission administers the Telephone Consumer Protection Act of 1991 (TCPA)[65] which offers a private

51. *Id.* subpt. 310.3(a)(3)(ii)(B).

52. *Id.* subpt. 310.3(a)(3)(ii)(C).

53. *Id.* subpt. 310.3(a)(3)(ii)(D).

54. *Id.* subpt. 310.3(a)(3)(ii)(E). The consumer's billing information must be identified in such a manner that the consumer understands which account will be used for the payment. *Id.*

55. *Id.* subpt. 310.3(a)(3)(ii)(F).

56. *Id.* subpt. 310.3(a)(3)(ii)(G).

57. *Id.* subpt. 310.3(a)(3)(iii). The means of verification cannot be used in a transaction involving free-to-pay conversion and preacquired account information. *Id.*

58. *Id.* subpt. 310.2(a)(6)(i)(A).

59. *Id.* subpt. 310.2(o). A "free-to-pay conversion" occurs when a consumer gets a product for an initial period for free and then incurs an obligation to pay once a certain period expires if the consumer does not take affirmative action. *Id.*

60. *Id.* subpt. 310.4(a)(6)(i)(A)-(C).

61. *Id.* subpt. 310.4(a)(6)(ii)(A)-(B).

62. Section 5(m)(1)(A) of the FTC Act, 15 U.S.C.S. § 45(m)(1)(A) (LEXIS 2004), along with section four of the Federal Civil Penalties Inflation Adjustment Act of 1990, 28 U.S.C.S. § 2461, authorizes the court to award civil penalties of not more than $11,000 for each violation. Further violations can result in an injunction or the requirement to pay redress to a consumer. 28 U.S.C.S. § 2461.

63. 15 U.S.C.S. § 6104(a). If there is a private cause of action, the FTC requires that it receive prior written notice of the complaint. *Id.*

64. *Id.* § 6103(a).

cause of action in state court for violations. The TCPA cause of action is narrower than the Telemarketing and Consumer Fraud and Abuse Prevention Act—the TCPA's main protection is statutory damages of $500 per call (up to $1500 if willful or knowing) if the telemarketing phones before 0800 or after 2100 hours.[66] Most states have enacted some type of protection against telemarketing fraud that provides consumers with a private cause of action.[67] As with all consumer protection issues, it is critical for practitioners to research their respective state laws.

Conclusion

The Telemarketing and Consumer Fraud and Abuse Prevention Act's amendments to the TSR provide consumers with much needed relief from those annoying dinner-time calls by telemarketers. Further, additional protections of the amended TSR thwart the latest schemes of unscrupulous telemarketers, such as the recent credit card loss protection insurance scam which defrauds consumers of their hard earned dollars. Awareness of these new TSR protections will help combat fraudulent and deceptive telemarketers.

65. 47 U.S.C.S. § 227.

66. *Id.* The Act also prohibits (1) sending unsolicited advertisements to fax machines; and (2) using an automatic dialing system to call emergency phone lines, rooms in hospitals and nursing homes, or other services when the called party is charged for receiving the call. The TCPA also prohibits using an artificial or pre-recorded voice to contact a residence without prior consent unless an exception applies. *Id.*

67. State Telemarketing Statutes include the following states: ALA. CODE §§ 8-19A-1–8-19A-24 (2004); ALASKA STAT. § 45.63.010 (2004); ARIZ. REV. STAT. ANN. § 44-1271 (LEXIS 2004); ARK.CODE ANN. § 4-99-101 (Michie 2003); CAL. BUS. & PROF. CODE § 17511 (2004); COLO. REV. STAT. § 6-1-301 (2003); CONN. GEN. STAT. §§ 42-284–42-289 (2003); DEL. CODE ANN. tit. 6, §§ 4401–4405 (2004); FLA. STAT. ANN. § 501.059 (2004); GA. CODE ANN. §§ 10-5B-1–10-5B-8 (2002); HAW. REV. STAT. §§ 481P-1–481P-8 (2003); IDAHO CODE §§ 48-1001–48-1010 (Michie 2004); 815 ILL. COMP. STAT. ANN. 413/1–413/30 (LEXIS 2004); IND. CODE ANN. §§ 24-5-12-1–24-5-12-25 (Michie 2004); IOWA CODE ANN. § 714.8(15) (LEXIS 2004); KAN. STAT. ANN. §§ 50-670–5-675 (2003); KY. REV. STAT. ANN. §§ 367.46951–367.46999 (Michie 2002); LA. REV. STAT. ANN. §§ 45:821–45:831 (LEXIS 2004); ME. REV. STAT. ANN. tit. 10, §§ 1498–1499 (LEXIS 2004); MD. COM. LAW §§ 14-2201–14-2205 (2003); MASS. GEN. LAWS ANN. ch. 159, § 19E (LEXIS 2004); MICH. COMP. LAWS ANN. § 445.111 (LEXIS 2004); MINN. STAT. ANN. § 325E.26-31 (LEXIS 2004); MISS. CODE ANN. §§ 77-3-601–77-3-619 (2004); MONT. CODE ANN. §§ 30-14-1401–30-14-1414 (2003); NEB. REV. STAT. §§ 86-1201–1222 (2004); NEV. REV. STAT. ch. 599B; N.H. REV. STAT. ANN. §§ 359-E:1–359-E:6 (2003); N.J. ADMIN. CODE 13:45A-1.1 (2004); N.M. STAT. ANN. 57-12-22 (Michie 2004); N.Y. PERS. PROP. LAW §§ 440–448 (2004), N.Y. GEN. BUS. LAW § 399-pp (2004); N.C. GEN. STAT. §§ 66-260–66-269 (2004); N.D. CENT. CODE § 51-18 (2004); OHIO REV. CODE ANN. §§ 4719.01–4719.99 (2004); OKLA. STAT. ANN. tit. 15, § 775A (2004); OR. REV. STAT. §§ 646.551–646.578 (2001); 73 PA. STAT. §§ 2241–2249 (2003); R.I. GEN. LAWS §§ 5-61-1–5-61-6 (2003); S.C. CODE ANN. §§ 16-17–445 (2003); S.D. CODIFIED LAWS §§ 37-30A-1–37-30A-17 (Michie 2003); TENN. CODE ANN. § 47-18-1526 (2003); TEX. BUS & COM. CODE ANN. §§ 38.001–44.200 (LEXIS 2004); UTAH CODE ANN. §§ 13-26-1–13-26-11 (2003); VT. STAT. ANN. tit. 9, § 2464 (2003); VA. CODE §§ 59.1-21.1 –59.1-21.7 (LEXIS 2004); WASH. REV. CODE ANN. §§ 19.158.010–19.158.901 (LEXIS 2004); W. VA. CODE ANN. §§ 46A-6F-101–46A-6F-703 (LEXIS 2004); WIS. STAT. ANN. §§ 423.201–423.205 (LEXIS 2003); WYO. STAT. ANN. §§ 40-14-251–40-14-255 (Michie 2003).

Note from the Field

Federal Circuit Clarifies the Total Cost Method of Proving Damages

Major Robert Neill

"If the total cost method of proving damages were not already dead, the [United States Court of Appeals for the Federal Circuit] CAFC drove a stake through its heart with the Propellex Corporation decision."[1]

Introduction

In a recent case, the United States Court of Appeals for the Federal Circuit (CAFC) clarified the requirements for recovery of damages in government contract disputes using a total cost method. In *Propellex Corp. v. Brownlee*,[2] the CAFC affirmed an Armed Services Board of Contract Appeals (ASBCA) decision that denied, in part, Propellex Corporation's (Propellex) modified total cost claim for damages on the basis that Propellex had not established the impracticability of proving its actual losses directly.[3] In its *Propellex* decision, the CAFC interpreted the four requirements for recovery of damages under the total cost method set out in *Servidone Construction Corp. v. United States*.[4] The *Propellex* decision clarified the first of the four *Servidone* proof prerequisites which requires that, in order to recover damages under the total cost method, a contractor must first establish the impracticability of proving its actual losses directly.[5] Here the court held that a contractor cannot establish the impracticability of proving its actual losses directly by unreasonably failing to keep records of its actual costs.[6]

Methods of Establishing Damages

The total cost method is one of several methods a contractor may employ to prove the amount of a claimed equitable adjustment. The accepted methods of proving damages include submitting actual cost data, submitting estimates of actual costs, using a total cost method or a modified total cost method, and using a "jury verdict" method.[7]

Using actual cost data to establish the amount of an equitable adjustment for additional work is the preferred method of proof.[8] Actual cost data "provides the court, or contracting officer, with documented underlying expenses, ensuring that the final amount of the equitable adjustment will be just that—equitable—and not a windfall for either the government or the contractor."[9] In the absence of actual cost data, contractors may use estimates to establish the amount of an equitable adjustment for additional work.[10]

The total cost method of measuring damages, in contrast to the specificity of proving actual damages, consists of merely subtracting the costs in a contractor's bid from its actual cost of the contract.[11] This imprecise method of proof does not identify the specific extra costs incurred as a result of the changes, differing site conditions, or delays encountered in contract performance.[12] Instead, this method assigns liability for all costs in excess of a contractor's bid estimate to the government.

1. Peter A. McDonald, C.P.A., Esq., Remarks at the Annual Meeting of the Boards of Contract Appeals Bar Association (Oct. 22, 2003).

2. 342 F.3d 1335 (Fed. Cir. 2003).

3. Propellex Corp., ASBCA No. 50203, 02-1 BCA ¶ 31,721.

4. 931 F.2d 860, 861 (Fed. Cir. 1991).

5. *Id.*

6. *Id.*

7. Major Thomas C. Modeszto, et al., *Contract and Fiscal Law Developments of 2002—The Year in Review,* ARMY LAW., Jan./Feb. 2003, at 102, n.22 [hereinafter *2002 Year in Review*].

8. *Propellex Corp.*, 342 F.3d at 1338.

9. Dawco Constr., Inc. v. United States, 930 F.2d 872, 882 (Fed. Cir. 1991), *overruled on other grounds by* Reflectone, Inc. v. Dalton, 60 F.3d 1572 (Fed. Cir. 1995).

10. *See* JOHN CIBINIC, JR. & RALPH C. NASH, JR., ADMINISTRATION OF GOVERNMENT CONTRACTS 706 (3d ed. 1995).

11. *Servidone Constr. Corp.*, 931 F.2d at 861.

12. CIBINIC & NASH, *supra* note 10, at 710.

Accordingly, the use of the total cost method to prove damages is not favored.[13]

The modified total cost method of calculating damages uses the total cost method as a starting point, but makes adjustments to allow for various factors (e.g., a below-cost bid) to arrive at a reduced figure that fairly represents "the increased costs the contractor directly suffered from the particular action of [the] defendant which was the subject of the complaint."[14] Use of both the total cost method and the modified total cost method of establishing damages is limited to cases that meet four basic requirements described below.[15]

Apart from using actual costs or estimates, the total cost method, or a modified total cost method to calculate damages, courts and boards have also used a jury verdict method to establish the amount of a contractor's damages when there is clear proof of injury, there is no more reliable method of computing damages, and there is sufficient evidence to make a fair and reasonable approximation of the damages.[16]

The Total Cost Method and the *Servidone* Requirements

The *Servidone* decision sets out four requirements that a contractor must meet in order to use the total cost method to prove its damages.[17] A claimant hoping to employ this method has the burden of proving: "(1) the impracticability of proving actual losses directly; (2) the reasonableness of its bid; (3) the reasonableness of its actual costs; and (4) lack of responsibility for the added costs."[18] A contractor hoping to employ a modified total cost method still must prove all four of these requirements. The *Propellex* court noted in its decision that, "under its modified total cost method claim, Propellex still had the burden of proving the four requirements for a total cost recovery set forth above. The modified method simply was a way of easing that burden somewhat."[19]

The Dispute

In 1988 and 1990, the U.S. Army Armament, Munitions and Chemical Command awarded Propellex two firm fixed-price contracts to deliver Mark 45 electric gun primers to the U.S. Navy for a combined total price of approximately $2.6 million.[20]

The contracts required Propellex to submit production lot samples to the government for testing at the Naval Surface Warfare Center (NSWC) facility in Indian Head, Maryland.[21] This lot acceptance testing included a moisture analysis of the black powder contained in the primers.[22] As a result of this testing, in September 1990, the Army determined that lot six under the first contract did not meet contract requirements, because black powder samples exceeded the maximum allowable moisture content limit.[23] In 1991, the NSWC conducted lot acceptance testing of production lots under the second contract, and the government found lots one through three also exceeded the maximum allowable black powder moisture content limit.[24]

The contracting officer notified Propellex on 18 October 1990 that lot six of the first contract had failed inspection requirements due to excessive black powder moisture content.[25] As a result, Propellex conducted an investigation into the cause of the alleged excessive moisture in the primers and diverted some of its employees to investigate the moisture problem.[26] While it kept records of tests it performed, Propellex's records

13. *See Servidone Constr. Corp.*, 931 F.2d at 861 ("A trial court must use the total cost method with caution and as a last resort.").

14. Propellex Corp. v. Brownlee, 342 F.3d 1335, 1339 (Fed. Cir. 2003).

15. *Id.*

16. WRB Corp. v. United States, 183 Ct. Cl. 409, 425 (1968).

17. *Servidone Constr. Corp.*, 931 F.2d at 861.

18. *Id.*

19. *See Propellex Corp.*, 342 F.3d at 1339.

20. Propellex Corp., ASBCA No. 50203, 02-1 BCA ¶ 31,721.

21. *Id.* at 156,720.

22. *Id.*

23. *Id.* at 156,722.

24. *Id.*

25. *Id.*

26. *Id.*

did not include the number of employees, labor hours, or materials used during testing.[27]

When Propellex completed this investigation, it informed the Army that it found no evidence to indicate that the moisture content of its black powder was excessive.[28] The government and Propellex then jointly observed testing procedures at the NSWC and found defects in the Navy's procedures.[29] The Army ultimately accepted all of the primers that Propellex produced.[30]

Propellex subsequently requested an equitable adjustment of the contract price, asserting that faulty government testing caused it to incur additional costs. On 16 September 1994, Propellex filed a claim with the contracting officer in the amount of $1,790,065 for both contracts.[31] The contracting officer issued a 5 September 1996 final decision admitting "some culpability" and allowing recovery of $77,325, but denying the remainder of Propellex's claim.[32]

The ASBCA Decision

Propellex appealed the contracting officer's final decision to the ASBCA under the Contract Disputes Act of 1978 (CDA).[33] Regarding entitlement, the board determined that the government had failed to conduct the disputed lot acceptance tests under the contract testing requirements.[34] Propellex presented its case for damages before the board using a modified total cost method.[35] In furtherance of its modified total cost claim, Propellex contended that it was impracticable to prove its claimed losses directly because Propellex "did not segregate and record, and could not estimate, the labor hours and costs of the black powder moisture investigation."[36] The labor hours and costs due to Propellex's moisture investigation were commingled with all labor hours and costs of contract performance.[37] Propellex, however, was able to estimate certain costs not attributable to the moisture investigation, and Propellex had documented its moisture investigation efforts.[38]

The ASBCA determined that the contractor had failed to establish the impracticability of proving its claimed losses directly.[39] Additionally, regarding the fourth prerequisite to using the total cost method, the board found that Propellex had not excluded from its claim other additional costs that were not attributable to the moisture investigation.[40] The board held that Propellex could not use the modified total cost method to prove its damages, because Propellex failed to meet two of the *Servidone* requirements.[41] The board awarded the appellant $33,110 plus applicable profit, fees, and interest.[42]

The CAFC Decision

On appeal, Propellex argued that the ASBCA erred in determining that Propellex had failed to prove the impracticability of

27. *Id*. at 156,727.

28. *Id*. at 156,723.

29. *Id*. at 156,725.

30. *Id.* at 156,722. Through bilateral contract modifications, the contracting officer waived the "high moisture content" of the rejected lots and accepted these lots in exchange for price reductions. *Id.*

31. *Id*. at 156,726. By the time of the ASBCA hearing, Propellex claimed $1,356,580 on a modified total cost basis. *Id.* at 156,727.

32. *Id*. at 156,726.

33. 41 U.S.C. § 607 (2000).

34. *Propellex Corp.*, 02-1 BCA ¶ 31,721 at 156,729.

35. Propellex both adjusted its bid for possible understatement [Servidone requirement #2] and excluded from its claim some of the actual incurred costs for which it admitted responsibility [Servidone requirement #4]. Propellex Corp. v. Brownlee, 342 F.3d 1335, 1339 (Fed. Cir. 2003); *see* Servidone Construction Corp. v. United States, 931 F.2d 860 (Fed. Cir. 1991).

36. *Propellex Corp.*, 02-1 BCA ¶ 31,721 at 156,730.

37. *Id.*

38. *Id.*

39. *Id.*

40. *Id.*

41. *Id.*

42. *Id*. at 156,731.

proving its claimed losses directly and had erroneously determined that it failed to satisfy the fourth *Servidone* requirement. The CAFC affirmed the board's decision. It held that substantial evidence supported the ASBCA's conclusion that Propellex had not established the impracticability of proving its actual losses directly.[43] Consequently, the CAFC did not decide whether Propellex met the fourth *Servidone* requirement.[44]

The CAFC found that Propellex had the ability to track the costs of the moisture investigation, but it failed to do so.[45] The CAFC noted that Propellex's controller testified that he could have set up an account in Propellex's cost accounting system to segregate the actual costs of the moisture investigation, but he did not do so.[46] The court also noted that Propellex's facilities manager testified that its labor records should have reflected which employees were engaged in the moisture testing and the amount of time they spent on it.[47] The court rejected Propellex's argument that it did not segregate the costs of its moisture investigation because it believed Propellex—not the government—was responsible for the moisture problem. The CAFC stated that if Propellex believed it was responsible for the problem, "it was all the more important for it to segregate costs relating to that problem from costs incurred under the contracts for which it was entitled to be paid by the Army."[48]

In holding that substantial evidence supported the board's conclusion that Propellex failed to establish the impracticability of proving its actual losses directly, the court clearly articulated the rule it applied:

> Where it is impractical for a contractor to prove its actual costs because it failed to keep accurate records, when such records could have been kept, and where the contractor does not provide a legitimate reason for its failure to keep the records, the total cost method of recovery is not available to the contractor.[49]

What the *Propellex* Decision Means to Practitioners

Government attorneys and contracting officers should carefully scrutinize the evidence of claimed costs that contractors submit in support of their requests for equitable adjustment. Contracting officers should insist on submission of sufficient actual cost data to support the claimed amount of damages before issuing a final decision on a contractor's claim, even if it appears the government may bear responsibility for additional costs incurred by the contractor due to a constructive change, differing site condition, or government-caused delay.

Similarly, contractors must track their actual costs carefully if there is any possibility that additional work is required because of government changes. Contractors are now on increased notice to account for additional costs due to constructive changes as the costs are incurred if they hope to be reimbursed by the government for such costs later. Propellex prevailed on entitlement before the ASBCA, only to lose its quantum case due to its insistence on asserting a total cost claim without the requisite evidence. If Propellex had simply submitted evidence of its actual costs, or had even estimated its actual costs, as it could have done, the appellant would likely have recovered those costs.

In addition, while Propellex used a modified total cost claim, neither the ASBCA decision nor the CAFC decision focused on the modified elements of Propellex's claim; rather, both holdings concerned the basic prerequisites for using any total cost method to prove damages. Accordingly, while the CAFC decision disposed of a modified total cost claim, its holding is broadly applicable to all claims employing a total cost method of proving damages.

Conclusion

While the total cost method may still apply to limited circumstances in which it is truly impossible to segregate additional costs, the CAFC has made it more difficult for claimants to use the total cost method of proving damages, or even a modified total cost method, in its *Propellex* decision. The CAFC will hold would-be total cost method claimants to a very high standard of proving damages. If a contractor can set up its

43. Propellex Corp. v. Brownlee, 342 F.3d 1335, 1342 (Fed. Cir. 2003).

44. *Id.* at 1340.

45. *Id.* at 1341-42.

46. *Id.* at 1341.

47. *Id.* This part of the court's analysis is unclear, because as these were fixed price contracts, there was no reason to segregate the costs for which the contractor believed itself responsible.

48. *Id.* at 1342.

49. *Id.* (citing WRB Corp. v. United States, 183 Ct. Cl. 409, 426 (1968)); Youngdale & Sons Constr. Co. v. United States, 27 Fed. Cl. 516 (1993); S.W. Elecs. & Mfg. Corp., ASBCA Nos. 20698 & 20860, 77-2 BCA ¶ 12,631 (June 23, 1977), *aff'd*, 655 F.2d 1078 (Ct. Cl. 1981).

accounting system to track additional costs resulting from a constructive contract change, but fails to keep such accounting records without a legitimate explanation, the contractor cannot obtain a total cost method recovery.

CLE News

1. Resident Course Quotas

Attendance at resident continuing legal education (CLE) courses at The Judge Advocate General's School, U.S. Army (TJAGSA), is restricted to students who have confirmed reservations. Reservations for TJAGSA CLE courses are managed by the Army Training Requirements and Resources System (ATRRS), the Army-wide automated training system. If you do not have a confirmed reservation in ATRRS, you do not have a reservation for a TJAGSA CLE course.

Active duty service members and civilian employees must obtain reservations through their directorates of training or through equivalent agencies. Reservists must obtain reservations through their unit training offices or, if they are non-unit reservists, through the U.S. Army Personnel Center (ARPERCEN), ATTN: ARPC-OPB, 1 Reserve Way, St. Louis, MO 63132-5200. Army National Guard personnel must request reservations through their unit training offices.

Questions regarding courses should be directed to the Deputy, Academic Department at 1-800-552-3978, dial 1, extension 3304.

When requesting a reservation, please have the following information:

TJAGSA Code—181

Course Name—133d Contract Attorneys Course 5F-F10

Course Number—133d Contract Attorney's Course 5F-F10

Class Number—133d Contract Attorney's Course 5F-F10

To verify a confirmed reservation, ask your training office to provide a screen print of the ATRRS R1 screen, showing by-name reservations.

The Judge Advocate General's School, U.S. Army, is an approved sponsor of CLE courses in all states that require mandatory continuing legal education. These states include: AL, AR, AZ, CA, CO, CT, DE, FL, GA, ID, IN, IA, KS, KY, LA, ME, MN, MS, MO, MT, NV, NH, NM, NY, NC, ND, OH, OK, OR, PA, RI, SC, TN, TX, UT, VT, VA, WA, WV, WI, and WY.

2. TJAGSA CLE Course Schedule (August 2003 - September 2005)

Course Title	Dates	ATTRS No.
	GENERAL	
52d Graduate Course	18 August 03 - 27 May 04	(5-27-C22)
53d Graduate Course	16 August 04 - 26 May 05	(5-27-C22)
54th Graduate Course	15 August 05 - thru TBD	(5-27-C22)
164th Basic Course	1 - 24 June 04 (Phase I - Ft. Lee) 25 June - 3 September 04 (Phase II - TJAGSA)	(5-27-C20) (5-27-C20)
165th Basic Course	14 September - 8 October 04 (Phase I - Ft. Lee) 8 October - 16 December 04 (Phase II - TJAGSA)	(5-27-C20) (5-27-C20)
166th Basic Course	4 - 28 January 05 (Phase I - Ft. Lee) 28 January - 8 April 05 (Phase II - TJAGSA)	(5-27-C20) (5-27-C20)
167th Basic Course	31 May - June 05 (Phase I - Ft. Lee) 25 June - 1 September 05 (Phase II - TJAGSA)	(5-27-C20) (5-27-C20)
168th Basic Course	13 September - thru TBD (Phase I- Ft. Lee) TBD (Phase II – TJAGSA)	(5-27-C20)
9th Speech Recognition Training	25 October - 5 November 04	(512-27DC4)

14th Court Reporter Course	26 April - 25 June 04	(512-27DC5)
15th Court Reporter Course	2 August - 1 October 04	(512-27DC5)
16th Court Reporter Course	24 January - 25 March 05	(512-27DC5)
17th Court Reporter Course	25 April - 24 June 05	(512-27DC5)
18th Court Reporter Course	1 August - 5 October 05	(512-27DC5)
4th Court Reporting Symposium	15 -19 November 04	(512-27DC6)
182d Senior Officers Legal Orientation Course	17 - 21 May 04	(5F-F1)
183d Senior Officers Legal Orientation Course	13 - 17 September 04	(5F-F1)
184th Senior Officers Legal Orientation Course	15 - 19 November 04	(5F-F1)
185th Senior Officers Legal Orientation Course	24 - 28 January 05	(5F-F1)
186th Senior Officers Legal Orientation Course	28 March - 1 April 05	(5F-F1)
187th Senior Officers Legal Orientation Course	13 - 17 June 05	(5F-F1)
188th Senior Officers Legal Orientation Course	12 - 16 September 05	(5F-F1)
11th RC General Officers Legal Orientation Course	19 - 21 January 05	(5F-F3)
34th Staff Judge Advocate Course	7 - 11 June 04	(5F-F52)
35th Staff Judge Advocate Course	6 - 10 June 05	(5F-F52)
7th Staff Judge Advocate Team Leadership Course	7 - 9 June 04	(5F-F52-S)
8th Staff Judge Advocate Team Leadership Course	6 - 8 June 05	(5F-F52-S)
2005 Reserve Component Judge Advocate Workshop	11 - 14 April 05	(5F-F56)
2005 JAOAC (Phase II)	2 - 14 January 05	(5F-F55)

35th Methods of Instruction Course	19 - 23 July 04	(5F-F70)
36th Methods of Instruction Course	18 - 22 July 05	(5F-F70)
2004 JAG Annual CLE Workshop	4 - 8 October 04	(5F-JAG)
15th Legal Administrators Course	21 - 25 June 04	(7A-550A1)
16th Legal Administrators Course	20 - 24 June 05	(7A-550A1)
16th Law for Paralegal NCOs Course	28 March - 1 April 05	(512-27D/20/30)
15th Senior Paralegal NCO Management Course	14 - 18 June 04	(512-27D/40/50)
16th Senior Paralegal NCO Management Course	13 - 17 June 05	(512-27D/40/50)
8th Chief Paralegal NCO Course	14 - 18 June 04	(512-27D- CLNCO)
9th Chief Paralegal NCO Course	13 - 17 June 05	(512-27D- CLNCO)
5th 27D BNCOC	12 - 29 October 04	
6th 27D BNCOC	3 - 21 January 05	
7th 27D BNCOC	7 - 25 March 05	
8th 27D BNCOC	16 May - 3 June 05	
9th 27D BNCOC	1 - 19 August 05	
4th 27D ANCOC	25 October - 10 November 04	
5th 27D ANCOC	10 - 28 January 05	
6th 27D ANCOC	25 April - 13 May 05	
7th 27D ANCOC	18 July - 5 August 05	
4th JA Warrant Officer Advanced Course	12 July - 6 August 04	(7A-270A2)
11th JA Warrant Officer Basic Course	31 May - 25 June 04	(7A-270A0)
12th JA Warrant Officer Basic Course	31 May - 24 June 05	(7A-270A0)
JA Professional Recruiting Seminar	14 - 16 July 04	(JARC-181)

JA Professional Recruiting Seminar	13 - 15 July 05	(JARC-181)

ADMINISTRATIVE AND CIVIL LAW

3d Advanced Federal Labor Relations Course	20 - 22 October 04	(5F-F21)
58th Federal Labor Relations Course	18 - 22 October 04	(5F-F22)
54th Legal Assistance Course	10 - 14 May 04	(5F-F23)
55th Legal Assistance Course	1 - 5 November 04	(5F-F23)
56th Legal Assistance Course	16 - 20 May 05	(5F-F23)
2004 USAREUR Legal Assistance CLE	18 - 22 Oct 04	(5F-F23E)
29th Admin Law for Military Installations Course	14 - 18 March 05	(5F-F24)
2004 USAREUR Administrative Law CLE	13 - 17 September 04	(5F-F24E)
2005 USAREUR Administrative Law CLE	12 - 16 September 05	(5F-F24E)
2004 Federal Income Tax Course (Charlottesville, VA)	29 November - 3 December 04	(5F-F28)
2004 Hawaii Estate Planning Course	20 - 23 January 05	(5F-F27H)
2004 USAREUR Income Tax CLE	13 - 17 December 04	(5F-F28E)
2005 Hawaii Income Tax CLE	11 - 14 January 05	(5F-F28H)
2005 PACOM Income Tax CLE	3 - 7 January 05	(5F-F28P)
22d Federal Litigation Course	2 - 6 August 04	(5F-F29)
23d Federal Litigation Course	1 - 5 August 05	(5F-F29)
2d Ethics Counselors Course	12 - 16 April 04	(5F-F202)
3d Ethics Counselors Course	18 - 22 April 05	(5F-F202)

CONTRACT AND FISCAL LAW

153d Contract Attorneys Course	26 July - 6 August 04	(5F-F10)
154th Contract Attorneys Course	28 February - 11 March 05	(5F-F10)
155th Contract Attorneys Course	25 July - 5 August 05	(5F-F10)
5th Contract Litigation Course	21 - 25 March 05	(5F-F102)
2004 Government Contract Law Symposium	7 - 10 December 04	(5F-F11)
68th Fiscal Law Course	26 - 30 April 04	(5F-F12)
69th Fiscal Law Course	3 - 7 May 04	(5F-F12)
70th Fiscal Law Course	25 - 29 October 04	(5F-F12)
71st Fiscal Law Course	25 - 29 April 05	(5F-F12)
72d Fiscal Law Course	2 - 6 May 05	(5F-F12)
13th Comptrollers Accreditation Course (Fort Monmouth)	14 - 17 June 04	(5F-F14)
6th Procurement Fraud Course	2 - 4 June 04	(5F-F101)
2005 USAREUR Contract & Fiscal Law CLE	10 - 14 January 05	(5F-F15E)
2005 Maxwell AFB Fiscal Law Course	7 - 11 February 05	

CRIMINAL LAW

10th Military Justice Managers Course	23 - 27 August 04	(5F-F31)
11th Military Justice Managers Course	22 - 26 August 05	(5F-F31)
47th Military Judge Course	26 April - 14 May 04	(5F-F33)
48th Military Judge Course	25 April - 13 May 05	(5F-F33)
22d Criminal Law Advocacy Course	13 - 24 September 04	(5F-F34)
23d Criminal Law Advocacy Course	14 - 25 March 05	(5F-F34)
24th Criminal Law Advocacy Course	12 - 23 September 05	(5F-F34)

28th Criminal Law New Developments Course	15 - 18 November 04	(5F-F35)
2005 USAREUR Criminal Law CLE	3 - 7 January 05	(5F-F35E)

INTERNATIONAL AND OPERATIONAL LAW

4th Domestic Operational Law Course	25 - 29 October 04	(5F-F45)
1st Basic Intelligence Law Course (TJAGSA)	28 - 29 June 04	(5F-F41)
2d Basic Intelligence Law Course	27 - 28 June 05	(5F-F41)
1st Advanced Intellgience Law (National Ground Intelligence Center)	30 June - 2 July 04	(5F-F43)
2d Advanced Intellgience Law	29 June - 1 July 04	(5F-F43)
82d Law of War Course	12 - 16 July 04	(5F-F42)
83d Law of War Course	31 January - 4 February 05	(5F-F42)
84th Law of War Course	11 - 15 July 05	(5F-F42)
42d Operational Law Course	9 - 20 August 04	(5F-F47)
43d Operational Law Course	28 February - 11 March 05	(5F-F47)
44th Operational Law Course	8 - 19 August 05	(5F-F47)
2005 USAREUR Operational Law CLE	10 - 14 January 05	(5F-F47E)

3. Civilian-Sponsored CLE Courses

For further information on civilian courses in your area, please contact one of the institutions listed below:

AAJE: American Academy of Judicial Education
P.O. Box 728
University, MS 38677-0728
(662) 915-1225

ABA: American Bar Association
750 North Lake Shore Drive
Chicago, IL 60611
(312) 988-6200

AGACL: Association of Government Attorneys in Capital Litigation
Arizona Attorney General's Office
ATTN: Jan Dyer
1275 West Washington
Phoenix, AZ 85007
(602) 542-8552

ALIABA: American Law Institute-American Bar Association
Committee on Continuing Professional Education
4025 Chestnut Street
Philadelphia, PA 19104-3099
(800) CLE-NEWS or (215) 243-1600

ASLM: American Society of Law and Medicine
Boston University School of Law
765 Commonwealth Avenue
Boston, MA 02215
(617) 262-4990

CCEB: Continuing Education
of the Bar
University of California Extension
2300 Shattuck Avenue
Berkeley, CA 94704
(510) 642-3973

CLA: Computer Law Association, Inc.
3028 Javier Road, Suite 500E
Fairfax, VA 22031
(703) 560-7747

CLESN: CLE Satellite Network
920 Spring Street
Springfield, IL 62704
(217) 525-0744
(800) 521-8662

ESI: Educational Services Institute
5201 Leesburg Pike, Suite 600
Falls Church, VA 22041-3202
(703) 379-2900

FBA: Federal Bar Association
1815 H Street, NW, Suite 408
Washington, DC 20006-3697
(202) 638-0252

FB: Florida Bar
650 Apalachee Parkway
Tallahassee, FL 32399-2300
(850) 561-5600

GICLE: The Institute of Continuing Legal Education
P.O. Box 1885
Athens, GA 30603
(706) 369-5664

GII: Government Institutes, Inc.
966 Hungerford Drive, Suite 24
Rockville, MD 20850
(301) 251-9250

GWU: Government Contracts Program
The George Washington University
National Law Center
2020 K Street, NW, Room 2107
Washington, DC 20052
(202) 994-5272

IICLE: Illinois Institute for CLE
2395 W. Jefferson Street
Springfield, IL 62702
(217) 787-2080

LRP: LRP Publications
1555 King Street, Suite 200
Alexandria, VA 22314
(703) 684-0510
(800) 727-1227

LSU: Louisiana State University
Center on Continuing Professional Development
Paul M. Herbert Law Center
Baton Rouge, LA 70803-1000
(504) 388-5837

MLI: Medi-Legal Institute
15301 Ventura Boulevard, Suite 300
Sherman Oaks, CA 91403
(800) 443-0100

NCDA: National College of District Attorneys
University of Houston Law Center
4800 Calhoun Street
Houston, TX 77204-6380
(713) 747-NCDA

NITA: National Institute for Trial Advocacy
1507 Energy Park Drive
St. Paul, MN 55108
(612) 644-0323 in (MN and AK)
(800) 225-6482

NJC: National Judicial College
Judicial College Building
University of Nevada
Reno, NV 89557

NMTLA: New Mexico Trial Lawyers' Association
P.O. Box 301
Albuquerque, NM 87103
(505) 243-6003

PBI: Pennsylvania Bar Institute
104 South Street
P.O. Box 1027
Harrisburg, PA 17108-1027
(717) 233-5774
(800) 932-4637

PLI: Practicing Law Institute
810 Seventh Avenue
New York, NY 10019
(212) 765-5700

TBA: Tennessee Bar Association
3622 West End Avenue
Nashville, TN 37205
(615) 383-7421

TLS: Tulane Law School
Tulane University CLE
8200 Hampson Avenue, Suite 300
New Orleans, LA 70118
(504) 865-5900

UMLC: University of Miami Law Center
P.O. Box 248087
Coral Gables, FL 33124
(305) 284-4762

UT: The University of Texas School of Law
Office of Continuing Legal Education
727 East 26th Street
Austin, TX 78705-9968

VCLE: University of Virginia School of Law
Trial Advocacy Institute
P.O. Box 4468
Charlottesville, VA 22905

4. Phase I (Correspondence Phase), RC-JAOAC Deadline

The suspense for submission of all RC-JAOAC Phase I (Correspondence Phase) materials is ***NLT 2400, 1 November 2004***, for those judge advocates who desire to attend Phase II (Resident Phase) at TJAGLCS in the year 2005 ("2005 JAOAC"). This requirement includes submission of all JA 151, Fundamentals of Military Writing, exercises.

This requirement is particularly critical for some officers. The 2005 JAOAC will be held in January 2005, and is a prerequisite for most judge advocate captains to be promoted to major.

A judge advocate who is required to retake any subcourse examinations or "re-do" any writing exercises must submit the examination or writing exercise to the Non-Resident Instruction Branch, TJAGLCS, for grading by the same deadline (1 November 2004). If the student receives notice of the need to re-do any examination or exercise after 1 October 2004, the notice will contain a suspense date for completion of the work.

Judge advocates who fail to complete Phase I correspondence courses and writing exercises by 1 November 2004 will not be cleared to attend the 2005 JAOAC. If you have not received written notification of completion of Phase I of JAOAC, you are not eligible to attend the resident phase.

If you have any further questions, contact Lieutenant Colonel JT. Parker, telephone (434) 971-3357, or e-mail JT.Parker@hqda.army.mil.

5. Mandatory Continuing Legal Education Jurisdiction and Reporting Dates

State	Local Official	CLE Requirements
Alabama**	Director of CLE AL State Bar 415 Dexter Ave. Montgomery, AL 36104 (334) 269-1515 http://www.alabar.org/	-Twelve hours per year. -Military attorneys are exempt but must declare exemption. -Reporting date: 31 December.
Arizona	Administrative Assistant State Bar of AZ 111 W. Monroe St. Ste. 1800 Phoenix, AZ 85003-1742 (602) 340-7328 http://www.azbar.org/AttorneyResources/mcle.asp	-Fifteen hours per year, three hours must be in legal ethics. -Reporting date: 15 September.
Arkansas	Secretary Arkansas CLE Board Supreme Court of AR 120 Justice Building 625 Marshall Little Rock, AR 72201 (501) 374-1855 http://courts.state.ar.us/clerules/htm	-Twelve hours per year, one hour must be in legal ethics. -Reporting date: 30 June.
California*	Director Office of Certification The State Bar of CA 180 Howard Street San Francisco, CA 94102 (415) 538-2133 http://calbar.org	-Twenty-five hours over three years, four hours required in ethics, one hour required in substance abuse and emotional distress, one hour required in elimination of bias. -Reporting date/period: Group 1 (Last Name A-G) 1 Feb 01-31 Jan 04 and every thirty-six months thereafter) Group 2 (Last Name H-M) 1 Feb 00 - 31 Jan 03 and every thirty-six months thereafter) Group 3 (Last Name N-Z) 1 Feb 02 - 31 Jan 05 and every thirty-six months thereafter).
Colorado	Executive Director CO Supreme Court Board of CLE & Judicial Education 600 17th St., Ste., #520S Denver, CO 80202 (303) 893-8094 http://www.courts.state.co.us/cle/cle.htm	-Forty-five hours over three year period, seven hours must be in legal ethics. -Reporting date: Anytime within three-year period.

Delaware	Executive Director Commission on CLE 200 W. 9th St. Ste. 300-B Wilmington, DE 19801 (302) 577-7040 http://courts.state.de.us/cle/rules.htm	-Twenty-four hours over two years including at least four hours in Enhanced Ethics. See website for specific requirements for newly admitted attorneys. -Reporting date: Period ends 31 December.
Florida**	Course Approval Specialist Legal Specialization and Education The FL Bar 650 Apalachee Parkway Tallahassee, FL 32399-2300 (850) 561-5842 http://www.flabar.org/newflabar/memberservices/certify/blse600.html	-Thirty hours over a three year period, five hours must be in legal ethics, professionalism, or substance abuse. -Active duty military attorneys, and out-of-state attorneys are exempt. -Reporting date: Every three years during month designated by the Bar.
Georgia	GA Commission on Continuing Lawyer Competency 800 The Hurt Bldg. 50 Hurt Plaza Atlanta, GA 30303 (404) 527-8712 http://www.gabar.org/ga_bar/frame7.htm	-Twelve hours per year, including one hour in legal ethics, one hour professionalism and three hours trial practice. -Out-of-state attorneys exempt. -Reporting date: 31 January.
Idaho	Membership Administrator ID State Bar P.O. Box 895 Boise, ID 83701-0895 (208) 334-4500 http://www.state.id.us/isb/mcle_rules.htm	-Thirty hours over a three year period, two hours must be in legal ethics. -Reporting date: 31 December. Every third year determined by year of admission.
Indiana	Executive Director IN Commission for CLE Merchants Plaza 115 W. Washington St. South Tower #1065 Indianapolis, IN 46204-3417 (317) 232-1943 http://www.state.in.us/judiciary/courtrules/admiss.pdf	-Thirty-six hours over a three year period (minimum of six hours per year), of which three hours must be legal ethics over three years. -Reporting date: 31 December.
Iowa	Executive Director Commission on Continuing Legal Education State Capitol Des Moines, IA 50319 (515) 246-8076	-Fifteen hours per year, two hours in legal ethics every two years. -Reporting date: 1 March.
Kansas	Executive Director CLE Commission 400 S. Kansas Ave. Suite 202 Topeka, KS 66603 (785) 357-6510 http://www.kscle.org	-Twelve hours per year, two hours must be in legal ethics. -Attorneys not practicing in Kansas are exempt. -Reporting date: Thirty days after CLE program, hours must be completed in compliance period 1 July to 30 June.
Kentucky	Director for CLE KY Bar Association 514 W. Main St. Frankfort, KY 40601-1883 (502) 564-3795 http://www.kybar.org/clerules.htm	-Twelve and one-half hours per year, two hours must be in legal ethics, mandatory new lawyer skills training to be taken within twelve months of admissions. -Reporting date: June 30.
Louisiana**	MCLE Administrator LA State Bar Association 601 St. Charles Ave. New Orleans, LA 70130 (504) 619-0140 http://www.lsba.org/html/rule_xxx.html	-Fifteen hours per year, one hour must be in legal ethics and one hour of professionalism every year. -Attorneys who reside out-of-state and do not practice in state are exempt. -Reporting date: 31 January.
Maine	Administrative Director P.O. Box 527 August, ME 04332-1820 (207) 623-1121 http://www.mainebar.org/cle.html	-Eleven hours per year, at least one hour in the area of professional responsibility is recommended but not required. -Members of the armed forces of the United States on active duty; unless they are practicing law in Maine. -Report date: July.
Minnesota	Director MN State Board of CLE 25 Constitution Ave. Ste. 110 St. Paul, MN 55155 (651) 297-7100 http://www.mb-cle.state.mn.us/	-Forty-five hours over a three-year period, three hours must be in ethics, every three years and two hours in elimination of bias. -Reporting date: 30 August.
Mississippi**	CLE Administrator MS Commission on CLE P.O. Box 369 Jackson, MS 39205-0369 (601) 354-6056 http://www.msbar.org/meet.html	-Twelve hours per year, one hour must be in legal ethics, professional responsibility, or malpractice prevention. -Military attorneys are exempt. -Reporting date: 31 July.

Missouri	Director of Programs P.O. Box 119 326 Monroe Jefferson City, MO 65102 (573) 635-4128 http://www.mobar.org/mobarcle/index.htm	-Fifteen hours per year, three hours must be in legal ethics every three years. -Attorneys practicing out-of-state are exempt but must claim exemption. -Reporting date: Report period is 1 July - 30 June. Report must be filed by 31 July.
Montana	MCLE Administrator MT Board of CLE P.O. Box 577 Helena, MT 59624 (406) 442-7660, ext. 5 http://www.montana-bar.org/	-Fifteen hours per year. -Reporting date: 1 March.
Nevada	Executive Director Board of CLE 295 Holcomb Ave. Ste. A Reno, NV 89502 (775) 329-4443 http://www.nvbar.org/	-Twelve hours per year, two hours must be in legal ethics and professional conduct. -Reporting date: 1 March.
New Hampphire**	Asst to NH MCLE Board MCLE Board 112 Pleasant St. Concord, NH 03301 (603) 224-6942, ext. 122 http://www.nhbar.org	-Twelve hours per year, two hours must be in ethics, professionalism, substance abuse, prevention of malpractice or attorney-client dispute, six hours must come from attendance at live programs out of the office, as a student. -Reporting date: Report period is 1 July - 30 June. Report must be filed by 1 August.
New Mexico	Administrator of Court Regulated Programs P.O. Box 87125 Albuquerque, NM 87125 (505) 797-6056 http://www.nmbar.org/mclerules.htm	-Fifteen hours per year, one hour must be in legal ethics. -Reporting period: January 1 - December 31; due April 30.
New York*	Counsel The NY State Continuing Legal Education Board 25 Beaver Street, Floor 8 New York, NY 10004 (212) 428-2105 or 1-877-697-4353 http://www.courts.state.ny.us	-Newly admitted: sixteen credits each year over a two-year period following admission to the NY Bar, three credits in Ethics, six credits in Skills, seven credits in Professional Practice/Practice Management each year. -Experienced attorneys: Twelve credits in any category, if registering in 2000, twenty-four credits (four in Ethics) per biennial reporting period, if registering in 2001 and thereafter. -Full-time active members of the U.S. Armed Forces are exempt from compliance. -Reporting date: every two years within thirty days after the attorney's birthday.
North Carolina**	Associate Director Board of CLE 208 Fayetteville Street Mall P.O. Box 26148 Raleigh, NC 27611 (919) 733-0123 http://www.ncbar.org/CLE/MCLE.html	-Twelve hours per year including two hours in ethics/or professionalism; three hours block course every three years devoted to ethics/professionalism. -Active duty military attorneys and out-of-state attorneys are exempt, but must declare exemption. -Reporting date: 28 February.
North Dakota	Secretary-Treasurer ND CLE Commission P.O. Box 2136 Bismarck, ND 58502 (701) 255-1404 No web site available	-Forty-five hours over three year period, three hours must be in legal ethics. -Reporting date: Reporting period ends 30 June. Report must be received by 31 July.
Ohio*	Secretary of the Supreme Court Commission on CLE 30 E. Broad St. FL 35 Columbus, OH 43266-0419 (614) 644-5470 http://www.sconet.state.oh.us/	-Twenty-four hours every two years, including one hour ethics, one hour professionalism and thirty minutes substance abuse. -Active duty military attorneys are exempt. -Reporting date: every two years by 31 January.
Oklahoma**	MCLE Administrator OK Bar Association P.O. Box 53036 Oklahoma City, OK 73152 (405) 416-7009 http://www.okbar.org/mcle/	-Twelve hours per year, one hour must be in ethics. -Active duty military attorneys are exempt. -Reporting date: 15 February.

Oregon	MCLE Administrator OR State Bar 5200 S.W. Meadows Rd. P.O. Box 1689 Lake Oswego, OR 97035-0889 (503) 620-0222, ext. 359 http://www.osbar.org/	-Forty-five hours over three year period, six hours must be in ethics. -Reporting date: Compliance report filed every three years, except new admittees and reinstated members - an initial one year period.
Pennsylvania**	Administrator PA CLE Board 5035 Ritter Rd. Ste. 500 P.O. Box 869 Mechanicsburg, PA 17055 (717) 795-2139 (800) 497-2253 http://www.pacle.org/	-Twelve hours per year, including a minimum one hour must be in legal ethics, professionalism, or substance abuse. -Active duty military attorneys outside the state of PA may defer their requirement. -Reporting date: annual deadlines: Group 1-30 Apr Group 2-31 Aug Group 3-31 Dec.
Rhode Island	Executive Director MCLE Commission 250 Benefit St. Providence, RI 02903 (401) 222-4942 http:// www.courts.state.ri.us/	-Ten hours each year, two hours must be in legal ethics. -Active duty military attorneys are exempt. -Reporting date: 30 June.
South Carolina**	Executive Director Commission on CLE and Specialization P.O. Box 2138 Columbia, SC 29202 (803) 799-5578 http://www.commcle.org/	-Fourteen hours per year, at least two hours must be in legal ethics/professional responsibility. -Active duty military attorneys are exempt. -Reporting date: 15 January.
Tennessee*	Executive Director TN Commission on CLE and Specialization 511 Union St. #1630 Nashville, TN 37219 (615) 741-3096 http://www.cletn.com/	-Fifteen hours per year, three hours must be in legal ethics/professionalism. -Nonresidents, not practicing in the state, are exempt. -Reporting date: 1 March.
Texas	Director of MCLE State Bar of TX P.O. Box 13007 Austin, TX 78711-3007 (512) 463-1463, ext. 2106 http:// www.courts.state.tx.us/	-Fifteen hours per year, three hours must be in legal ethics. -Full-time law school faculty are exempt (except ethics requirement). -Reporting date: Last day of birth month each year.
Utah	MCLE Board Administrator UT Law and Justice Center 645 S. 200 East Salt Lake City, UT 84111-3834 (801) 531-9095 http://www.utahbar.org/	-Twenty-four hours, plus three hours in legal ethics every two years. -Non-residents if not practicing in state. -Reporting date: 31 January.
Vermont	Directors, MCLE Board 109 State St. Montpelier, VT 05609-0702 (802) 828-3281 http://www.state.vt.us/courts/	-Twenty hours over two year period, two hours in ethics each reporting period. -Reporting date: 2 July.
Virginia	Director of MCLE VA State Bar 8th and Main Bldg. 707 E. Main St. Ste. 1500 Richmond, VA 23219-2803 (804) 775-0577 http://www.vsb.org/	-Twelve hours per year, two hours must be in legal ethics. -Reporting date: 31 October.
Washington	Executive Secretary WA State Board of CLE 2101 Fourth Ave., FL 4 Seattle, WA 98121-2330 (206) 733-5912 http://www.wsba.org/	-Forty-five hours over a three-year period, including six hours ethics. -Reporting date: 31 January.
West Virginia	MCLE Coordinator WV State MCLE Commission 2006 Kanawha Blvd., East Charleston, WV 25311-2204 (304) 558-7992 http://www.wvbar.org/	-Twenty-four hours over two year period, three hours must be in legal ethics, office management, and/or substance abuse. -Active members not practicing in West Virginia are exempt. -Reporting date: Reporting period ends on 30 June every two years. Report must be filed by 31 July.
Wisconsin*	Supreme Court of Wisconsin Board of Bar Examiners Tenney Bldg., Suite 715 110 East Main Street Madison, WI 53703-3328 (608) 266-9760 http:// www.courts.state.wi.us/	-Thirty hours over two year period, three hours must be in legal ethics. -Active members not practicing in Wisconsin are exempt. -Reporting date: Reporting period ends 31 December every two years. Report must be received by 1 February.

Wyoming	CLE Program Director WY State Board of CLE WY State Bar P.O. Box 109 Cheyenne, WY 82003-0109 (307) 632-9061 http://www.wyoming bar.org	-Fifteen hours per year, one hour in ethics. -Reporting date: 30 January.	* Military exempt (exemption must be declared with state) **Must declare exemption.

Current Materials of Interest

1. The Judge Advocate General's School, U.S. Army (TJAGSA) Materials Available through the Defense Technical Information Center (DTIC)

For a complete listing of TJAGSA Materials Available Through the DTIC, see the March 2004 issue of *The Army Lawyer.*

2. Regulations and Pamphlets

For detailed information, see the March 2004 issue of *The Army Lawyer*.

3. The Legal Automation Army-Wide Systems XXI—JAGCNet

a. The Legal Automation Army-Wide Systems XXI (LAAWS XXI) operates a knowledge management and information service called JAGCNet primarily dedicated to servicing the Army legal community, but also provides for Department of Defense (DOD) access in some cases. Whether you have Army access or DOD-wide access, all users will be able to download TJAGSA publications that are available through the JAGCNet.

b. Access to the JAGCNet:

(1) Access to JAGCNet is restricted to registered users who have been approved by the LAAWS XXI Office and senior OTJAG staff:

(a) Active U.S. Army JAG Corps personnel;

(b) Reserve and National Guard U.S. Army JAG Corps personnel;

(c) Civilian employees (U.S. Army) JAG Corps personnel;

(d) FLEP students;

(e) Affiliated (U.S. Navy, U.S. Marine Corps, U.S. Air Force, U.S. Coast Guard) DOD personnel assigned to a branch of the JAG Corps; and, other personnel within the DOD legal community.

(2) Requests for exceptions to the access policy should be e-mailed to:

LAAWSXXI@jagc-smtp.army.mil

c. How to log on to JAGCNet:

(a) Using a Web browser (Internet Explorer 4.0 or higher recommended) go to the following site: http://jagcnet.army.mil.

(b) Follow the link that reads "Enter JAGCNet."

(c) If you already have a JAGCNet account, and know your user name and password, select "Enter" from the next menu, then enter your "User Name" and "Password" in the appropriate fields.

(d) If you have a JAGCNet account, *but do not know your user name and/or Internet password*, contact your legal administrator or e-mail the LAAWS XXI HelpDesk at LAAWSXXI@jagc-smtp.army.mil.

(e) If you do not have a JAGCNet account, select "Register" from the JAGCNet Intranet menu.

(f) Follow the link "Request a New Account" at the bottom of the page, and fill out the registration form completely. Allow seventy-two hours for your request to process. Once your request is processed, you will receive an e-mail telling you that your request has been approved or denied.

(g) Once granted access to JAGCNet, follow step (c), above.

4. TJAGSA Publications Available Through the LAAWS XXI JAGCNet

For detailed information, see the March 2004 issue of *The Army Lawyer*.

5. TJAGSA Legal Technology Management Office (LTMO)

The LTMO continues to improve capabilities for faculty and staff. We have installed new computers throughout the School, all of which are compatible with Microsoft Windows 2000 Professional and Microsoft Office 2000 Professional throughout the School.

The TJAGSA faculty and staff are available through the Internet. Addresses for TJAGSA personnel are available by e-mail at jagsch@hqda.army.mil or by calling the LTMO at (434) 971-3314. Phone numbers and e-mail addresses for TJAGSA personnel are available on TJAGSA Web page at http://www.jagcnet.army.mil/tjagsa. Click on "directory" for the listings.

Personnel desiring to call TJAGSA can dial via DSN 521-7115 or, provided the telephone call is for official business only, use our toll free number, (800) 552-3978; the receptionist will connect you with the appropriate department or directorate.

For additional information, please contact our Legal Technology Management Office at (434) 971-3264. CW3 Tommy Worthey.

6. The Army Law Library Service

Per *Army Regulation 27-1*, paragraph 12-11, the Army Law Library Service (ALLS) must be notified before any redistribution of ALLS-purchased law library materials. Posting such a notification in the ALLS FORUM of JAGCNet satisfies this regulatory requirement as well as alerting other librarians that excess materials are available.

Point of contact is Mr. Dan Lavering, The Judge Advocate General's School, United States Army, ATTN: ALCS-ADD-LB, 600 Massie Road, Charlottesville, Virginia 22903-1781. Telephone DSN: 521-3306, commercial: (434) 971-3306, or e-mail at Daniel Lavering@hqda.army.mil.

Individual Paid Subscriptions to *The Army Lawyer*

Attention Individual Subscribers!

The Government Printing Office offers a paid subscription service to *The Army Lawyer.* To receive an annual individual paid subscription (12 issues) to *The Army Lawyer*, complete and return the order form below (photocopies of the order form are acceptable).

Renewals of Paid Subscriptions

To know when to expect your renewal notice and keep a good thing coming . . . the Government Printing Office mails each individual paid subscriber only one renewal notice. You can determine when your subscription will expire by looking at your mailing label. Check the number that follows "ISSUE" on the top line of the mailing label as shown in this example:

A renewal notice will be sent when this digit is 3.
↓

```
ARLAWSMITH212J          ISSUE003  R  1
JOHN SMITH
212 MAIN STREET
FORESTVILLE MD 20746
```

The numbers following ISSUE indicate how many issues remain in the subscription. For example, ISSUE001 indicates a subscriber will receive one more issue. When the number reads ISSUE000, you have received your last issue unless you renew. You should receive your renewal notice around the same time that you receive the issue with ISSUE003.

To avoid a lapse in your subscription, promptly return the renewal notice with payment to the Superintendent of Documents. If your subscription service is discontinued, simply send your mailing label from any issue to the Superintendent of Documents with the proper remittance and your subscription will be reinstated.

Inquiries and Change of Address Information

The individual paid subscription service for *The Army Lawyer* is handled solely by the Superintendent of Documents, not the Editor of *The Army Lawyer* in Charlottesville, Virginia. Active Duty, Reserve, and National Guard members receive bulk quantities of *The Army Lawyer* through official channels and must contact the Editor of *The Army Lawyer* concerning this service (see inside front cover of the latest issue of *The Army Lawyer*).

For inquiries and change of address for individual paid subscriptions, fax your mailing label and new address to the following address:

United States Government Printing Office
Superintendent of Documents
ATTN: Chief, Mail List Branch
Mail Stop: SSOM
Washington, D.C. 20402

United States Government INFORMATION
PUBLICATIONS • PERIODICALS • ELECTRONIC PRODUCTS

Army Lawyer and Military Review
SUBSCRIPTION ORDER FORM

Order Processing Code: 5937

Easy Secure Internet: **bookstore.gpo.gov**
Toll Free: 866 512-1800
Phone: 202 512-1800
Fax: 202 512-2250
Mail: Superintendent of Documents, PO Box 371954, Pittsburgh, PA 15250-7954

☐ **YES,** enter my subscription(s) as follows:

_____ subscription(s) of the ***Army Lawyer* (ARLAW)** for $45 each ($63 foreign) per year.

_____ subscription(s) of the ***Military Law Review* (MILR)** for $20 each ($28 foreign) per year. The total cost of my order is $_______.

Prices include first class shipping and handling and is subject to change.

Personal name (Please type or print)

Company name

Street address — City, State, Zip code

Daytime phone including area code

Purchase Order Number

Check method of payment:

☐ Check payable to Superintendent of Documents

☐ SOD Deposit Account ☐☐☐☐☐☐☐ — ☐

☐ VISA ☐ MasterCard ☐ Discover/NOVUS ☐ American Express

☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐

☐☐☐☐ (expiration date)

Thank you for your order!

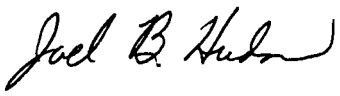
Authorizing signature

11/02

By Order of the Secretary of the Army:

PETER J. SCHOOMAKER
General, United States Army
Chief of Staff

Official:



JOEL B. HUDSON
Administrative Assistant to the
Secretary of the Army
0410502

Department of the Army
The Judge Advocate General's School
U.S. Army
ATTN: JAGS-ADL-P
Charlottesville, VA 22903-1781

PERIODICALS

PIN: 081405-000