

Court Hands Raytheon \$60 Million Victory in CAS 413 Case

Written by Nick Sanders
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On July 16, 2012, Judge Firestone of the U.S. Court of Federal Claims [handed](#) The Raytheon Company another CAS 413 victory in a string of victories won by contractors against the government. What makes this decision so interesting is that it has to do with pension deficits—i.e., having the government make the contractor whole when a segment-closing pension adjustment calculation indicates that the pension plan was underfunded. The majority of decisions to date have focused on the other side of the equation, where the government demands its share of an over-funded pension plan at the time of segment closing.

The decision itself was 149 pages long. It dealt with multiple CAS segments and multiple issues associated with those segments. As you might well imagine, we are only going to provide the highest-level summary of the decision. CAS 413 aficionados (and, yes, some of you are that thing) are advised to read the decision in its entirety.

Raytheon asked for about \$69 million related to segment closing pension adjustments associated with four segments (AIS, Optical, Aerospace, and PWF. Judge Firestone articulate the CAS 412 requirements associated with the adjustments as follows—

When a business segment is closed, the contractor must calculate both the market value of the assets in the pension plan allocated to the segment and the actuarial accrued liability for the segment. The difference between the plan's assets and liabilities indicates the amount by which the plan is over- or under-funded.... Arithmetically, the difference representing the adjustment may be positive, negative, or zero. As a practical matter, the results of these calculations, based on complex actuarial assumptions and the frequent swings of market investments, is rarely, if ever, zero. If the difference is positive, the government may be entitled to a share of the surplus from the contractor. CAS 413- 50(c)(12)(vi). If the difference is negative, the contractor may be entitled to a share of the deficit from the government. ... In either event, the end goal pursued by both the government and the contractor is to settle-up and pay their fair shares to ensure that the pension plans at issue are fully-funded to meet the promises made to the employee-participants covered by the pension plans.

In deciding the case, Judge Firestone had to address several arguments. We summarize her findings and decision with respect to those arguments below.

Novation agreements that Raytheon and the Government executed did not act to waive Raytheon's rights to recover its share of the segment-closing pension adjustment, *because such claims are not contract-specific*

. This is interesting because it approaches the contract adjustments related to the pension

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surplus/deficit calculation from a different viewpoint. So we'll quote the Judge at some length. She wrote—

The consistent and overwhelming evidence adduced at trial establishes that not one of the government or Raytheon employees involved in the processing and signing of the AIS novation agreement or in the negotiations surrounding the AIS CAS 413 segment closing adjustment (several of whom were involved in both) understood that the waiver set forth in the AIS novation agreement, which was taken from FAR 42.1204(i), barred Raytheon's CAS 413 segment closing claim. To the contrary, the evidence established that the government and Raytheon employees involved in the negotiations of both the novation agreement and the CAS 413 segment closing adjustment believed up until issuance of the DCMA/DCAA Joint Guidance in July 2004 that Raytheon was entitled to payment of the government's share of any pension deficit identified in the segment closing calculations undertaken after the AIS sale to L-3. ... The witnesses from both sides explained at trial that the waiver in the novation agreement was included to fulfill the regulatory obligation set out in the FAR and was edited to ensure consistency with the language in FAR 42.1204(i). ... [Thus,] the court concludes that the waiver set forth in the AIS novation agreement, which incorporates the language of the FAR, encompasses only contract-specific claims. The court concludes that the subject waiver did not extend to the AIS CAS 413 segment closing claim *because the AIS segment closing claim is not a contract-specific claim but instead involves a claim to settle-up pension liabilities that are still retained by Raytheon and were not transferred as part of the segment sale*. ... The [novation agreement] waiver is intended to protect the government from multiple claims that might arise 'in connection with' the specific contracts that are transferred from the seller to the buyer ... The provision is focused on what is being transferred and fixes the relationship among the players—the government, the seller, and the buyer—with regard to the obligations that are transferred. In other words, it protects the government from facing the prospect of having to deal with multiple claims arising from the transferred contracts. ... Because Raytheon retains the liability for paying pensions to eligible AIS employees, Raytheon is required to resolve the pension deficit or surplus claim under other open government contracts Raytheon has with the government. The claim is not resolved through the contracts transferred from Raytheon to L-3. Moreover, because Raytheon retained the pension liability separate from any individual contract, the government does not face the possibility of conflicting liability with regard to the contracts transferred to L-3 and therefore the government does not need the AIS novation agreement to protect itself from possible conflicting CAS claims. Raytheon's CAS 413 segment closing claim is thus not 'in connection with' contracts, under the terms of FAR 42.1204(i)(b)(1).

(Emphasis added.)

Judge Firestone used similar logic to conclude that the Government was on the hook for pension deficits related to the Optics segment as well.

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The Judge also addressed assertions by DCAA that Raytheon made errors in its segment-closing pension adjustment calculation. According to DCAA, Raytheon erred by “(a) [basing its calculations] on sales data rather than pension costs and (b) [using] an unrepresentative government participation period.” The DCMA Contracting Officer used the DCAA audit report to find that Raytheon was in noncompliance with the requirements of CAS 413. As Judge Firestone noted, the Government found Raytheon’s calculations acceptable for calculating the amount of the Government’s share of over-funded pension plans (which the Government immediately demanded and Raytheon promptly paid), but did not accept Raytheon’s calculations of the Government’s share of under-funded pension plans (which the Government refused to pay). The basis for the Government’s denial was (in addition to the two alleged errors noted above) that Raytheon had failed to fund pension costs in the current tax year as required by FAR 31.205-6(j). (Readers should note that this particular rationale has been previously dealt with by Judge Firestone, to the detriment of the Government’s position.)

In short, Judge Firestone sided with Raytheon, finding that—

... Raytheon reasonably followed the advice provided in CAS illustration 413-60(c)(9) to determine the government’s share. Put another way, the court finds that it was reasonable for Raytheon to utilize sales data as a proxy for pension cost data when performing its CAS 413 government share calculations, where a reasonable search for historical data was performed, and actual pension cost data could not be located. The court further finds that the government’s reliance on the investigation by Ms. Robbins is misplaced. The investigation relied on assumptions that were not correct and therefore does not provide any basis for second-guessing Raytheon’s government share calculation.

In addition, the Government asserted that Raytheon’s calculations were wrong because “Raytheon failed in its segment closing adjustment to account for pension costs that were paid before the segment closing provisions were added to the CAS in 1978 and for pension costs that were paid in connection with fixed price contracts between 1978 and 1995, before the CAS was amended in 1995.” Raytheon did not dispute the Government’s assertion, and the Judge agreed, that Raytheon’s calculations did not include the Government’s participation in those contracts for those periods.

However, Raytheon argued that the Government’s equitable adjustment was a *separate action* from the segment-closing pension adjustment. According to Judge Firestone, “Raytheon argues that the equitable adjustment must take the form of a CDA claim because the equitable adjustment under FAR 52.230-2 is distinct from the segment closing adjustment required under CAS 413-50(c)(12).” Given this, Raytheon argued that—

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... the government is not entitled to an equitable adjustment in this case because it failed to make a claim against Raytheon or receive a decision from the contracting officer and thus failed to comply with the requirements of the CDA. In such circumstances, Raytheon argues, this court lacks jurisdiction to award the equitable adjustment to the government. Specifically, Raytheon argues that because a prerequisite to an equitable adjustment under the CAS clause at FAR 52.230-2 is a government CDA claim, and because the government never issued a contracting officer's final decision asserting an equitable adjustment, the court lacks jurisdiction to award the government an equitable adjustment.

Judge Firestone agreed with Raytheon and concluded that the Court did not have jurisdiction over the Government's claim for an equitable adjustment, because there was no Contracting Officer's Final Decision (COFD) on the matter.

With respect to the Optical segment, Judge Firestone agreed with the Government that Raytheon made errors in its segment-closing pension adjustment calculation and, consequently, could not recover pension deficits related to that segment. The Government argued that its share of the Optical segment pension surplus should be used to "set-off" monies owed to Raytheon with respect to the other segments. However, Judge Firestone agreed with Raytheon that there was no ability to set-off the segment closing calculations against each other because (as was the case with the equitable adjustment issue) the Government did not follow the requirements of the Contract Disputes Act and did not obtain a COFD. The Judge wrote—

... the court agrees with Raytheon, and holds that because the government's claim for the pension surplus as a set-off is governed by the CDA, and because the government did not comply with the CDA, the court does not have jurisdiction over the government's claim for a set-off based on the Optical segment closing adjustment surplus. ... Because the government's claim for a set-off based on the Optical pension surplus is governed by the CDA, the government must show either that it complied with the CDA or that it is exempt from obtaining an administrative decision from the contracting officer establishing Raytheon's liability for the surplus. ... the government cannot establish this court's jurisdiction over its set-off claim on the grounds that the court has jurisdiction over Raytheon's Optical claim. The fact that there was a decision on Raytheon's claim does not excuse the government from having to provide its own contracting officer decision. Each specific claim has to have been the subject of a contracting officer decision. ... The purpose of this requirement is to ensure that the contractor is on notice of its potential liability. ... Here, Raytheon did not have notice of the government's claim to a pension surplus in connection with the Optical segment closing until trial. To the contrary, the DCMA CIPR Center initially approved, and the DCAA did not take exception to, Raytheon's pension deficit calculation for the Optical segment, except insofar as it included a deficit for PRBs. ... Raytheon would have had no reason to suspect that the government would later seek a set-off. Indeed, there was no suggestion by any government official that Raytheon might owe the government a payment following the Optical segment

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closing. Thus, Raytheon did not have any notice of the government's claim, contrary to the requirements of the CDA. ... In sum, because the government needed a CDA decision in order to obtain payment from Raytheon for the Optical pension surplus and failed to obtain one, and because the court cannot find any reason for excusing the government's failure to comply with the CDA's jurisdictional requirements, this court will not exercise jurisdiction over the government's claim for a set-off of the pension surplus arising from the Optical segment closing.

The Judge also found that Raytheon's PFW segment was not a "segment" as defined by CAS, and thus Raytheon could not recover pension deficits related to that business. The Judge wrote—

There was no evidence introduced to show that PWF itself reported directly to a home office. Second, the government relies on testimony to show that PWF never had any CAS contracts or subcontracts of its own and thus the government never directly reimbursed PWF for its pension costs.

With respect to Raytheon's Aerospace segment, the Court sided with Raytheon and found that the Government was liable for its share of the deficit calculated by the segment-closing pension adjustment, for much the same reasons as discussed with respect to the other segments.

In total, Judge Firestone awarded Raytheon \$59.2 Million of the \$69 Million it was seeking.

We wonder how much Raytheon would have settled for, had the Government been willing to enter into negotiations, rather than litigate the matter.