ARMED SERVICES BOARD OF CONTRACT APPEALS

Appeal of --	)	
	)	
MPR Associates, Inc.	)	ASBCA No. 54689
	)	
Under Contract Nos. N00024-91-C-2106	)	
N61533-94-D-0049	)	
N00014-97-C-2049	)	
N00173-98-C-2018	)	

APPEARANCE FOR THE APPELLANT: Mr. Douglas M. Chapin
Principal Officer

APPEARANCES FOR THE GOVERNMENT: E. Michael Chiaparas, Esq.
Acting Chief Trial Attorney
Sharon K. Parr, Esq.
Trial Attorney
Defense Contract Management Agency
Manassas, VA

OPINION BY ADMINISTRATIVE JUDGE KETCHEN
UNDER RULE 12.3

MPR Associates, Inc. (MPR or appellant) appeals from a government claim under FAR 31.205-36(b)(3). The government seeks reimbursement of allegedly unallowable lease rental costs in the amount of $85,981 for fiscal years (FYs) 1996-98 for MPR's lease of space in a building owned by 320 King Street LLC (320 King LLC) that has the same owners as MPR. Appellant elected an accelerated proceeding pursuant to Rule 12.3. The parties elected to have the appeal decided on the record pursuant to Rule 11. We sustain the appeal.

FINDINGS OF FACT

1. The government awarded to MPR four cost reimbursable contracts for the purpose of providing engineering services: Contract No. N00024-91-C-2106, dated 14 December 1990 (contract 2106); Contract No. N61533-94-D-0049, dated 9 September 1994 (contract 0049); Contract No. N00014-97-C-2049, dated 31 July 1997 (contract 2049); and Contract No. N00173-98-C-2018, dated 7 May 1998 (contract 2018). The contracting officer assigned contract administration for each contract to the Defense Contract Management Agency (DCMA) (or a predecessor organization of DCMA). These contracts incorporated by reference, *inter alia*, FAR 52.216-7, ALLOWABLE COST

AND PAYMENT (APR 1984, JUL 1991, FEB 1997, APR 1998, respectively). This clause applies FAR Part 31 CONTRACT COST PRINCIPLES AND PROCEDURES to MPR's contracts by reference. (R4, tabs 1-4) MPR's fiscal year is the same as the calendar year.

2. The FAR 52.216-7, ALLOWABLE COST AND PAYMENT (APR 1998) clause provides, in pertinent part, as follows:

> (a) *Invoicing.* The Government shall make payments to the Contractor when requested as work progresses . . . in amounts determined to be allowable by the Contracting Officer in accordance with Subpart 31.2 of the Federal Acquisition Regulation (FAR) in effect on the date of this contract and the terms of this contract. . . .
>
> (b) *Reimbursing costs.*
>
> . . . .
>
> (3) Notwithstanding the audit and adjustment of invoices or vouchers under paragraph (g) below, allowable indirect costs under this contract shall be obtained by applying indirect cost rates established in accordance with paragraph (d) below.
>
> . . . .
>
> (d) *Final indirect cost rates.* (1) Final annual indirect cost rates and the appropriate bases shall be established in accordance with Subpart 42.7 of the Federal Acquisition Regulation (FAR) in effect for the period covered by the indirect cost rate proposal.
>
> (2)(i) . . .
>
> (ii) The proposed rates shall be based on the Contractor's actual cost experience for that period. The appropriate Government representative and the Contractor shall establish the final indirect cost rates as promptly as practical after receipt of the Contractor's proposal.
>
> (3) The Contractor and the appropriate Government representative shall execute a written understanding setting

> forth the final indirect cost rates. The understanding shall specify (i) the agreed-upon final annual indirect cost rates. . . . The understanding is incorporated into this contract upon execution.
>
> . . . .
>
> (5) Failure by the parties to agree on a final annual indirect cost rate shall be a dispute within the meaning of the Disputes clause.

Prior versions of the language quoted above were identical except for subparagraph numbering.

3. FAR 42.705, Final indirect cost rates, as in effect from 3 March 1997 through 1998, provides:

> (a) Final indirect cost rates shall be established on the basis of --
>
> (1) Contracting Officer determination procedure (see 42.705-1) or
>
> (2) Auditor determination procedure (see 42.705-2).

Prior versions of FAR 42.705 were essentially the same.

4. FAR 42.705-1, Contracting officer determination procedure, as in effect from 24 April 1998 through 1998, provides in pertinent part:

> (b) *Procedures.* (1) In accordance with the Allowable Cost and Payment clause at 48 CFR 52.216-7 or 52.216-13, the contractor shall submit to the contracting officer . . . and to the cognizant auditor a final indirect cost rate proposal. . . .
>
> . . . .
>
> (3) The contracting officer . . . shall head the Government negotiating team, which includes the cognizant auditor and technical or functional personnel as required. . . .

(4) The Government negotiating team shall develop a negotiation position. Pursuant to 10 U.S.C. 2324(f) and 41 U.S.C. 256(f), the contracting officer shall—

(i) Not resolve any questioned costs until obtaining —

(A) Adequate documentation on the costs;
and

(B) The contract auditor's opinion on the allowability of the costs.

. . . .

(5) The cognizant contracting officer shall—

(i) Conduct negotiations;

(ii) Prepare a written indirect cost rate agreement conforming to the requirements of the contracts;

(iii) Prepare, sign, and place in the contractor general file (see 4.801(c)(3)) a negotiation memorandum covering—

(A) the disposition of significant matters in the advisory audit report;

(B) reconciliation of all costs questioned, with identification of items and amounts allowed or disallowed in the final settlement as well as the disposition of period costing or allocability issues;

(C) reasons why any recommendations of the auditor or other government advisors were not followed; and

(D) identification of cost or pricing data submitted during the negotiations and relied upon in reaching a settlement; and

(iv) Distribute resulting documents in accordance with 42.706.

Prior versions of FAR 42.705-1 were essentially the same.

5. The parties dispute the allowability of the rental costs exceeding ownership costs for FYs 1996-1998 that MPR paid to 320 King LLC. FAR 31.205-36, Rental Costs, provides, in pertinent part, as follows:

> (b) The following costs are allowable:
>
> (1) Rental costs under operating leases, to the extent that the rates are reasonable at the time of the lease decision, . . .
>
> . . . .
>
> (3) Charges in the nature of rent for property between any . . . organizations under common control, to the extent that they do not exceed the normal costs of ownership, . . .

6. MPR is an engineering service business. On 1 August 1991, MPR negotiated at arms-length a ten-year lease at reasonable, below market rental rates compared to those charged for similar facilities for MPR's current office space located at 320 King Street, Alexandria, VA with Gadsby Associates Limited Partnerships (Gadsby). Neither Gadsby nor JBG Associates, Inc., Gadsby's property manager, was related to MPR or under the common control of the MPR owners. MPR's 1991 lease included an option to purchase the building. (R4, tab 5; supp. R4, tabs 39, 50-52; app. supp. R4, tabs S-1, S-5)

7. In late 1993, MPR was considering exercising the option to purchase 320 King Street. Mr. Howard Niad of Rosenblum, Gloss, Niad & Dietz, P.C. (Rosenblum), MPR's outside auditor, represented MPR throughout the period of time before and after MPR's purchase of 320 King Street. On 10 November 1993, Mr. Niad contacted Mr. Phil Rogers, Senior Auditor, at the Defense Contract Audit Agency (DCAA) Branch Office, Alexandria, VA, to discuss generally the allowability of MPR's lease rental costs if it exercised the option. (Supp. R4, tab 84 at G0692; app. supp. R4, tab S-13) Mr. Niad's contemporaneous handwritten notes of the conversation with Mr. Rogers state:

> In practice, common control is not overruling, if rent is reasonable! (b)(3) doesn't override (b)(1) Gov't contract mix < 50% is better! Actually 30%
>
> Up to contracting officer[;] can override DCAA[;]
>
> But Rogers says the auditor is likely to start off by disallowing due to common control. It helps that:

(1) other tenants
(2) pre-existing lease
(3) 30% DCAA contracts
(4) 36% non officer S/H

(Notes attached to app. reply br.)[1]

8. MPR received advice from its real estate attorney on 14 January 1994 that MPR's purchase of the building at 320 King Street through a limited liability company having the same owners as MPR would be an "ownership shell" and that:

> . . . with the identity of ownership as between that of the LLC and MPR, I see real difficulties in getting DCAA to accept any lease between LLC and MPR as an arm's length transaction. It is a hope, and not more.

(Supp. R4, tab 41 at G0089)

9. Nevertheless, on 18 January 1994, the owners of MPR formed 320 King LLC. On 1 March 1994, MPR assigned to 320 King LLC its right to purchase the building, and Gadsby confirmed that the option to purchase had been exercised, and assigned to 320 King LLC its rights as landlord. MPR's rent under the original Gadsby lease and the pertinent lease provisions did not change. At and after the purchase, the owners, directors and officers (owners) of MPR were owners, directors and officers (owners) of 320 King LLC. Officers of MPR and 320 King LLC controlled the operations of 320 King Street for FY 1994 through FY 1998. (Supp. R4, tabs 42-49, 53; app. supp. R4, tabs S-2, S-3, S-5)

10. On 11 August 1994, MPR's Comptroller, Ms. Carolyn Stirrett informally contacted Mr. Joel Garcia, DCAA Branch Manager, Alexandria, VA by telephone concerning the allowability of MPR's rental expense for 320 King Street. According to a memorandum to file by Ms. Stirrett, which was not shown to have been sent to or received by the government, Mr. Garcia purportedly advised her that DCAA would not question under the common control limitation the allowability of MPR's rental rate and costs negotiated at a fair market rate that remained unchanged after the purchase. However, Mr. Garcia subsequently called Ms. Stirrett back and referred her to the DCAA Contract Audit Manual (DCAAM) Section 7-207 entitled "Leases Between Related

[1] Although this evidence was untimely, the government has responded on the merits and not moved to strike it. (Gov't letter to the Board dated 18 August 2005) Accordingly, we receive it.

Parties" (January 1994). That section provides that leases between parties under common control "are generally allowable to the extent that costs do not exceed the normal costs of ownership. . . " (R4, tab 6; supp. R4, tab 40 at G0086; app. supp. R4, tab S-4). Ms. Stirrett represented to Mr. Garcia that "I had already started reading over the section (after our earlier conversation) and that it appeared we met the necessary audit requirements" (R4, tab 6).

11. MPR did not disclose to DCAA for FY 1994 by required incurred cost submissions and related disclosure documents (including, *e.g.*, Schedule M, "Listing of Office Locations and Numbers of Employees at Each Location for Fiscal Year Ended . . . ;" Schedule T, "Schedule of Leased Assets Under Common Control for Fiscal Year Ended . . .") the common ownership of MPR and 320 King LLC. Nor did it reveal that MPR leased office space at 320 King Street from 320 King LLC (supp. R4, tab 66 at G0444-G0520). Rather, MPR's Schedule T for FY 1994 affirmatively stated there were no leased assets under common control to report (supp. R4, tab 66 at G0497).

12. On 29 March 1996, MPR forwarded to DCAA overhead cost summaries and related exhibits and schedules for FY 1995 but did not include Schedule T (supp. R4, tab 66 at G0521-G0560). On 11 June 1996, MPR's accountants sent Ms. Stirrett a draft office ownership schedule, disclosing that 320 King was commonly owned. The cover letter to Ms. Stirrett stated that "minimum, accurate disclosure" was best, and that the matter needed to be discussed with MPR's executive "before anything is submitted to DCAA." (Supp. R4, tab 53) We find appellant has not proved it forwarded this schedule to the government prior to April 2000, after the dispute arose. We find MPR did not notify the government by disclosure in required reports for FY 1995 (including incurred cost submissions) of the common ownership of MPR and 320 King LLC and their relationship with respect to MPR's rented space at 320 King Street.

13. Based on its assessment of low audit risk, DCAA limited the scope of its audit of MPR's FYs 1991-95 to indirect transaction testing of FY 1991 incurred costs, the only year with no voluntary MPR deletions of allowable overhead costs. DCAA performed no transaction testing of FYs 1994 and 1995 overhead costs that included MPR's rental costs for 320 King Street. DCAA informed MPR on 20 March 1997 that it would not question the allowability of MPR's indirect overhead cost rates for FYs 1991-95 based on its acceptance of MPR's argument that the overall impact of large voluntary deductions by MPR from its indirect overhead pools that lowered claimed overhead rates offset overhead costs. Thus, DCAA's audit and final audit report for FYs 1991-95 did not specifically focus on and audit MPR's rental rates and costs. (App. supp. R4, tab S-8; supp. R4, tabs 64, 65 at G0374-G0393, G0404-G0427, G0432-0439) We find with respect to MPR's FYs 1991-95 overhead costs that DCAA did not specifically consider and approve by final audit the allowability of MPR's rental rates and costs for its leased space at 320 King Street.

14. On 19 March 1997, the DCAA Branch Manager executed the indirect cost rate agreement for fiscal years 1991-1995 in accordance with FAR 42.705-2, Auditor determination procedure. On 20 March 1997, Ms. Stirrett executed the agreement, stating MPR accepted the final indirect cost rates. (R4, tab 65 at G0416-8)

15. MPR's incurred cost submissions and related reports submitted to DCAA for FY 1996 did not notify or otherwise disclose to DCAA that the rental costs MPR allocated to its overhead cost pools and G&A pools for these years exceeded its normal costs of ownership and fell within the FAR common control limitation based on the common control of 320 King Street by the same owners of MPR and 320 King LLC. MPR's Schedule T, "Schedule of Leased Assets Under Common Control For Fiscal Year Ended 12/31/96," stated "Nothing to report" (supp. R4, tab 85 at G0773). The index to the MPR incurred cost submission for FY 1996 labeled Schedule T as "N/A" or not applicable (*id*. at G0708). MPR did not disclose its relationship to 320 King LLC in its Schedule M, "Listing of Office Locations and Numbers of Employees at each Location for Fiscal Year Ended 12/31/96," included in its FY 1996 incurred cost submission (*id.* at G0766).

16. The audit DCAA conducted for FY 1996 of MPR's final overhead rates began with an audit of MPR's incurred cost submissions and included a review of FY 1996 rental costs in the transaction testing plan. The auditors noted that the Internal Control Questionnaire (ICQ) revealed a relationship between MPR (the lessee) and 320 King LLC (the lessor) and that the rent cost was a major expense in the claimed overhead pool. For the first time, DCAA's draft report of 29 September 1999 questioned as unallowable MPR's rental expense that exceeded the normal costs of ownership of MPR's leased space at 320 King Street. (R4, tab 8; supp. R4, tabs 83 at G0629-G0688, 84 at G0701-G0705).

17. MPR's letter of 19 April 2000 responded to the draft audit report. The letter asserted the FY 1996 rental expense was allowable because the monthly rental rate resulted from an arms-length negotiation of the lease agreement, the rental rate was consistent with market rental rates at the time MPR first entered into the lease, and the rental rate did not change after 320 King LLC purchased 320 King Street. MPR enclosed a memorandum from counsel arguing *inter alia* that the government could not retroactively disallow the costs. (R4, tab 9)

18. On 27 December 2000, DCAA issued its final "Report on the Audit of MPR's Direct and Indirect Costs and Rates Claimed for FY 1996." DCAA questioned MPR's rental costs of $218,771 that exceeded the normal costs of ownership of 320 King Street. The report included a DCAA Form 1 disapproving related-party lease costs totaling $37,992, consisting of G&A and overhead allocated to contracts 2106 and 0049. DCAA

also questioned excessive executive compensation and bid and proposal (B&P) costs. (R4, tab 10)

19. DCAA's 21 June 2002 final audit report of MPR's incurred costs for FYs 1997-1998 questioned the allowability of $229,818 and $74,578, respectively, of MPR's FYs 1997 and 1998 rental costs that exceeded the normal cost of ownership of 320 King Street. The report included a DCAA Form 1 dated 17 June 2002 disapproving related-party lease costs totaling $38,824 for FY 1997 and $11,535 for FY 1998, consisting of G&A and overhead allocated to contracts including the four captioned contracts. (R4, tab 12) DCAA ultimately questioned four categories of costs in MPR's proposal of FYs 1996-98 final overhead rates, including MPR's rental costs above the normal costs of ownership of 320 King Street, excessive executive compensation, B&P costs and patent amortization costs for FYs 1997-98 (supp. R4, tab 86 at G0798).

20. The Form 1s issued to MPR provide that if the contractor disagrees with DCAA, the contractor may request the contracting officer "to consider whether the unreimbursed costs should be paid and to discuss his or her findings with the contractor" (R4, tab 10 at 23, tab 12 at 27). After DCAA issued the Form 1 for FY 1996, MPR requested a meeting with the DCMA Administrative Contracting Officer (ACO) to resolve outstanding issues. Although a meeting was held in April 2001, the parties did not resolve the rental cost issue then or prior to the issuance of the Form 1 for FYs 1997 and 1998. (R4, tabs 13-20)

21. On 19 December 2002, the parties met at MPR's offices to discuss the 12 June 2002 Form 1, that questioned as allowable four categories of costs included in MPR's 1997-1998 overhead submissions. The participants included Mr. Alan D. Fredericks, ACO; Ms. Sylvia Moore and Ms. Sherry Konzman, both representing DCAA; Ms. Carolyn Stirrett, MPR's Chief Financial Officer; Mr. Niad of Rosenbaum; and two of MPR's outside attorneys retained in connection with the 19 April 2000 letter. The parties agreed to meet one month later "to try to reach a settlement of all the outstanding issues" (app. supp. R4, tabs S-13, S-14).

22. ACO Fredericks along with DCAA representatives and MPR representatives met again on 15 January 2003 as agreed. They reached an oral understanding with respect to the four outstanding cost items DCAA questioned in the 21 June 2002 audit report. ACO Fredericks agreed to the allowability of MPR's rental rates and costs for FYs 1996-98 for 320 King Street. For its part, MPR accepted the government's disallowance of patent costs, a portion of MPR's executive compensation and DCAA's allocation of B&P costs. (App. supp. R4, tabs S-13, S-14) Based on MPR counsel's (at the time) unrebutted and credible affidavit, dated 22 June 2005, the discussion relating to the parameters of the meeting and rental costs was as follows (we omit the details relating to the other cost issues):

The ACO stated at the outset of the meeting that he regarded the entire discussion to be in the nature of a mediation aimed at resolving all of the outstanding issues. Each of the questioned categories of cost were then discussed separately with the following results:

> . . . .
>
> d. Rental Costs – At the prior meeting on December 19, 2002, the ACO, Mr. Fredericks, had taken as an action item the task of reviewing MPR's April 2000 memorandum regarding the recovery of the full rental costs. At the outset of the discussion of this issue, he stated that he had consulted counsel prior to the meeting and was comfortable with the position being taken by the DCAA. He also stated, however, that he understood that MPR had negotiated the lease for the building in an arms-length transaction with its prior owner (before there was any possibility of common control). He further stated that he recognized that the rent thus negotiated remained unchanged and below market. He did not specifically address the estoppel issue or the argument MPR had made in its April 2000 memorandum based upon the government's course of conduct in approving the allowability of the rental cost for the years prior to the September 1999 draft audit report. At the conclusion of this discussion he stated that it was his determination that the full amount of the rental costs for FYs 1996-1998 were allowable.

In order to then bring closure to all of the issues, MPR then agreed to accept the disallowance of the executive compensation costs discussed at the beginning of the meeting.

8. At that point, agreement had been reached by Ms. Stirrett, representing MPR, and by the ACO, Mr. Fredericks. No questions or objections were raised by any of the other people at the meeting, and there was no further substantive discussion of the issues. At no time did Mr. Fredericks state that his agreement was subject to further review or approval, or anything other than final. Rather, the discussion shifted to

> the administrative steps required to reduce the agreement to writing. Thus, the parties discussed the fact that before the agreement could be captured in a new set of final rates for the three years at issue, the FYs 1996-98 overhead rates would have to [be] recomputed to reflect the agreements reached during the meeting. DCAA was tasked by the ACO to make those calculations by:
>
> . . . .
>
> d. Including the full rental costs for FYs 1996-1998.
>
> The ACO further stated that he intended to prepare a Post-Negotiation Memorandum reflecting the agreements reached, in order to explain the bases used to compute the final rates, . . .

(App. supp. R4, tab S-14) Appellant also provided a similar affidavit from Mr. Niad (*id.*, tab S-13). Neither appellant nor the government provided an affidavit from the principals at the meeting, Ms. Stirrett and Mr. Fredericks, with respect to the matters discussed at the 15 January 2003 meeting.

23. The parties discussed the allowability of the MPR rental rates further by email during 2003, following their 15 January 2003 meeting. On 26 February 2003, Ms. Stirrett wrote Mr. Fredericks that:

> [W]e are now almost a month behind our commitment (agreement from our last meeting) and I am concerned that somehow we'll have to revisit this entire audit issue unless we close this loop soon. . . . We are anxious to get the revised official audit report on record.

(R4, tabs 21-22)

24. Mr. Fredericks emailed Ms. Stirrett on 30 April 2003 that:

> . . . the following is provided for your info, as previously promised. the [sic] cost impact of the [sic] our discussed cost isses' [sic] settlement. DCAA is not happy about yielding on the rent issue, as it is counter to their standing policy and previous practice. More discussions continue.

The following information has been provided to me by DCAA:
The following is the difference between CPFF costs claimed and questioned, both with and w/o the rent exception taken by DCAA:

YEAR	KTR CLAIMED	DCAA-w/o Rent Exception	Questioned Costs	
96	$2,806	$2,712	$94	Total of 3yrs
97	$2,688	$2,612	$76	is $239K
98	$2,261	$2,192	$69	

YEAR	DCAA w/ rent Included	Questioned Costs	
96	$2,749	$57	Total of 3 years
97	$2,654	$34	is $148K
98	$2,204	$57	

Net difference between the two positions is a reduction of $91K in questioned costs, which reverts to Contractor.

(R4, tab 24)

25. Mr. Fredericks emailed Ms. Stirrett on 1 May 2003:

The following information was provided by DCAA:

	MPR PROPOSED		DCAA w/ Rent Out		DCAA w/ Rent Accepted	
YEAR	OH	G&A	OH	G&A	OH	G&A
1996	77.59%	8.07%	56.55%	15.03%	59.09%	15.2%
1997	70.31	8.98	50.96	16.45	53.74	16.65
1998	92.63	9.10	59.17	23.69	60.18	23.96

Based upon agreement to settle issues, with DCAA taking exception to the rent charged, and their position accepting rent charges. Hope this helps you understand abit [sic] better. Look at this along with email sent yesterday.

(R4, tab 25) On 2 May 2003 Ms. Stirrett emailed: "Should we receive a revised Form 1 with rent accepted?" (R4, tab 26) Mr. Fredericks responded by email on 2 May 2003

that "I interpret your question to mean that following review, your management is agreeable to the revised cost situation, with Government acceptance of the rent costs?" (R4, tab 26) Ms. Stirrett responded a month later by email of 2 June 2003 that "[w]e accept the changes noted with acceptance of rent costs. Please advise DCAA to issue a revised audit report for our signature" (R4, tab 27).

26. On 28 November 2003, Mr. Fredericks emailed Ms. Stirrett, in pertinent part, as follows:

> Much time has passed and we have to address the settlement of the above subject (Question Costs/Indirect Rate Settlement, FY96-98) final indirect cost rates, for MPR fiscal years' 1996, 1997, and 1998.
>
> . . . .
>
> I had talked about numbers, slightly higher than the DCAA-Recommended, as a settlement position, but my legal informed me that I was exceeding my authority to formulate and push for such a settlement.
>
> I would welcome the opportunity to sit down with you and your management to discuss your possible corporate acceptance of the DCAA-recommended numbers.

(R4, tab 28) The DCAA-recommended numbers excluded rent.

27. Ms. Stirrett's email of 2 December 2003 reiterated that MPR understood that the rent was being considered as an allowable expense. Mr. Fredericks responded by email on 3 December 2003 that:

> You are correct in that we did discuss acceptance of the rent as an allowable expense, in order to achieve a settlement of all issues, in order to settle the final rates. This was in keeping with prevailing thought that everyone has to think outside the box.
>
> However, I was counseled by my inhouse [sic] legal that the DCAA-exception to the rent expense is based upon a statuatory [sic] citation, FAR 31.205-36(b)(3) wherein related-party lease expenses are allowable only to the extent they do not exceed the constructive cost of ownership. As

> explained to me, my ACO-warrant does not provide me the legal authority to rewrite, or ignore the statutes, only to follow them and uphold them.

(R4, tab 32) Ms. Stirrett on 3 December 2003 responded that she thought the ACO had made a binding decision agreed to by MPR (R4, tab 35). She stated in an email on 22 January 2004 that MPR did not agree with the government's position on the rental rate issue and would "contest the way the matter had been handled" (R4, tab 36).

28. On 26 April 2004, ACO Fredericks issued a unilateral final indirect rate determination that excluded MPR's rental costs that exceeded the normal ownership cost of 320 King Street (R4, tab 37).

29. On 29 April 2004, ACO Fredericks issued his contracting officer's final decision for FY 1996, FY 1997 and FY 1998 that disallowed $523,167 of MPR rental costs under FAR 31.205-36(b)(3), of which $85,981 was allocated to the captioned contracts. ACO Fredericks demanded that MPR reimburse the government for provisional payments of $85,981 for unallowable MPR rental costs in excess of the normal costs of ownership for these fiscal years. (R4, tab 38) MPR filed a timely appeal.

DECISION

MPR contends that the common ownership control limitation of FAR 31.205-36(b)(3) does not apply to its rental rates and costs for 320 King Street, which it agrees is owned and controlled by the same owners of MPR and 320 King LLC, because it entered into the lease for a reasonable rate prior to the purchase and the rental rate has not changed (compl. at 1). We need not decide this issue because, in our opinion, the parties reached a binding agreement to settle the matter at the 15 January 2003 meeting.

The government contends that the parties did not reach a settlement agreement on the rental cost issues. It also maintains that the ACO was not authorized to violate FAR 31.205-36(b) by agreeing to pay the rental costs in excess of normal ownership costs. (Gov't br. at 37; gov't reply br. at 21, 24)

The issues before us concern whether the parties reached a binding, oral agreement that is enforceable. When the government goes into the market place, it may reach oral agreements settling parties' rights, as any other contracting entity may do. In *Texas Instruments, Inc. v. United States*, 922 F.2d 810 (Fed. Cir. 1993), the Court of Appeals for the Federal Circuit stated that negotiation of price pursuant to a contract term did not constitute a modification of the contract. There, the oral agreement to a price

term in accordance with a contract requirement did not require a contract modification for the agreement to be enforceable. The Court expressed that it has long been held that:

> '[i]t makes no difference that the contract was not formally signed or the bond formally approved' for the Government to be bound by the terms of a contract. *United States v. Purcell Envelope Co.*, 249 U.S. 313, 319, 39 S. Ct. 300, 301-302, 63 L.Ed. 620 (1918). '[F]ormal execution, as we have seen, [is] not essential to the consummation of contract. *Id.*' [Brackets in original]

Texas Instruments, Inc. v. United States, supra, 922 F.2d at 814. Thus, the government may enter into an enforceable oral agreement with respect to resolution of rights under a contract without formal modification of the contract itself.

The issue before us, like that in *Texas Instruments, supra*, does not concern bilateral modifications of the four captioned contracts. The issue concerns fulfillment of regulatory requirements (FAR 42.7) incorporated into the contracts with respect to the determination of the parties' rights under the contract through negotiations.

This Board has stated with respect to disputes before the Board involving parties' settlement agreements that form does not triumph over substance. A written settlement agreement entered into by the government is not required to bind the government. The Board in *Kurz & Root Company*, ASBCA No. 17146, 74-1 BCA ¶ 10,543 at 49,942 expressed:

> The Courts and Boards of Contract Appeals have repeatedly held that a binding oral contract or agreement is formed when the government accepts an offer notwithstanding the fact that both parties intend to sign a formal contract or agreement at a later time.

See also Penn-Ohio Steel Corp v. United States, 173 Ct. Cl. 1064, 1086, 354 F.2d 254, 266-67 (1965) and cases cited therein; *Escote Manufacturing Company v. United States*, 144 Ct. Cl. 452, 458-59, 169 F. Supp. 483, 488 (1959).

In their 15 January 2003 meeting, the parties reached an oral agreement on all matters discussed. MPR agreed to relinquish its position on the allowability of excessive executive compensation, patent costs and B&P costs. The ACO agreed to the allowability of MPR's FY's 1996-1998 rental costs for 320 King Street. At the close of the parties' 15 January 2003 meeting, the parties had completed all steps necessary to reach an oral agreement binding both parties. They had exchanged consideration and had

a meeting of the minds on the agreement's major terms with respect to the outstanding cost issues before them. They intended to be bound by their agreement. All that remained to be done were the simple mechanical formalities of DCAA calculations of the indirect cost rates with the MPR full rent included, the ACO's completion of a post-negotiation memorandum and the creation of an indirect cost rate agreement. The requirement for further ACO action to accomplish these formalities did not contemplate further negotiations that would negate the binding nature of the parties' oral agreement. Thus, the parties orally reached a settlement of rights under the contracts, as distinguished from a subsequent modification of the contracts themselves that may have required written contract modifications to complete the agreement. *Texas Instruments, supra,* 922 F.2d at 814.

While there is a plausible argument that under the regulations the post-meeting emails between the parties, particularly the ACO's email of 2 May 2003 and Ms. Stirrett's response of 2 June 2003, constitute the writing required by such cases as *Mil-Spec Contractors v. United States*, 835 F.2d 865, 868 (Fed. Cir. 1987) (contracting officer understood SF 30 was required), we do not have to decide that issue in the appeal before us. Since the parties orally settled rights within the context of their contracts, and did not modify the contracts themselves, their agreement did not conflict with the requirement for a signed writing to modify an integrated bilateral contract. Moreover, in our opinion, the ACO could not repudiate the parties' agreement on all major issues by refusing to put their agreement in writing or to complete the simple mechanical steps required by the regulation of completing a post-negotiation memorandum and an indirect cost rate agreement with the DCAA calculated indirect cost rates and costs that included MPR's total rent for FY's 1996-1998. It is also noteworthy that even at the time of close of the record in the captioned appeal, there is no ACO disagreement with the oral agreement reached at the 15 January 2003 meeting that settled the parties' rights under the contracts. Appellant's affidavits describing the parties' oral agreement are unrebutted.

The government maintains, however, that the ACO lacked the authority to enter into the oral agreement providing for the allowability of MPR's rental rates and costs above the normal costs of ownership contrary to the common control limitation of FAR 31.205-36(b)(3) (gov't br. at 37-38; gov't reply br. at 24). We disagree.

This is not a case where the ACO violated a plain requirement of a statute or regulation as was the case in *Johnson Management Group CFC, Inc. v. Martinez,* 308 F.3d 1245 (Fed. Cir. 2002), cited by the government. There is no plain illegality here. The ACO was authorized to exercise his judgment in interpreting the regulations to resolve the rent issue under the cost principles. The ACO's interpretation of the cost principles in light of the change in appellant's status during the course of the lease was not clearly unreasonable. Under the totality of these circumstances, therefore, the ACO

acted within his authority in interpreting the regulations to resolve the doubt concerning the reasonableness of the MPR rental rates and costs and entering into the oral agreement with MPR that settled all cost issues.

The appeal is sustained.

Dated: 27 October 2005

EDWARD G. KETCHEN
Administrative Judge
Armed Services Board
of Contract Appeals

I concur

EUNICE W. THOMAS
Administrative Judge
Vice Chairman
Armed Services Board
of Contract Appeals

I certify that the foregoing is a true copy of the Opinion and Decision of the Armed Services Board of Contract Appeals in ASBCA No. 54689, Appeal of MPR Associates, Inc., rendered in conformance with the Board's Charter.

Dated:

CATHERINE A. STANTON
Recorder, Armed Services
Board of Contract Appeals