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Heritage Reporting Corporation

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1. GAO will examine GSA's allocation to executive agencies of liability incurred in settlement of contract claim to determine legal errors in the allocation. 2. Securities and Exchange Commission was exempt from mandatory use provision in FSS contract based on GSA's actions in connection with a proposed contract modification. 3. Federal Maritime Commission's existing contract for court reporting services exempted the Commission from mandatory use of FSS contract for period that existing contract was in effect. 4. GAO will entertain claims regarding allocation of settlement liability in this matter for 30 days from the date of this decision. In order to render a final determination of liability, no claims will be considered after that date.

DECISION

The General Services Administration (GSA) entered into a compromise settlement of claims brought by Heritage Reporting Corporation before the General Services Administration Board of Contract Appeals (GSBCA). That agreement allocated liability among various agencies. The Department of Treasury has asked for our analysis of the amount of reimbursements owed by various agencies to the Judgment Fund, 31 U.S.C. Sec. 1304, for the GSBCA judgment of $7,254,525.60 paid to Heritage. In our view GSA's allocation of liability among the various agencies is entitled to deference unless that allocation is demonstrably erroneous. In this regard, we believe that the Securities and Exchange Commission and the Federal Maritime Commission have presented evidence of demonstrable legal error on the part of GSA. Accordingly, the allocations made by GSA to the Securities and Exchange Commission and the Federal Maritime Commission should be adjusted.

Background

On July 22, 1988, the General Services Administration (GSA) awarded a mandatory federal supply schedule (FSS) contract for court reporting services to Heritage.[1] The contract was for one year, from August 1, 1988 through July 31, 1989, with two one-year options. Each federal executive agency was required to use Heritage for its court reporting needs unless the agency had a contract in place prior to the award of the schedule contract or unless the agency obtained a waiver from GSA.[2] The catalog/price list published by GSA for this contract was dated October 31, 1988, three months after the contract went into effect, and reached the agencies sometime thereafter.

GSA did not exercise its option to extend Heritage's contract after the initial base year term expired. According to GSA, it canceled the entire MAS for court

reporting services because of numerous agency complaints about services under the schedules. Heritage then filed a claim with GSA arguing that the government had breached its contract by procuring court reporting services off schedule. The claim was denied and Heritage appealed the decision to the GSBCA.

GSA and Heritage pursued discovery and dispositive motions over the course of two years. On August 28, 1992, prior to a full hearing on the case, GSA negotiated a settlement with Heritage of $7,254,525.60 and allocated settlement liability among the user agencies. Although the Board entered a judgment in that amount, it specifically declined to adopt GSA's allocation of liability.[3] The Board stated that those agencies had not been a party to the Board action and that agency contribution for reimbursement of the fund was an intragovernmental matter and therefore not justiciable by the Board.

GAO has certified the payment of the judgment to Heritage from the Judgment Fund. The Contract Disputes Act, 41 U.S.C. Sec. 612 (c), requires reimbursement of the fund by the agency whose appropriations were used for the contract. In this case, both GSA and the user agencies share liability for the judgment.[4] Under the federal supply schedule system, GSA enters into contracts with suppliers to fulfill the government's requirements. Agencies then place purchase orders directly with the supplier in accordance with the terms of the FSS contract. If the FSS contract is a mandatory source of supply, as it was here, agencies must, with a few limited exceptions, order their requirements only from the FSS. Consequently, whenever an agency improperly uses another source of supply, the FSS contract is breached. GSA allocated liability for breach of the Heritage contract based on a formula that incorporates the number of pages ordered off schedule. That formula first requires multiplying the number of pages the agency ordered off schedule by 70% (Heritage's market share). For originals, this number is multiplied by $4.393 (Heritage's price per page for originals) and 30% (Heritage's profit rate). For copies, the number is multiplied by $1.25 (Heritage's price per page for copies) and 1.167 (average number of copies ordered). GSA has already agreed to pay a portion of the judgment due to its delay in publishing and distributing the catalog for this contract.[5] While there may be alternative methods of allocating liability in this case, we think the method GSA used is objective and reasonable, and an allocation by GSA is entitled to deference unless it is demonstrably legally erroneous. 31 U.S.C. Sec. 1304, 3526, 3702. The Justice Department and the Securities and Exchange Commission (SEC), two of the largest users of court reporting services, object to GSA's allocation, as does the Federal Maritime Commission. There is no indication that the approximately 70 other executive branch entities to which GSA has allocated a share of the judgment are aware of the settlement and the charges pending against their accounts.

SECURITIES AND EXCHANGE COMMISSION

The SEC argues that its own pre-existing and wholly separate contract with Heritage exempted it from mandatory use of the FSS contract and thus from any damages resulting from breach of that contract. The SEC requires reporting services for its investigation of possible violations of securities laws. On October 1, 1986, the agency awarded a 1-year contract with two 1-year options to Heritage Corporation for court reporting services.[6] The original term ran from October 1, 1986 to September 30, 1987 and notice of renewal was required at least 30 days prior to contract expiration. The SEC exercised both options, the second option on August 23, 1988.

SEC was aware, prior to exercising the final option, that GSA was contemplating a mandatory contract for all executive agencies. There were several conversations and a meeting between the two agencies regarding the proposed contracts. SEC's contract for the services it required was generally less expensive than the schedule contract. The record shows that GSA sent a contract modification to Heritage that specifically exempted SEC from the GSA contract. Heritage signed the modification on September 1, returned it to GSA, and copied the SEC. GSA inexplicably did not sign the modification. Apparently, in February or March of 1989, after attempting to obtain a copy of the modification from GSA, Heritage was told that GSA no longer planned to proceed with the modification. SEC was not given this information.

The record does not indicate why GSA failed to sign the modification, or why GSA would have told Heritage that it no longer planned to proceed with the modification. In our view, its actions with respect to that modification led the SEC to reasonably believe that the use of its own contract was proper and not in violation of the FSS contract mandatory use requirement.

Section 8.404-1 of the Federal Acquisition Regulation (FAR) provides that an agency that is a mandatory user under a schedule may purchase items from nonschedule sources if they are less expensive than schedule items. In this case, the services under SEC's own contract with Heritage were less expensive than under the FSS contract. However, the services under the SEC contract were somewhat different than those under the Heritage schedule contract. FAR Sec. 8.404-3 provides that when a mandatory user under a schedule determines that items available from the schedule will not meet its specific needs, but similar items from another source will, it shall submit a request for waiver to GSA. By preparing and sending to Heritage the proposed modification to the FSS contract specifically exempting the SEC, GSA effectively waived SEC's obligation to purchase necessary reporting services under that contract. SEC, reasonably believing the modification to be effective, had no reason to seek a further waiver under section 8.404-3. Under these circumstances, we believe that SEC properly purchased reporting services for a lower price under its own contract with Heritage.

Accordingly, we believe SEC should not be required to pay the requested reimbursement of $910,230.59 to the Judgment Fund.

DEPARTMENT OF JUSTICE

The Department of Justice is the major user of court reporting services. The services are used in connection with administrative, quasi-judicial and judicial proceedings. GSA assigned $2,681,287.95 of the judgment to Justice using a formula based on the number of pages the agency ordered off the GSA schedule. Justice objects to the allocation on several grounds.

First, Justice contends that GSA erroneously settled the case with Heritage on the basis of lost profits. Justice, citing GSBCA and federal case law, argues that anticipated profits is not the proper measure of damages in government contracts cases absent bad faith. GSA, relying on the same cases, argues that the proper measure of damage for a breach of a requirements contract is compensatory damages and anticipated profits. Justice's objection goes to the amount of the government's settlement with Heritage, not to the amount of the settlement allocated to Justice. The amount of the settlement was established by agreement between Heritage and GSA and is binding on the parties. The only

question before us is GSA's allocation of liability.

Second, Justice argues that the Heritage contract did not cover judicial proceedings (primarily depositions) and grand jury proceedings. GSA advanced this argument on Justice's behalf as a respondent before the Board. The Board denied GSA's motion for partial summary relief, stating:

In the instant case, we find that there are legitimate questions as to what the contract means. The interpretation respondent advances regarding depositions is strained given that respondent is relying solely upon contract language that is less than decisive. Further, the contract is silent as to grand jury proceedings, but contains language which could be construed to include such proceedings, i.e., "courthouse and/or legal hearings." Thus, the contract is ambiguous on whether grand jury proceedings are within its scope.

GSBCA No. 10396, Oct. 19, 1990.

The Board went on to say that factual issues exist regarding grand jury reporting and that further evidence was required. The record before us does not establish that GSA committed legal error in agreeing to a settlement that included the original recordings of these proceedings in calculating the amount of damages.

Finally, Justice argues that GSA mismanaged this contract and that Justice should not be forced to bear the financial burden caused by GSA's unreasonable actions. Justice notes that GSA never consulted Justice regarding the formation of the schedule contract in which Justice would be the largest executive branch user.[7] Justice argues that the agencies' interests were not represented in the GSBCA hearing and that in fact, GSA's interests were adverse to the interests of the user agencies. GSA responds that 41 U.S.C Sec. 612(c) provides that the agency whose appropriations were used for the contract is responsible for reimbursement. GSA notes further that the user agencies, not GSA, breached the contract.

Whether or not GSA managed the procurement well, agencies whose appropriatons were used for the contract must reimburse the Judgment Fund under 41 U.S.C. Sec. 612(c). Justice does not contend that GSA was unauthorized to enter into the contract and settle the claim arising from its breach. Justice's argument that GSA should have done a better job exercising its authority does not establish that GSA's method of allocations, based upon the extent of each agency's breach of its obligations, is unreasonable, or overcome the reimbursement requirement in 41 U.S.C. Sec. 612(c).

FEDERAL MARITIME COMMISSION

GSA assigned $10,438.38 of the judgment to the Federal Maritime Commission. The Commission disputes the allocation on two points. According to the Commission, it ordered 3,625 pages off schedule. The Commission states that it had a contract for court reporting services in effect for the calendar year commencing January 1988 through December 31, 1988. Consequently, it believes its liability should be reduced by the 633 pages that were ordered during the 5-month period its contract was in place. The Commission also believes its liability to be between $1,631-$2,175 based on GSA's formula for determining settlement amounts.

Section I.10 of GSA's contract provided:

Any agency designated above as a mandatory user shall be exempt from the mandatory use provision if prior to the issuance of the GSA contract, the agency may have entered into a prior contract on its own with an ordering period conflicting with the GSA contract ordering period. Upon expiration of the agency's previous commitment, GSA mandatory use provisions shall prevail without exception.[8]

We think the Commission's preexisting contract fits squarely within this exception and consequently the agency was exempt from the mandatory use requirement. However, since GSA has already assumed liability for the first 3 months of the contract period, only the liability for those pages ordered during the remaining 2 months should be deleted from the Commission's share. We do not know for certain how many of the 633 pages were ordered in the first three months. Assuming the pages ordered were divided evenly over the period, a 2month share is 253 pages.[9]

The record reflects that GSA determined the Commission's liability based on an estimated 4,816 pages. Subtracting the 253 pages yields 4,563 pages. This total is 938 pages more than the 3,625 Maritime states it ordered off schedule. We have no reason to question GSA's page estimate absent legal error and consequently that figure should be used in calculating the Commission's liability.

CONCLUSION

Accordingly, GSA should adjust the allocation made to the SEC, the allocation to the Federal Maritime Commission and the other allocations, as appropriate and necessary.

We have not reviewed the allocations of all agencies that were assessed a portion of the settlement liability. So that the agencies have sufficient time to submit claims, we suspend final allocation of this amount until 30 days from the date of this decision. Once those are resolved, GSA may consider all page estimates as final, and should recalculate the allocations as necessary and appropriate. Because the settlement amount is fixed, the elimination of pages from an agency estimate, as with SEC and the Federal Maritime Commission, will result mathematically, in a higher price per page, and a different amount of liability than currently assessed by GSA.[10] In addition, GSA should re-assess the amount it owes the Fund as a result of its delays in printing and distributing the contract catalog. (See note 5.) GSA allocated to itself three months, or one-quarter, of the total liability, which is $1,813,631.40 rather than the $1,580.036 GSA computed.

1. Under a GSA schedule, agencies place orders directly with GSA-approved contractors. 48 C.F.R. Sec. 38.101. The award to Heritage was a multiple award schedule (MAS) contract. A MAS consists of contracts with more than one supplier for services at varying prices for delivery within the same geographic area. In this case, Heritage was listed as the sole contractor in 39 of the 48 contiguous states; in the District of Columbia and the remaining contiguous states, Heritage was one of several contractors listed.

2. The U.S. Postal Service, the Department of Defense, the National Labor Relations Board and the Equal Employment Opportunity Commission were specifically exempted.

3. The Board denied the parties' first request for entry of judgment because the parties stipulated that the settlement offer would not be binding unless the Board adopted the proposed allocation. The parties dropped the stipulation in their second request and the Board entered judgment.

4. See S. Rep. No. 95-1118, 95th Cong., 2d Sess. 93. ("In order to promote settlements and to assure the total economic cost of procurement is charged to those programs, all judgments awarded on contract claims are to be paid from the defendant agency's appropriations. If the agency does not have the funds to make the payment the agency is to request additional appropriations from Congress . . . Requiring the agencies to shoulder the responsibility for interest and payment of judgments brings to bear on them the only real incentives available to induce more management involvement in contract administration and dispute resolution").

5. Many MAS contracts require the vendor to print and distribute a catalog of the goods and services available under the particular contract. In this instance, GSA deleted this requirement. Agencies were therefore not given notice of the award until they received the GSA catalog/price list dated October 31, approximately three months later. Because of this delay, GSA allocated to itself three months worth of damage and arrived at the $1,580,036 figure. However, we note that a 3 month (1/4 share) of $7,254,525.60 is $1,813,631.40.

6. The initial contract was actually awarded to Acme. Heritage was a successor in interest.

7. GSA convened a user panel on transcripts and stenographic services consisting of 6 agencies: Veterans Administration, Social Security Administration, Housing & Urban Development, Internal Revenue Service, Federal Mine Safety & Health Review Commission and Department of Transportation.

8. The FSS schedule issued by GSA notifying the agencies of the terms and conditions of the contract contained an identical clause.

9. If this estimate is substantially inaccurate, GSA should make adjustments upon further submission by the parties.

10. GSA will have to recalculate the amount of liability it redistributed from Justice to other agencies when Justice informed GSA that by law, grand jury proceedings are secret and as a result Heritage would have made no copies. GSA redistributed $1.1 million; however, that amount was based on the original price per page.