We can't help reporting on Raytheon's litigation because the decisions in its cases are important. Plus, you know, Raytheon *actually litigates*—unlike the other major defense contractors who report settlement after settlement in the contract dispute fora. As we've noted before, we suspect one reason that Raytheon keeps litigating is because it seems to win more than its fair share of disputes.

And here we are again, reporting on **another decision** at the ASBCA. This decision addressed ASBCA Nos. 57576, 57579, and 58290. As Judge Delman noted in his decision, he had previously dismissed three other appeals that covered many of the same issues because the claims had been issued "untimely" by the government—i.e., the Statute of Limitations associated with the Contract Disputes Act had expired. Thus, Raytheon had already started with a victory for its Fiscal Years 2002, 2003, and 2004.

The three appeals at issue concern alleged violations of both CAS and FAR. In one dispute (No. 57576) "the government contends that Raytheon failed to identify and exclude from its cost submissions the costs of bonus and incentive compensation (BAIC) for those persons engaged in activities that generate unallowable costs under the following cost principles: FAR 31.205-1, -22, -27, and -47, and that are 'expressly unallowable' under these principles." In other words, the government asserted that the bonus and incentive compensation (BAIC) was a directly associated unallowable cost and, accordingly, it should have been treated as being expressly unallowable.

In the other two disputes (Nos. 57579 and 58290), "the government contends that Raytheon failed to identify and exclude from its cost submissions the costs of certain stock awards to employees under its long-term performance plan (LTPP) that are 'expressly unallowable' under FAR 31.205-6(i)."

Obviously, the definition of “expressly unallowable” played a key role in Judge Delman’s decision. We’ve addressed the controversy over that definition **before** . The decision would also turn on the requirements of Cost Accounting Standard (CAS) 405. In fact, the Judge took about 11 pages to establish the pertinent statutes, CAS rules, and FAR requirements before turning to the Statements of Facts for each appeal.

Getting back to No. 57576, Judge Delman found that Raytheon had briefed DCAA on its various incentive compensation plans as early as 2000. In September, 2002, a DCAA audit report on Raytheon’s incentive compensation concluded that the audit agency “took no exception” to Raytheon’s incentive compensation. A year later, another DCAA audit report concluded that Raytheon’s FY 2002 incentive compensation costs were allowable costs pursuant to the requirements of FAR 31.205-6(f). A year after that, another DCAA audits report reached the same conclusion. In 2006, another DCAA audit report reached the same conclusion. There were other DCAA audit reports discussed by Judge Delman; they also reached similar conclusions. Perhaps our readers are sensing a pattern here.

Regardless of the foregoing litany of audits and audit conclusions, in September, 2007, a DCAA audit alleged a Raytheon noncompliance with CAS 405, stemming from its failure to “withdraw from its incurred cost submissions a proportionate share of its costs of bonuses, restricted stock, and other compensation costs paid to employees engaged in ‘expressly unallowable activities’ as defined by various FAR cost principles. The alleged CAS noncompliance pertained to Raytheon’s Fiscal Years 2002 through 2005. The Corporate Administrative Contracting Officer (CACO) agreed with DCAA, and told Raytheon –

Raytheon Company, Corporate Home Office, withdraws labor and a portion of fringe expenses for employees engaged in expressly unallowable advertising, lobbying, organization, and legal activities. However, they do not withdraw the applicable portion of bonus, restricted stock, and other incentive compensation in connection with these expressly unallowable activities.

Subsequently, DCAA and DCMA added Raytheon’s FY 2006 claimed costs to the alleged CAS noncompliance. Meanwhile, Raytheon was busy calculating GDM cost impacts related to the alleged noncompliance. There was a “fringe delta” cost impact, which was rejected by the government. Then Raytheon prepared a “discrete” impact calculation. Importantly, although the government’s alleged CAS noncompliance covered only four (4) areas of unallowable activity, Raytheon’s cost impact included a fifth area (“Contributions”). Raytheon argued that inclusion of the fifth area was inadvertent. However, the government used Raytheon’s

calculation (which included all five areas) to arrive at a quantum of $20,012,578. (That amount included penalties and interest as well.)

With respect to No. 57576, Judge Delman dismissed the part of the government's claim relating to Raytheon's inadvertent inclusion of the Charitable Contributions cost center in its cost impact calculation. Because the government had never specifically asserted a claim for a violation of that FAR cost principle, it could not include that amount in the damages it sought from Raytheon. With respect to the rest of No. 57576 and the other two appeals, the Judge had more work in front of him.

Judge Delman reminded the litigants that "An 'expressly unallowable' cost, by the plain terms of the definition, must be an item of cost or a type of cost that is specifically named and stated as unallowable by law, regulation or contract." He then explored the various FAR cost principles to determine whether or not "BAIC" was expressly unallowable under each. He concluded as follows:

31.205-1 – BAIC was not specifically named and stated as being unallowable. Victory to Raytheon. However, Judge Delman did not rule on whether BAIC was merely unallowable, or whether it was a directly associated unallowable cost. The parties will have to proceed to trial on those issues.

31.205-22 – BAIC was not specifically named and stated as being unallowable. Victory to Raytheon. However, Judge Delman ruled that the BAIC paid to individuals engaged in such activities was unallowable (but not *expressly* unallowable), so the Government won on that issue.

31.205-27 – BAIC was not specifically named and stated as being unallowable. Victory to Raytheon.

31.205-47 – Because the cost principle made "all elements of compensation" unallowable, and "it is unreasonable under all circumstances to conclude that [Raytheon's] BAIC costs with respect to the defined proceedings are allowable," the BAIC was found to be expressly unallowable. Victory to the Government.

With respect to Nos. 57679 and 58290, Judge Delman found that certain aspects of Raytheon's Long-Term Performance Plan (LTTP) were expressly unallowable under 31.205-6(i). That was a victory for the Government.

To the extent that the Government "won" a victory with respect to Raytheon's claimed costs, Raytheon argued that the Government should be precluded from recovering any damages, under the "retroactive disallowance" principle. Judge Delman wrote—

According to [Raytheon], given the government's consistent approval of and/or acquiescence to the subject BAIC and TSR metric costs, it was barred from disallowing those costs prior to the issuance of an authoritative notice that such costs were no longer allowable. [Raytheon] posits that the government's 2011 final decisions on the BAIC costs and TSR costs were the first such government notices, and hence any costs incurred prior to these dates are not recoverable.

(Internal citations omitted.)

Judge Delman found that there were material facts in dispute on that affirmative defense, and declined to issue summary judgment to either party. Thus, the matter will proceed to trial.

What is one to make of this Raytheon decision? First, there will be a trial and there will be another decision. And that decision may well be appealed by either party (or both parties). Therefore, it's not clear at this point how big a victory Raytheon won. That said, it's fairly clear that the amount of damages sought by the government was whittled down significantly by summary judgment.

Other commenters, more learned that we, offered the opinion that Judge Delman's rulings in favor of the government were flawed. For example, one set of legal practitioners **wrote** –

Unfortunately, the *Raytheon* decision does nothing to resolve the long-standing dispute

between contractors and the government regarding the proper application of expressly unallowable penalties. Specifically, while the Board acknowledged that a cost is only subject to penalty if it is 'specifically named and stated to be unallowable,' the Board then found that certain bonus and incentive costs where an employee billed time to unallowable legal activity and long term compensation costs that include a Total Shareholder Return (TSR) element, both which are not expressly referenced anywhere in the FAR, are expressly unallowable. Thus, contractors will be left guessing at whether the government will consider particular costs to be expressly unallowable even if they are not specifically named in the FAR.

Thus, it appears that to the extent Raytheon lost an aspect of its appeals, legal commenters believe that Judge's logic was flawed. That might give some hope to Raytheon, as it considers whether or not to appeal the ASBCA decision.