
Legal Insights: Holding the Government to Commercial Contract Terms

By Ross Crown

The United States Court of Federal Claims recently handed down an opinion addressing the federal government's liability under a commercial-style equipment lease. In *DMS Imaging, Inc. v. United States*, 2015 WL 6469461 (Fed. Cl. October 27, 2015), DMS leased to the Department of Veterans Affairs a mobile MRI system. The procurement was a sole source due to the VA's critical need for this diagnostic tool. DMS presented to the VA its standard commercial lease for execution. The contracting officer delegated review of the contract to a subordinate and did not herself read anything other than the cover page of the agreement. She also did not consult with the VA's legal department. Notwithstanding this superficial assessment of the proposed contract, the VA signed a nine month lease for the MRI unit.

The VA used the MRI unit for about six weeks until it was destroyed in a fire. After the fire, DMS sought to recover from the VA compensation owed under the lease. The VA paid nothing. In accordance with the Contract Disputes Act, DMS submitted a claim to the contracting officer. The contracting officer denied the claim and DMS appealed this denial to the Court of Federal Claims.

This case presents an unusual scenario. Due to the rushed nature of the procurement, coupled with inadvertence on the part of its contracting officer, the VA was faced with liability under contractual terms common in a commercial lease, but not the kind of provisions generally found in a government contract. In defending the appeal, the VA deployed a variety of contract defenses mostly unique to the government. Unfortunately for the VA, the Court found these defenses inapplicable and held the agency bound to the terms of the contract it signed.

The appeal focused on the Risk of Loss clause in the lease. This provision recited that the "Lessee shall bear the entire risk of loss, theft, destruction or damage of the leased property from any cause whatsoever" and that no such loss "shall relieve Lessee of the obligation to pay rent or any other obligations under this lease." The VA argued that, as a federal government agency, it could not be held subject to what it considered an oppressively one-sided provision.

After considering the arguments of the parties, the Court observed that a contractual provision is not unenforceable simply because it is not particularly favorable for the government. An agreement the government executes without negotiating or changing a contractor's proposed contractual language remains binding. When the government enters the commercial marketplace, it sheds its sovereign mantle and must honor its bargains just as any other contracting party.

In trying to get out from under the obligations of the Risk of Loss clause, the VA challenged the Court's jurisdiction over the

appeal, its liability to DMS for lease payments for the months after the MRI unit was destroyed, and its responsibility for late payment fees, service charges and attorneys' fees. The Court rejected each of these contentions.

Court's Jurisdiction Over Appeal

The VA's first defense was a motion to dismiss the appeal for lack of jurisdiction. In its motion, the VA contended that the appeal was a request for specific performance disguised as damages action. The VA interpreted DMS' claim as a demand that the Court require the VA to lease the MRI machine for the period of time prescribed in the agreement. The VA relied on case authority to argue that the Court could not award DMS the damages spelled out in the lease because this would be a requirement that the government perform the contract. The Court held the cases cited by the VA inapplicable, found DMS was seeking only an award of damages permitted by the lease and denied the VA's motion to dismiss.

Unpaid Lease Payments

The VA objected to paying rent for the months after the MRI unit was destroyed. Initially, the VA argued that the Prompt Payment Act (PPA) prevents the government from paying for goods or services not received. The Court disagreed. It noted that the purpose of the PPA is to provide incentives for the government to pay its bills on time. The PPA, said the Court, is not pertinent to the present case as DMS did not seek interest under this statute. According to the Court, there is nothing in the PPA that prohibits the government from fulfilling its contractual obligation to pay for the entire term of a lease where the leased equipment was destroyed while in the government's possession.

In another effort aimed at avoiding making all of the lease payments, the VA contended that the contract was "constructively terminated" at the time of the fire, advancing the theory that because the fire destroyed the object of the lease, the government's obligations under the lease ended. This argument, the Court ruled, was inconsistent with the lease. Again, the Court noted, the government entered into a valid contract that put the risk of loss of the leased property on the government itself. The contract did not leave room for a constructive termination argument.

The VA then invoked the frustration of purpose doctrine to argue that the government had no obligation to pay the remaining lease payments because the purpose of the contract was frustrated by the fire. The Court held the frustration of purpose doctrine inapposite since the Risk of Loss clause expressly stated that the government as lessee would bear the risk of loss for destruction of the MRI unit and



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that such destruction would not relieve the government of its obligation to make lease payments.

Finally, the government maintained that DMS was not entitled to eight months of unpaid lease payments because it did not show how much of the monthly payments would have been profit. The Court said the government's notion that DMS must prove the individual components of each monthly payment and justify that each such element is a proper form of damages is incorrect. Instead, the Court held the parties agreed on the amount of the monthly lease payments and that the government would be responsible for these payments if the MRI unit were destroyed.

Late Payment Fees and Service Charges

DMS also claimed entitlement to a monthly 5 percent late fee and a 1.5 percent service charge on the unpaid lease payments. The DVA objected to paying this fee and charge by again citing the Prompt Payment Act. Accordingly to the VA, the Court should have denied DMS' request for late fees and service charges as interest owing on the unpaid balance. The VA contended that the PPA is the only means by which a contractor can receive these types of payments from the government. Thus, DMS did not qualify for prompt payment interest and the lease's late payment provision was not authorized by law. The Court ruled against the VA, however, finding there is no provision of the PPA preventing a commercial entity and the government from separately agreeing via contract for the payment of late fees, services fees and interest. Here, DMS did not claim PPA interest. The contractor's claim for the late fee and service charge was based solely on the lease. Although sovereign immunity shields the government from interest charges for which it would otherwise be liable, the Court noted an agency can waive that immunity by contract. It is well-established that interest can be awarded against the government if the contract provides for the interest payment so long as the provision is affirmative and unambiguous.

Attorneys' Fees

The lease between DMS and the VA provided that in the event that legal or other action is required to enforce the Lessor's rights thereunder, Lessee agrees to reimburse Lessor for its reasonable attorneys' fees and costs. The VA disclaimed any liability for attorneys' fees by contending the Court lacked the power to grant DMS an award of attorneys' fees under the lease. First, the VA argued that the Tucker Act did not permit the Court to award attorneys' fees because they are unrelated to contract performance and the government did not waive sovereign immunity for fee-shifting. Second, the VA argued that because the Tucker Act does not waive sovereign immunity, the only way for DMS to recover attorneys' fees is under the Equal Access to Justice Act (EAJA).

At issue, said the Court, is whether an express fee-shifting term in a lease signed by the VA's contracting officer constitutes an affirmative waiver of sovereign immunity

subjecting the government to liability for attorneys' fees. The Court observed it is settled law that, as is true of interest payments, the government can waive sovereign immunity with respect to attorneys' fees by entering into an enforceable contract with an express fee-shifting provision. Here, the Court concluded that the government affirmatively waived sovereign immunity as to payment of attorneys' fees.

The VA further contended that the EAJA defines the limits of the waiver of sovereign immunity for payment of attorneys' fees and, absent compliance with the EAJA, the government cannot be liable to contractors for payment of attorneys' fees. The Court shot down this defense as well since DMS was only seeking attorneys' fees under a contract that expressly provides for such fees. The Court concluded the EAJA does not preclude a fee award under these circumstances.

What Can We Learn?

As noted above, *DMS Imaging* presents an unusual scenario. The VA allowed an urgent need for an item and an inattentive contracting officer to override its usual procurement practices and enter into a commercial equipment lease. The agency's ensuing struggles to dodge the consequences of contract provisions commonplace in the commercial world are almost comical. Because this case is not typical, it does not necessarily offer much guidance to contractors engaged in more conventional contract disputes with the government. At the same time, however, the decision does demonstrate that the plain terms of a contract will often override legal defenses on which the government generally depends. Contractors should not be reluctant to rely on commercial language the government finds distasteful and they can cite *DMS Imaging* as support when they do so. •

Ross is a partner in the Albuquerque office of Lewis Roca Rothgerber LLP where his practice emphasizes government contracts. This article is intended for general information only and should not be construed as legal advice or opinion. Any questions concerning your legal rights or obligations in any particular circumstance should be directed to your lawyer.

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