Michigan Law Review

Volume 62 | Issue 6

1964

Government Contracts-Judicial Review Under Disputes Clause

Amos J. Coffman Jr.
University of Michigan Law School

GOVERNMENT CONTRACTS—JUDICIAL REVIEW UNDER DISPUTES CLAUSE—In a factual dispute arising under a standard government construction contract, the contractor followed the procedures required by the disputes clause.[1] The contractor, after its claim was denied by the contracting officer, appealed to the Board of Claims and Appeals of the Corps of Engineers. The Board rejected the claim, and the contractor brought suit in the Court of Claims, alleging, in the words of the Wunderlich Act,[2] that the Board's decision was "capricious or arbitrary or so grossly erroneous as necessarily to imply bad faith, or was not supported by substantial evidence." Over the Government's objection, a commissioner of the court received evidence de novo and concluded that the contractor was entitled to recover. The court received further evidence on the issue of damages and entered judgment for the contractor.[3] On certiorari, *held*, reversed, two Justices dissenting. In cases subject to the standard disputes clause, the court may look only to the administrative record in order to determine, with respect to any of the Wunderlich Act's standards of finality except fraud, whether the administrative decision should retain its finality. *United States v. Carlo Bianchi & Co.*, 373 U.S. 709 (1963).

Under the standard disputes clause, an appeal from the decision of a contracting officer is generally to a contract appeals board to which the department head has delegated his authority.[4] These boards operate under

1 The standard clause involved in the principal case provided: "Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the contracting officer subject to written appeal by the contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties thereto. In the meantime the contractor shall diligently proceed with the work as directed." Principal case at 710 n.2. This clause became obsolete with the passage of the Wunderlich Act, 68 Stat. 81 (1954), 41 U.S.C. §§ 321-22 (1958). The clause currently in use is found in Standard Form 23A: General Provisions (Construction Contract), 41 C.F.R. § 1-16.901-23A(6) (1963). The essential change is the inclusion of the language of the Wunderlich Act, quoted note 2 *infra*.

2 68 Stat. 81 (1954), 41 U.S.C. §§ 321-22 (1958). The first section, which is the only one here applicable, provides: "No provision of any contract entered into by the United States, relating to the finality or conclusiveness of any decision of the head of any department or agency or his duly authorized representative or board in a dispute involving a question arising under such contract, shall be pleaded in any suit now filed or to be filed as limiting judicial review of any such decision to cases where fraud by such official or his said representative or board is alleged: *Provided, however*, that any such decision shall be final and conclusive unless the same is fradulent [*sic*] or capricious or arbitrary or so grossly erroneous as necessarily to imply bad faith, or is not supported by substantial evidence."

3 For discussions of this case and others subsequent to the Court of Claims decision, see Harrison, *Eight Years After Wunderlich—Confusion in the Courts*, 28 GEO. WASH. L. REV. 561 (1960); Note, 17 WYO. L.J. 73 (1962).

4 Haas, *Contract Procedures for Obtaining Additional Compensation Under Government Construction Contracts*, 24 FORDHAM L. REV. 535, 543 (1956); Joy, *The Disputes Clause in Government Contracts: A Survey of Court and Administrative Decisions*, 25 FORDHAM L. REV. 11, 17 (1956). Not all of the departments and agencies have such boards. Thus, references in the text to "board" will include reference to department and agency heads where no board is in existence.

procedural rules and regulations promulgated by the various departments and agencies[5] and are not subject to the Administrative Procedure Act.[6] In *United States v. Wunderlich*[7] the Supreme Court declared that fraud was the only ground on which the finality of a board's decision could be challenged. Prior to this decision, the standards of finality established by the Supreme Court had been fraud and error so gross as to imply bad faith.[8] The Court of Claims had expanded the list of standards to include arbitrariness and capriciousness,[9] but in the district[10] and circuit courts there was some dissent[11] from this expansion. It is not altogether clear what procedure was followed by the courts in reviewing decisions of boards during the pre-*Wunderlich* period; however, it appears that they must have admitted evidence de novo or else held full trials de novo prior to making any decision on the question of finality.[12] The Wunderlich Act, passed in response to the *Wunderlich* case,[13] was an attempt to restore the availability of review on broader grounds. The intent of Congress, as specifically set forth in the committee reports, was to adopt the standards generally applied prior to the *Wunderlich* case,[14] and to add one new standard—substantial evidence.[15] The avowed purpose of this addition was to force each party to

5 *E.g.*, Agriculture Department, 7 C.F.R. §§ 2.400-.440 (1963); Department of Defense, 32 C.F.R. § 30.1 (Cum. Supp. 1963); Rules of the Corps of Engineers Board of Contract Appeals, 33 C.F.R. § 210.4 (1962).

6 60 Stat. 237 (1946), 5 U.S.C. §§ 1001-11 (1958). It is not wholly clear that the Administrative Procedure Act does not apply; however, it has never been applied and the Government Accounting Office recently ruled specifically that it has no application to procedures arising under the disputes clause. G.A.O. B-152346, 32 U.S.L. WEEK 2280 (Nov. 22, 1963).

7 342 U.S. 98 (1951).

8 United States v. Moorman, 338 U.S. 457, 461 (1950). In some of the earlier cases, failure to exercise honest judgment was also a ground for denying finality, but this standard was subsequently dropped. Martinsburg & P.R.R. v. March, 114 U.S. 549, 551 (1885).

9 L. E. Myers Co. v. United States, 101 Ct. Cl. 41, 64 F. Supp. 148 (1944); Silberblatt & Lasker, Inc. v. United States, 101 Ct. Cl. 54 (1944).

10 The district courts are given jurisdiction concurrent with that of the Court of Claims over claims not exceeding $10,000 by 28 U.S.C. § 1346(a)(2) (1958). Jurisdiction is conferred on the Court of Claims by 28 U.S.C. § 1491 (1958).

11 See Lindsay v. United States, 181 F.2d 582 (9th Cir. 1950), where fraud and gross mistake implying bad faith were the only two standards applied.

12 An administrative record was not always available as a basis for review. See Volentine & Littleton v. United States, 136 Ct. Cl. 638, 145 F. Supp. 952 (1956). Extensive findings of fact were made in all Court of Claims decisions. *E.g.*, Great Lakes Dredge & Dock Co. v. United States, 116 Ct. Cl. 679, 90 F. Supp. 963 (1950); Loftis v. United States, 110 Ct. Cl. 551, 76 F. Supp. 816 (1948); Bein v. United States, 101 Ct. Cl. 144 (1943). And, when a board's decision was overturned, no further administrative proceedings were necessary before judgment could be rendered by the Court of Claims. Great Lakes Dredge & Dock Co. v. United States, *supra*; Loftis v. United States, *supra*; Bein v. United States, *supra*.

13 H.R. REP. No. 1380, 83d Cong., 2d Sess. 1 (1954); S. REP. No. 32, 83d Cong., 1st Sess. 1 (1953). The Senate report is substantially included in that of the House; hereafter only the House report will be cited.

14 H.R. REP. No. 1380, *op. cit. supra* note 13, at 1, 2, 3.

15 Substantial evidence means "such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." Consolidated Edison Co. v. NLRB, 305 U.S.

present its side of the controversy openly and to afford each an opportunity to rebut the other's evidence.[16] By including the substantial evidence requirement in the Wunderlich Act, Congress called forth a wealth of precedent concerning judicial review of administrative decisions. The standard had long been used in this area, and in all but a few instances its application had been limited to review based solely on the administrative record.[17]

Substantial evidence, however, was only one of the five standards contained in the Wunderlich Act. Although the manner of review concerning substantial evidence was fairly clear,[18] the manner of review with respect to the other four standards was not. This is evident from the fact that, subsequent to the *Wunderlich* decision, a split developed between the Court of Claims (which admitted evidence de novo whenever a transgression of any of the standards was alleged)[19] and the district courts (which refused to look beyond the administrative record unless fraud was alleged).[20] In the principal case the Supreme Court followed the district courts, thus declaring, in effect, that the nature of review appropriate to the substantial evidence standard is appropriate also to all the other standards except fraud. The Court conceded that, where fraud is alleged, evidence extrinsic to the record is admissible in order to prove it.[21]

In reaching its decision the Court relied on the Wunderlich Act, interpreting it as limiting the manner of review of a board's decision to an examination of the administrative record only. The Court found support in both the language of the act and its legislative history, placing particular emphasis on the inclusion of the substantial evidence standard.[22] However, a careful examination of both these sources indicates that the Court's interpretation was not forced upon it by either, and that, but for the presence of the substantial evidence standard, the opposite conclusion might easily have been reached. The act speaks only of the availability of judicial review, saying nothing about the manner of review, and the legislative history gives no definite indication that Congress intended to deal with anything more than availability.[23]

197, 229 (1938). This basic test was adhered to in Universal Camera Corp. v. NLRB, 340 U.S. 474 (1951), where it was also held that the review should be on the whole record and not merely on the evidence tending to support the finding.

16 H.R. REP. No. 1380, *op. cit. supra* note 13, at 5.

17 See Mann Chem. Labs. v. United States, 174 F. Supp. 563, 565 (D. Mass. 1958).

18 Principal case at 715.

19 *E.g.*, P.L.S. Coat & Suit Corp. v. United States, 148 Ct. Cl. 296, 180 F. Supp. 400 (1960); Carlo Bianchi & Co. v. United States, 144 Ct. Cl. 500, 169 F. Supp. 514 (1959), *rev'd*, in principal case; Fehlhaber Corp. v. United States, 139 Ct. Cl. 837, 151 F. Supp. 817, *cert. denied*, 355 U.S. 877 (1957); Volentine & Littleton v. United States, 136 Ct. Cl. 638, 145 F. Supp. 952 (1956).

20 *E.g.*, Wells & Wells, Inc. v. United States, 269 F.2d 412 (8th Cir. 1959); United States v. Hamden Co-op. Creamery Co., 185 F. Supp. 541 (E.D.N.Y. 1960), *aff'd*, 297 F.2d 130 (2d Cir. 1961); Mann Chem. Labs. v. United States, 174 F. Supp. 563 (D. Mass. 1958).

21 Principal case at 714.

22 *Id.* at 714-17.

23 Concerning the act's language, the Court noted that the act is entitled, "An

If, therefore, the act deals only with availability of review, the Court in the principal case was, in reality, free to consider the most appropriate manner of review under the various standards. An approach more in line with the intent of Congress to make review available would have been to segregate the substantial evidence standard just as the Court had previously segregated fraud,[24] for yet a third kind of review would be most appropriate where it is alleged that a board's decision was arbitrary or capricious or so grossly erroneous as necessarily to imply bad faith. If, for example, a board considered evidence submitted ex parte to be decisively significant,[25] its decision would apparently be capricious or arbitrary, yet the reviewing court would not necessarily discover this by looking at the administrative record alone. It is possible that a decision ultimately turning on such evidence would still be supported by substantial evidence. If, therefore, meaningful review is to be available under these three standards, the contractor must be allowed to introduce in court a limited amount of evidence extrinsic to the record,[26] and in denying the admission of any extrinsic evidence, the Supreme Court appears partially to have contravened the policy behind the Wunderlich Act. This is not to suggest a return to the Court of Claims position with an exception for substantial evidence. Only evidence dealing directly with whether a board's decision was fraudulent,

Act to permit review . . . ." Principal case at 714. It relied on National Broadcasting Co. v. United States, 319 U.S. 190 (1943), and Tagg Bros. & Moorhead v. United States, 280 U.S. 420 (1930), to show that where, in other legislation, Congress had called for "review" without specifying procedures, the Court had refused to admit evidence extrinsic to the administrative record. In those cases the Secretary of Agriculture and the Federal Communications Commission were authorized by statutes to fix rates and make regulations, respectively. They performed typical administrative functions, and their procedures are today subject to the Administrative Procedure Act (APA), 60 Stat. 237 (1946), 5 U.S.C. §§ 1001-11 (1958). In the area of government contracts, the administrative authority is conferred by contract, and, as noted in text, the APA is not applicable. The differences between these two contexts suggest that it is not necessary that one control the other.

As to the intent of Congress, the manner of review contemplated under the proposed legislation is not once specifically mentioned in H.R. REP. No. 1380, *op. cit. supra* note 13, or in the hearings. *Hearings Before the Subcommittee on Review of Finality Clauses in Government Contracts of the House Committee on the Judiciary*, 83d Cong., 1st & 2d Sess., ser. 12 (1953-1954) [hereinafter cited as *Hearings on Review of Finality Clauses*]; *Hearings on S. 2487 Before a Subcommittee of the Senate Committee on the Judiciary*, 82d Cong., 2d Sess. (1952). The question of the manner of review utilized prior to the *Wunderlich* decision came up twice in the House hearings (two witnesses flatly contradicted each other, *Hearings on Review of Finality Clauses* 59, 79), but not a word was uttered shedding any light on the kind of review anticipated.

24 *E.g.*, principal case at 714.

25 The dissent hinted that this may have been true in the principal case. See principal case at 719. On remand, however, the issue was not presented. Carlo Bianchi & Co. v. United States, No. 466-54, Ct. Cl. Comm'r Rep., Nov. 4, 1963, at 2.

26 The Court of Claims has taken the principal case to mean that the court may base its action on *nothing* but the administrative record and briefs of counsel. See Wingate Constr. Co. v. United States, No. 394-60, Ct. Cl., Jan. 24, 1964, at 7 (by implication); Carlo Bianchi & Co. v. United States, *supra* note 25, at 2. Thus the court would apparently not consider a party's affidavit that the board had grounded its decision on ex parte information or otherwise acted arbitrarily or capriciously in a manner not reflected in the administrative record.

arbitrary, capricious, or so grossly erroneous as necessarily to imply bad faith should be admissible.[27] Such a procedure would be particularly appropriate in view of the trial facilities maintained by the reviewing courts.

It is arguable that the Wunderlich Act should be interpreted as going to the jurisdiction of the reviewing courts, although this position does not appear to have been accepted by any court. Such an approach would view the act as conferring original jurisdiction where fraud is alleged and as conferring a sort of appellate jurisdiction in all other cases. The following factors tend to confirm the position recently taken by the Court of Claims that the act has nothing to do with jurisdiction.[28] First, the act speaks in terms of pleading and review; there is no express jurisdictional language.[29] Second, although there is no conclusive expression of congressional intent, it appears that none of the participants in the hearings before the House subcommittee believed that a jurisdictional question was involved.[30] Third, these same hearings indicate that Congress must have intended merely to achieve a statutory revision of the terms of the disputes clause.[31] Since the parties to a contract cannot, by that contract, deprive a court of its jurisdiction,[32] alteration of the terms of a contract cannot affect jurisdiction. Finally, the act need not be interpreted as a jurisdictional statute in order to provide for the full effectuation of the act's purposes.

It should also be noted that contract appeals boards are not independent administrative agencies, and the Court's decision has the effect of applying to the former the manner of review appropriate to the latter. It is true that the Wunderlich Act is a step toward formalization of the whole disputes process, but, until Congress sees fit to subject contract appeals boards to the Administrative Procedure Act or a similar procedural system, the decisions of these boards should not be invested with the same degree of finality as, for example, those of the Federal Power Commission.

Amos J. Coffman, Jr.

27 In practice this might in certain cases amount to an opportunity to place before the reviewing court all of the evidence relied on by the board which does not appear in the record. This procedure would assume particular significance in instances where the record is "inadequate." See principal case at 717.

28 In Stein Bros. Mfg. Co. v. United States, 32 U.S.L. WEEK 2050 (Ct. Cl. July 12, 1963), the Court of Claims held that the Wunderlich Act, as interpreted by the Supreme Court in the principal case, did not go to the jurisdiction of the reviewing court, but rather set forth procedural rights which must be asserted else they are waived. The court applied this doctrine in a case in which the Government failed to object to the holding of a trial de novo until after the trial itself had been completed. *Accord*, WPC Enterprises, Inc. v. United States, 323 F.2d 874 (Ct. Cl. 1963).

29 68 Stat. 81 (1954), 41 U.S.C. § 321 (1958).

30 Their collective reaction to a disputes clause adopted by the defense department subsequent to the *Wunderlich* decision was only that, though the clause contained the standards generally believed to have prevailed prior to that decision, not all agencies would voluntarily adopt such a clause, and that no agency, once it adopted the clause, could be forced to retain it. *Hearings on Review of Finality Clauses* 32, 43-44, 58, 97, 103. No one expressed the idea that it was necessary to circumscribe the jurisdiction of the reviewing courts in order to fulfill the general purpose of any of the proposed bills.

31 *Hearings on Review of Finality Clauses* 35, 97.

32 6A CORBIN, CONTRACTS § 1432 (1962), and authorities cited therein.