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Author: Ralph C. Nash, Professor Emeritus of Law, The George Washington University
Contributing Authors: Vernon J. Edwards and James F. Nagle

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¶ 72 COMMERCIAL ITEMS: Confusion In Court

Vernon J. Edwards

The Government often says that it wants to do business with commercial firms, but that many commercial firms don't want to do business with the Government. Wonder why? Consider the case of JKB Solutions and Services, LLC, a small business of Norfolk, Virginia, hereinafter "JKB."

Background To The Dispute

In 2015, the Army used simplified acquisition procedures to award an indefinite-delivery, indefinite-quantity contract to JKB for education/training-training/curriculum development services. The procurement was set aside for small businesses, and the agency made the award pursuant to Federal Acquisition Regulation Part 12, "Acquisition of Commercial Items." The first page of the contract was Standard Form 1449, "Solicitation/Contract/Order for Commercial Items," and the contract included the clause at FAR 52.212-4, "Contract Terms and Conditions—Commercial Items." The contract provided for a one-year ordering period, included options for two additional one-year ordering periods, and permitted the Government to order up to 14 training classes in each ordering period. The agency reported the estimated value of the award, including the first period and the two option periods, as $1,072,594.00. The specified minimum amount was $15,000.

At the beginning of the first ordering period the agency issued a fully funded "delivery order" for one "lot" of 14 classes. The value of the order was equal to the value of the 14 classes, and the agency obligated funds for the full amount. But the agency required JKB to conduct only nine classes and used Government personnel to conduct the remainder. The agency did the same thing at the beginning of each of the two successive ordering periods, requiring the conduct of thirteen classes in the second and eight in the third.

The agency paid JKB for the classes it taught. Then in 2018 it modified the three delivery orders to deobligate the balances of the funding. JKB submitted a claim on June 11, 2018, in reaction to the deobligations, asserting that since the agency had issued delivery orders for 14 classes in each period it had bought them and was obligated to pay for all of them. The agency Contracting Officer

rejected that claim on November 20, 2018, asserting that it was obligated to pay only for services rendered. The contractor filed a second claim on January 6, 2019, to which the CO did not respond.

The Appeal To The Court Of Federal Claims

JKB appealed to the U.S. Court of Federal Claims on September 11, 2019. The Government moved for dismissal or summary judgment, arguing that it was obligated under contract to pay only for services rendered. It argued alternatively that it had constructively terminated the orders for the remaining classes pursuant to FAR 52.212-4, paragraph (l), "Termination for the Government's convenience," and was thus obligated to pay only termination costs.

The court found the contract to be latently ambiguous as to whether the Government was required to pay for services ordered but not required. "The result is a quintessential case of contractual ambiguity because the contract's language is reasonably susceptible to differing interpretations." *JKB Solutions & Services, LLC v. U.S.*, 148 Fed. Cl. 93 (2020). It denied the Government's motions and ordered it to file an answer to the contractor's complaint.

In its answer, the Government again asked the court to find that it had constructively terminated the contract for convenience pursuant to FAR 52.212-4(l). In response, JKB argued that FAR 52.212-4 did not properly apply to the contract in question because the contract did not procure commercial items, that the contract thus did not include an applicable termination for convenience clause, and that the Government thus could not assert constructive termination. The court decided as follows:

> *JKB argues that FAR 52.212-4(l) is inapplicable in this case because that section of the FAR deals with commercial item contracts, and this contract between JKB and the Government is a service contract.* JKB is mistaken. It is true that FAR 52.212-4 does have the heading "Contract Terms and Conditions—Commercial Items." *However, as the Government correctly notes, nothing in the FAR limits the applicability of Section 52.212-4(l) to commercial item contracts.* To allow JKB to escape the application of the termination for convenience clause, which was incorporated by explicit reference into its contract with the Army, simply because the clause was initially envisioned as a provision in a different sort of contract would be to deny the Government the benefit of its bargain. The Court will not do this. [Emphasis added.]
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> First, the contract between JKB and the Army did contain a termination for convenience clause. The contract explicitly states that it "Incorporates By Reference FAR 52.212-4." As the Government notes, the relevant question in this case is whether each task order issued pursuant to the contract between JKB and the Army also included a termination for convenience clause. They did. The contract said that "[a]ll...task orders are subject to the terms of this contract." Therefore, not only the contract, but also all of the task orders issued pursuant to it, included the termination for convenience clause from FAR 52.212-4(l).
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> Second, there is no indication that the Army terminated the task orders in bad faith, and its decision to do so was not an abuse of discretion.

JKB could recover only termination for convenience costs. *JKB Solutions & Services, LLC v. U.S.*, 150 Fed. Cl. 252 (2020).

Note that the first italicized sentence in the above quote seems to make a distinction between a commercial items contract and a service contract. Such a distinction is false because the term *commercial item* as defined in FAR 2.101 includes services. The proper distinction would have been between commercial items contracts for commercial services and noncommercial items contracts for noncommercial services.

Note, too, that the second italicized sentence in the quote suggests that the court did not understand the concept of FAR clause prescription, which is described in FAR 52.101(c), *Prescriptions*, as follows;

> (c) *Prescriptions.* Each provision or clause in [FAR] subpart 52.2 is prescribed at that place in the FAR text where the subject matter of the provision or clause receives its primary treatment. The prescription includes all conditions, requirements, and instructions for using the provision or clause and its alternates, if any. The provision or clause may be referred to in other FAR locations.

See FAR 12.301(b)(3), which prescribes the proper use of FAR 52.212-4:

> (b) Insert the following provisions in solicitations for the acquisition of commercial items, and clauses in solicitations and contracts for the acquisition of commercial items:
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> * * *
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> (3) *The clause at [FAR] 52.212-14, Contract Terms and Conditions-Commercial Items.* This clause includes terms and conditions which are, to the maximum extent practicable, consistent with customary commercial practices and is incorporated in the solicitation and contract by reference (see Block 27, SF 1449). Use this clause with its Alternate I when a time-and-materials or labor-hour contract will be awarded. The contracting officer may tailor this clause in accordance with [FAR] 12.302.

See also FAR 52.101(d), *Introductory text*: "Within [FAR] subpart 52.2, the introductory text of each provision or clause includes a cross-reference to the location in the FAR subject text that prescribes its use." Then read the introductory text to FAR 52.212-4, which tells COs to insert that clause in contracts "As prescribed in FAR 12.301(b)(3)." Next, see FAR 1.401(a), which defines one type of FAR *deviation* as follows:

> (a) The issuance or use of a policy, procedure, solicitation provision (see definition in [FAR] 2.101) contract clause (see definition in [FAR] 2.101), method, or practice of conducting acquisition actions of any kind at any stage of the acquisition process that is inconsistent with the FAR.

Then read FAR Subpart 1.4, "Deviations From The FAR," sections 1.402, "Policy," 1.403, "Individual deviations," and 1.404, "Class deviations," which describe the procedures for obtaining authorization to deviate. Finally, see FAR 1.602-1(b), which commands COs to ensure that contract awards are made in compliance with "all" laws and regulations.

In short, it simply is not true, and the court was mistaken in saying that "nothing in the FAR limits the applicability of Section 52.212-4(l) to commercial item contracts." Why didn't the court know that? Perhaps because the parties' lawyers did not mention it.

If it were true that JKB's contract was not for commercial services, then the proper termination clause would have been either FAR 52.249-2, "Termination for Convenience of the Government (Fixed-Price)" or FAR 52.249-4, "Termination for Convenience of the Government (Services) (Short Form)," as prescribed in FAR 49.502(b), "Fixed-price contracts that exceed the simplified acquisition threshold." If the services acquired were not commercial items, then the insertion of FAR 52.212-4 in that contract was an unauthorized FAR deviation—a violation of a regulation that has the force and effect of law. The omission of the proper clause was also an unauthorized deviation. The court appears to have overlooked those facts, perhaps because the parties' lawyers did not present them to the court.

The Appeal To The Federal Circuit

JKB appealed the Court of Federal Claims decision to the U.S. Court of Appeals for the Federal

Circuit, *JKB Solutions & Services, LLC v. U.S.*, No. 2021-1257, 2021 WL 5348537 (Fed. Cir. Nov. 17, 2021), 63 GC ¶ 358. In its plaintiff-appellant brief, JKB again argued, as it had before the Court of Federal Claims, that (1) the services the Government specified and procured were not commercial items as defined in FAR 2.101, (2) FAR 52.212-4 thus did not apply to the contract, (3) the contract thus did not contain an applicable termination for convenience clause, and (4) the Court of Federal Claims should not have held that the Government constructively terminated the contract for convenience. See Brief of Appellant, *JKB Solutions & Services, LLC v. U.S.*, No. 2021-1257 (Fed. Cir. Jan. 19, 2021), 2021 WL 236305, at *9–12, stating:

> The plain language of the FAR makes it abundantly clear that FAR 52.212-4 applies only to contracts for commercial items. FAR 52.212-4(e) incorporates the definitions from FAR 52.202-1 into FAR 52.212-4. FAR 52.202-1 provides that unless certain circumstances exist, which are not present in this case, words and terms are given the same meaning as in FAR 2.101, which is the general definitions section of the FAR. FAR 2.101(a) expressly provides that a word defined in that section has the same meaning throughout all of the FAR (48 CFR Chapter 1) unless (1) The context in which the word or term is used clearly requires a different meaning; or (2) Another FAR part, subpart, or section provides a different definition for the particular part or portion of the part.
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> In other words, the definition of "commercial items" in FAR 52.212-4 is the exact same as the definition of that term in FAR 2.101…
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> As the above definitions explain, a commercial items contract is intended to allow the government to obtain items which are ordinarily sold to the public, in large quantities, in the commercial marketplace. While FAR 2.101(6) can apply to certain types of services which are "offered and sold competitively in substantial quantities in the commercial marketplace," this is clearly not the case with the present Contract. JKB taught classes only to U.S. government personnel. This is the only service that JKB provided, and it is not a type of service which is offered in substantial quantities in the commercial marketplace. In fact, by definition, this is not a service that could ever be offered in the commercial marketplace in any form, since the classes were provided exclusively on United States military installations to government personnel. *Therefore, FAR 52.212-4 does not apply because the Contract at issue in this appeal is a service contract and not a commercial items contract.* [Emphasis added.]
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> Furthermore, FAR 12.207 explains what type of contracts may be used to acquire commercial items. With the exceptions of time-and-materials and labor hour contracts, commercial items must be procured through fixed price contracts. While FAR 12.207(c) does allow Indefinite Quantity contracts for commercial items, this only applies when the fixed price of the commercial item is set forth in the prime contract. This is not the case in the present Contract, wherein the prime contract did not contain fixed prices for the classes but only estimates, and the government has admitted that the only way to order classes was via Task Orders.
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> FAR 12.207(e) explicitly states that the use of any other type of contract for commercial items is prohibited. FAR 12.207(e). FAR 16.202-2 confirms this, stating that a fixed price contract is suitable for the acquisition of commercial items when certain conditions are met. It is undisputed that the Contract at issue here is an IDIQ service contract under which classes were ordered via Task Orders. It was neither a fixed price contract, nor a commercial items contract. Therefore, FAR Part 12, of which FAR 52.212-4(l) is a part, simply does not apply.

Note the italicized sentence, which makes a false distinction between "commercial items contracts" and "service contracts." The appropriate distinction would have been between a contract for commercial services and a contract for noncommercial services.

Comments During Oral Argument

The Federal Circuit heard oral argument on September 2, 2021. The court's audio recording

reveals in several places that the lawyers and circuit judges either had a tenuous grasp of the rules governing the acquisition of commercial items and of how the FAR works or that they communicated poorly. Although they acknowledged at times that commercial items include services, they seem at other times to have thought that the word *items* in the term *commercial items* refers only to "goods," and that there is a distinction between a contract for commercial *items*, meaning *goods*, and a contract for a service. A few excerpts (times are approximate):

Judge at approximate 15:31, addressing counsel for the appellant: Is this contract applying to both items and services such that maybe this FAR provision applied only to your provision the portion of the contract in which you were providing goods as opposed to services? Or was this 100 percent a service contract?

* * *

Judge at approximately 20:20, addressing counsel for the Government: Why are there so many provisions in the FAR talking about terminations for convenience, some with respect to items, others with respect to services…?

Government counsel: The FAR does provide different types of termination for convenience clauses that, at times seem to reflect considerations related to certain forms of contracts, the, as we know, the FAR 12.301, which describes when the contracting officer, it describes inserting this FAR 52.212-4, and it doesn't say that it can only be used in a specific type of contracts…

Judge (interrupting): But it does refer to commercial items contracts.

Government counsel: It does refer in that part.

Judge: And then you've got FAR 52.249-4 that talks about inserting these kinds of clauses in service contracts. And so I guess my point is, why shouldn't we take FAR at face value and say, some of these relate to commercial items contracts, some of them relate to service contracts. But you can't just mix them up whenever you want to.

Government counsel: Well, plaintiff did not make an argument below that, that this, stating that a FAR provision like 52.212-4 could not be, that there was a specific reason it could not be used in this context. In fact, I…

Judge (interrupting): Didn't they say it was inapplicable because this is a service contract?

Government counsel: Yes, Your Honor.

Judge: That is the specific reason. So I think they did argue the specific reason.

Government counsel: Well, I think our position is that inapplicable and irrelevant are not reasons to excise a term out of a contract that both parties have signed.

Judge: Well, it's not a matter of excising it out, it's just a matter of you having included a term that wasn't relevant to the contract. I mean, it's not a matter of excising it out. It just doesn't apply. Well, this particular contract now, I mean, you, maybe you incorporate this in as a matter of standard course in every contract. But when you go on in detail that only services are being provided you understand, I mean, a lot of these government contracts that I've seen, my God, they just incorporate the entire FAR, it's like almost without regard for what the provision covers. So why isn't it reasonable to say you incorporated this into the extent that this contract was going to exist or be expanded to come cover commercial items, this provision would then apply, but to the extent it is applying to services as opposed to goods This provision is not going to apply?

* * *

Judge, at approximately 38:00, addressing counsel for the Government: So what is your best argument for why [FAR] 52.212, which expressly by its title suggests it's applicable to commercial items, and in light of a different FAR that is expressly extending a termination for convenience for services,

what is your best argument for why [FAR] 52.212-4 should nonetheless apply to this contract, even though it seems to be a pure services contract?

* * *

Appellant's counsel, at approximately 44:18: We point out that the services that were procured hereunder don't even come close to constituting commercial items. There were no items first of all, but second of all there is nothing commercial about teaching government employees government regulations that they will utilize as government contracting officers to procure goods for the government. And so there weren't any items. It has nothing to do with commercial.

* * *

Appellant's counsel, at approximately 48:26: There's absolutely, in my assessment, based upon what we have presented, there's no way that this clause could be applicable as a commercial items clause to a services contract.

Oral Argument of September 2, 2021, *JKB Solutions & Services, LLC v. U.S.,* No. 2021-1257, 2021 WL 5348537 (Fed. Cir. Nov. 17, 2021), transcribed by this author, available at *https://cafc.uscourts.gov/home/oral-argument/listen-to-oral-arguments*.

The Government did not dispute for the purposes of summary judgment the contractor's assertion that the service procured was not commercial. Oral Argument at approximately 23:31 and at 25:28. Instead, the Government argued, as it had at the Court of Federal Claims, that FAR 52.212-4(l) was, in fact, in the contract, that the contractor had assented to its terms when it signed the contract, and that by its own terms the clause did not limit its application to commercial services. This is surprising, to say the least. The Government had determined the service to be commercial and had advertised the procurement as one for commercial items. No one protested that determination. JKB was asserting that the service was not, in fact, commercial. That was the crux of its argument against constructive termination for convenience. If the Government could make a good case that it had properly determined the service to be commercial, then the propriety of including FAR 52.212-4 would be established and JKB's argument against constructive termination would be defeated. JKB's description and analysis of the service in its plaintiff-appellant brief is interesting, but it struck us as inconclusive, so why not dispute it? Was the Government unsure that it could convince the court that its determination had been rational?

The Federal Circuit's Decision

The Federal Circuit vacated the lower court's decision, stating:

Here, the Claims Court erred by holding that JKB Solutions' contract contained an applicable termination for convenience clause. The Claims Court relied solely on the contract's incorporation of FAR 52.212-4 by reference. *JKB Sol'ns II*, 150 Fed. Cl. at 256. *But, as explained below, FAR 52.212-4 governs the termination of commercial item contracts for the government's convenience, and it does not apply to service contracts, such as the contract at issue in this case.* [Emphasis added.]

* * *

The Claims Court rationalized its holding, finding that "nothing in the FAR limits the applicability of Section 52.212-4(*l*) to commercial item contracts." *JKB Sol'ns II*, 150 Fed. Cl. at 255–56. The government reiterates this reasoning on appeal. As previously noted, the text of FAR 52.212-4 and FAR 12.301 limit the applicability of the incorporated termination for convenience clause to commercial item contracts. The existence of other termination for convenience clauses in the FAR further supports our conclusion. For example, Part 52 of the FAR provides for the insertion of several termination for convenience clauses "[a]s prescribed" in FAR 49.502. *See* FAR 52.249-1 to 52.249-5 (2015). FAR 49.502 prescribes the insertion of FAR 52.249-4's "Termination for Convenience of the Government (Services) (Short Form)" clause

> in certain "contracts for services." FAR 49.502(c) (2015). Moreover, the FAR provides that the part to which FAR 49.502 belongs "does not apply to commercial item contracts awarded using part 12 procedures." FAR 49.002(a)(2) (2015). A different FAR provision, which references FAR 52.212-4, governs the termination policies of those contracts for the acquisition of commercial items. *Id.* (citing FAR 12.403 (2015)). The FAR's own distinction between termination for convenience clauses based on types of contracts confirms that FAR 52.212-4's termination for convenience clause does not apply to JKB Solutions' service contract.
>
> We are unpersuaded by the government's remaining arguments as to the applicability of FAR 52.212-4.

So the court accepted JKB's argument, but did it do so for the right reason? Note in the italicized sentence that the court seems to have based its decision on a false distinction between commercial item contracts and service contracts, despite the fact that the parties' attorneys had pointed out on several occasions during oral argument, albeit inconsistently, that services could be commercial items. Whether the italicized sentence is the product of ignorance, faulty reasoning, or just careless writing is anyone's guess, but it startled some persons in the acquisition community, who contacted us to express confusion and concern about what it might mean.

The Federal Circuit remanded the case to the Court of Federal Claims, stating that the court could consider whether a termination clause could be incorporated into the contract via the *Christian* doctrine. But that might be problematical based on the Federal Circuit's decision in *Maxima Corp. v. U.S.*, 847 F. 2d 1549 (May 1988).

Voluminous, Convoluted, And Confusing Rules

If the lawyers and judges involved in the *JKB* case were confused about commercial items and services, it is no wonder. The term *commercial items* was misleading for more than 20 years, and the former definition of *commercial items* in FAR 2.101 was awful. The Section 809 Panel, in Volume 1 of its Final Report, said of the old definition:

> The FAR's commercial buying terms are confusing, poorly defined, or undefined altogether. The term commercial item is overly broad, encompassing both commercial products and commercial services. The terms commercial item and commercially available off-the-shelf item appear in the U.S. Code in numerous sections, but do not incorporate the same universal definition; in some instances, the terms are defined differently, and in other instances they lack any definition at all. Subcontracting, which is subject to dozens of unique definitions for the terms subcontract and subcontractor, reflects similar disharmony. The inconsistency among commercial definitions generates confusion and creates risk that contracting officers may fail to apply commercial practices uniformly.

Vol. 1 of the Report of the Advisory Panel on Streamlining and Codifying Acquisition Regulations 26 (Jan. 18, 2018). We see confusion at work in the decisions of both the Court of Federal Claims and the Federal Circuit. One can only imagine how much confusion the thousands of pages of acquisition statutes, regulations, class deviations, and procedures cause among would-be new Government contractors. (The definition of commercial items that applied to JKB's contract was replaced by definitions of *commercial product* and *commercial service* effective December 6, 2021, see Federal Acquisition Circular 2022-01, 86 Fed. Reg. 61017 (Nov. 4, 2021). Whether the new definitions make anything clearer remains to be seen.)

Does The System Deter Firms From Seeking Government Contracts?

In *G.L. Christian & Associates v. U.S.*, 320 F.2d 345, 351 (1963), *cert. denied*, 375 U.S. 954 (1963), the original source of the *Christian* doctrine, the Federal Circuit's predecessor, the U.S. Court of Claims, famously stated:

> Like other individuals who deal with the Federal Government (*see, e.g.*, *Federal Crop Insurance Corp. v. Merril*, 332 U.S. 380, 68 S. Ct. 1, 92 L. Ed. 10 (1947)), potential contractors can validly be bound to discover the published directives telling them the limits and the scope of the agreements the Government can make.

That notion is absurd today. Full-time Government contracting personnel, lawyers, and judges struggle to understand, explain, and apply the Government's voluminous, poorly organized, and poorly written procurement rules. If they cannot understand them, how can would-be Government contractors hope to understand them? At one point during oral argument at the Federal Circuit one of the judges asked JKB's attorney why, if the services to be acquired were not commercial, his client did not object to the imposition of commercial item terms and conditions:

> Judge, addressing appellant's counsel at approximately 49:25: I understand all of your arguments about why these are services, not items. But what do we do with the fact that that you had a contract in front of you that very clearly incorporated this particular provision with specificity and you signed it saying it applies?
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> Appellant's counsel: Your Honor, I think that's a fair question.

A question to which he had no answer.

We think we know the answer. Large contractors that have been doing business with the Government for many years have contracting personnel who are steeped in the rules, and they can afford attorneys who are expert. But the kinds of companies that the Government wants to bring into its supply chain are not equipped to deal with the Government's awful rule system and COs who would do something as bizarre as issuing orders under an indefinite-delivery indefinite-quantity contract for a "lot" of 14 classes, obligate funds to pay for them without intending to use them all, then wait to deal with the matter until the end of the contract simply by deobligating funds. Why do something so strange, potentially confusing, and misleading as to order and fund the maximum quantity and then insist that you must pay only for the quantity you actually use? Was it to make office life easier by issuing only one order for a "lot" at the beginning of each of the three ordering periods, fund the entire quantity, and then write one modification at the end of the contract to deobligate excess funds from all three orders? Was it all about paperwork avoidance? Did someone receive an innovation award for coming up with that scheme? Did anyone explain to the contractor what was being done and why before doing it? Did anyone call or meet with the contractor to explain that ordering 14 classes under an IDIQ contract was not to be considered the same as actually buying them?

The Government needs COs who can navigate oceans of regulation, seas of procedure, and squalls of confusion and bring all passengers into the safe harbor of successful contract completion. It needs COs who know and can explain rules to contractors before there is a misunderstanding and dispute, and who can resolve conflicts that arise from administrative errors and misunderstandings without resort to expensive litigation. It needs COs who can speak coherently, persuasively, and reassuringly to anxious business partners.

When businesspersons ask me if they should pursue Government contracting opportunities I say, "It depends on how much you think you can make and what you are willing to put up with in order to make it." Then I tell them what I think they can expect from their business "partner." It is not an answer I like to give, but it's an honest one. Does the system deter firms from seeking Government contracts? We are not sure, but we think the system should give them pause. *VJE*

