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I. Introduction

In January of 1991, after three years of development, the United States Navy terminated its contract for the A-12 Avenger carrier-based stealth aircraft. Over twenty two years later, the legal saga to determine the remedy in this breach of contract dispute continues.

In *General Dynamics v. United States*[1] the Supreme Court of the United States examined what result should occur when the United States invokes its state secrets privilege to prevent discovery in a civil dispute.[2] The Supreme Court unanimously held that a court should leave the parties as it found them when the government is unable to adequately respond to a contractor's prima facie valid superior knowledge claim because the government properly invoked its state secrets privilege.[3] Despite the Court's assurance that its holding has clarified the state secrets privilege and will reduce litigation over the issue,[4] an understanding of the defense industry undermines the Court's assertion and questions the necessity of changing precedent.

The purpose of this note is to discuss the state secrets privilege in the contracts context and provide greater insight into its likely impact upon the defense industry. The analysis section posits that while the Court's holding appears, on its face, to be a practical way to reduce litigation when the state secrets privilege is raised, the Court's opinion — combined with changes in the defense industrial market — will likely lead to more litigation over the state secrets privilege.[5] Specifically, the *General*

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1. 131 S. Ct. 1900 (2011).
2. *Id.* at 1903.
3. *Id.* at 1906. The state secrets privilege is a well-established exception to the rules of discovery that permits the government to prevent disclosure of certain information pursuant to trial. United States v. Reynolds, 345 U.S. 1, 6–7.
4. *Gen. Dynamics Corp.*, 131 S. Ct. at 1909.
5. *See infra* Part V.A.

Dynamics holding is likely to increase litigation involving the state secrets privilege because the Court's decision (a) provides the government with the ability and incentive to use the new legal standard to its advantage,[6] (b) does not provide the government with incentive to contract around the state secrets privilege,[7] and (c) does not dissuade government contractors from pursuing litigation when contracts are cancelled.[8] These concerns are manifest in the present case as the Court's holding and its stated purpose appear to be at odds.[9] The Supreme Court should have affirmed the Court of Federal Claims' ruling that left the parties bound by the Contracting Officer's determination instead of issuing a decision that, in effect, determined the merits of a claim deemed to be nonjusticiable.[10] To remedy the current situation, Congress should pass legislation to statutorily restore the de facto prior precedent.[11]

II. The Case

In 1988, the Navy awarded two defense companies, General Dynamics Corporation and McDonnell Douglas Corporation, a contract for the full-scale engineering and development[12] of the A-12 Avenger carrier-based stealth aircraft.[13] The contract was a fixed-price agreement[14] with a ceiling price of approximately $4.8 billion dollars, which was to be paid in installments throughout the life of the agreement.[15] According to the contract, the Navy was to make an installment payment of $185,000,000 on November 1, 1990, and a second payment of $553,200,000 on January 7, 1991.[16] In return, the contractors were to produce eight prototype aircraft that were to test different characteristics of the A-12.[17] The first aircraft was scheduled to be delivered in June of 1990, with the other aircraft delivered monthly through January 1991.[18]

6. *See infra* Part V.A.2.
7. *See infra* Part V.A.3.
8. *See infra* Part V.A.4.
9. *See infra* Part V.A.5.
10. *See infra* Part V.B.
11. *See infra* Part V.C.
12. The purpose of an engineering and development contract is to mature necessary technologies and finalize the design of a system so as to demonstrate the capability of the platform and allow management of the platform's lifecycle costs. Defense Acquisition University, Defense Acquisition Guidebook 256–57 (2012) [hereinafter Defense Acquisition Guidebook].
13. McDonnell Douglas Corp. v. United States, 35 Fed. Cl. 358, 361 (1996), *rev'd,* 182 F.3d 1319 (Fed. Cir. 1999).
14. A fixed-price agreement is a contract in which the government agrees to pay a government contractor a set amount regardless of the contractor's costs. Defense Acquisition Guidebook, *supra* note 12, at 1210.
15. *McDonnell Douglas Corp.*, 35 Fed. Cl. at 361–62.
16. *Id.* at 362.
17. *Id.*
18. *Id.*

Early in the development process, General Dynamics and McDonnell Douglas encountered difficulties in designing and manufacturing the A-12 aircraft.[19] The contractors failed to deliver their first aircraft on time in June 1990.[20] On August 17, after subsequent negotiations to restructure the schedule of the contract failed to reach a solution, the Navy unilaterally modified the contract to set a first fly date[21] of December 31, 1991.[22] The Navy made its installment payment of $185 million in early November 1990.[23]

Following a Major Aircraft Review study,[24] the Navy's support for the A-12 program halted abruptly.[25] On December 14, 1990, Secretary of Defense Cheney issued a show cause memorandum to the Navy, directing the Navy to justify, by January 4, 1991, why the Department of Defense (DoD) should not terminate the A-12 program.[26] On December 17, the Navy issued a cure notice[27] to the contractors.[28] Shortly thereafter, the Office of the Secretary of Defense assumed control of the determination of whether to continue the program.[29] Over the weekend of January 5–6, 1991, the Office of the Secretary of Defense withdrew support for the A-12 program and refused to provide further funds for the program.[30] The next day, the Navy's Contracting Officer terminated the A-12 contract for contractor default.[31]

19. *Id.*

20. *Id.*

21. The first flight date of an aircraft is the date by which a working model of the aircraft must be proven operational. *See* Defense Acquisition Guidebook, *supra* note 12, at 74–75.

22. *McDonnell Douglas Corp.*, 35 Fed. Cl. at 362.

23. *Id.* at 363.

24. The Secretary of Defense specifically directed this additional program study to determine whether the end of the Cold War would impact the need for A-12 aircraft. U.S. Accounting Office, GAO/NSIAD-92-190FS, Naval Aviation: Events Surrounding the Navy's A-12 Aircraft Program 4 (1992).

25. *McDonnell Douglas Corp.*, 35 Fed. Cl. at 365–68.

26. *Id.* at 364.

27. A cure notice is a government issued delinquency notice stipulating that a contractor's performance is so deficient that the government may terminate the contract for default if the contractor does not cure the deficiency in the time stipulated by the notice. 48 C.F.R. § 49.607 (2011).

28. *McDonnell Douglas Corp.*, 35 Fed. Cl. at 364.

29. *Id.* at 365.

30. *Id.* at 365–66.

31. *Id.* at 367–68. Under the Contract Disputes Act, a contractor must submit a contract claim against the federal government to the contract's Contracting Officer for a decision. 41 U.S.C. § 7103(a) (Supp. V. 2012). The Contracting Officer must issue a written decision, which must include the Contracting Officer's reasons for making its determination. 41 U.S.C. § 7103(d)–(e). The Contracting Officer's decision is "final and conclusive . . . unless an appeal or action is timely commenced as authorized by this chapter." 41 U.S.C. § 7103(g). The Contracting Officer may terminate a contract for government convenience or contractor default. The government may terminate a contract for convenience, in effect cancelling the contract and limiting the government's obligation to the contractor for work completed, if the contractor fails to perform the contract and does not cure such failure within 10 days of receipt of a notice from the Contracting Officer specifying the failure. 48 C.F.R. § 52.249–9 (2011). The government may, whenever the Contracting Officer determines that a termination is in the best interest of the government, terminate a contract for convenience. 48 C.F.R. § 52.249–2 (2011). When a termination for convenience occurs, the government is obligated to fulfill all contractual obligations agreed to in the contract's default provisions. *See* 48 C.F.R. § 52.249–2 (2011).

By the date of contract termination, General Dynamics and McDonnell Douglas had spent $3.88 billion attempting to develop the A-12 while the Government had provided $2.68 billion in progress payments.[32] On February 5, 1991, the Navy sent McDonnell Douglas and General Dynamics a letter demanding the return of approximately $1.35 billion in progress payments for default of the contract.[33] On that same day, the defense contractors entered into a deferred payment agreement.[34] Under the terms of that agreement, the contractors acknowledged the government's demand but the government agreed to defer collection pending court action.[35]

On June 7, 1991, the defense contractors filed suit in Federal Claims Court under the Contract Disputes Act[36] requesting that the court, inter alia, convert the termination for default into one for convenience.[37]

At trial, the Plaintiffs asserted that the government had breached its duty under the "superior knowledge" doctrine.[38] Discovery of Plaintiffs' superior knowledge claim required access to two classified stealth aircraft programs, the Air Force's B-2 and F-117A programs.[39] During the discovery process in March 1993, the acting-Secretary of the Air Force, General Merrill McPeak, asserted the government had a right to call upon the state secrets privilege given the nature of the inquiry.[40] Despite this warning, state secrets were revealed during two separate depositions in March and July of 1993.[41] Shortly thereafter, the Acting Secretary of the Air Force filed a declaration formally invoking the state secrets privilege.[42] The court found that the government had properly raised its state secrets privilege, and held that the court could not resolve the merits of the case and that further inquiry was needed to determine whether Plaintiffs' claim should be dismissed.[43]

The Court of Federal Claims issued an order, based upon further factual inquiry, that the contract was terminated at the convenience of the Department of Defense,

32. Gen. Dynamics Corp. v. United States, 131 S. Ct. 1900, 1903 (2011).

33. McDonnell Douglas Corp. v. United States, 25 Cl. Ct. 342, 345 (1992).

34. *Id.*

35. *Id.* at 349.

36. 41 U.S.C. §§ 7101–7109 (Supp. V. 2012).

37. *McDonnell Douglas Corp.*, 25 Cl. Ct. at 346. In full, Plaintiffs requested "(1) grant plaintiffs' December 31, 1990 equitable adjustment requests, (2) convert the termination for default to one for convenience, (3) deny defendant's demand for return of progress payments, (4) award performance costs and reasonable profit, (5) award settlement expenses, and (6) award damages for breach of contract." *Id.* In this instance, the conversion of contract termination for default to convenience would have resulted in plaintiffs receiving $1.2 billion from the government instead of plaintiffs owing the government $1.35 billion. *Gen. Dynamics Corp.*, 131 S. Ct. at 1903–05.

38. McDonnell Douglas Corp. v. United States, 29 Fed. Cl. 791, 791 (1993). The superior knowledge doctrine is an affirmative defense a contractor can assert against the government under specific circumstances. *See infra* Part III.A.

39. *McDonnell Douglas Corp.*, 29 Fed. Cl. at 795.

40. *Id.* at 794–95.

41. *Gen. Dynamics Corp.*, 131 S. Ct. at 1904.

42. *McDonnell Douglas Corp.*, 29 Fed. Cl. at 794–95.

43. *Id.* at 795.

and thus vacated the determination that the cause of termination was contractor default.[44] The court reasoned that the Navy had not provided evidence that it was displeased with the contractor's performance, which was necessary to justify the contract termination for default.[45] Subsequently, the Court of Federal Claims determined that the contract was cancelled at the convenience of the government,[46] holding that that the DoD failed to exercise reasonable discretion when terminating the contract, but instead relied upon a technical default as a pretext.[47]

A new trial was then held in order to determine the damages incurred by the DoD for terminating the contract at their convenience. The Federal Claims Court concluded that the government properly invoked its state secrets privilege and, given the circumstances of the case, the Plaintiffs' superior knowledge could not be litigated.[48] The Federal Claims Court determined that the issue was nonjusticiable because "numerous layers of potentially dispositive facts" were hidden by the privilege and, as a result, any adjudication of the matter would be a "sham" trial.[49] The court acknowledged that even a sham trial may pose a danger to national security.[50] Hence, the court determined that Plaintiffs' damages were limited to incurred and allowable costs plus interest.[51]

The Court of Federal Claims held, inter alia, that the court would assume the role of Contracting Officer in order to issue a final judgment, as opposed to remanding to the Navy's Contracting Officer.[52] At a subsequent trial, the Court of Federal Claims resolved that contractors and subcontractors were entitled to settlements that were "reasonable, allocable, and allowable" under the contract.[53] Remedy may include "incurred costs, profit or loss adjustment, and the subcontractor's settlement expenses."[54] The court determined that Plaintiffs' reasonable, allocable and allowable costs were approximately $3.878 billion, but, since the contractors had already received $2.678 billion in payments, Plaintiffs were due only $1.200 billion plus statutory interest on that sum from June 26, 1991 until paid.[55]

The Court of Appeals for the Federal Circuit held that the trial court erred when it determined that the government's decision to terminate the contract was unrelat-

44. McDonnell Douglas Corp. v. United States, No. 91-1204C, 1994 WL 715992, at *1 (Fed. Cl. Dec. 9, 1994).

45. *Id.*

46. McDonnell Douglas Corp. v. United States, 35 Fed. Cl. 358, 361 (1996).

47. *Id.* at 372–73.

48. McDonnell Douglas Corp. v. United States, 37 Fed. Cl. 270, 284–85 (1996).

49. *Id.*

50. *Id.* at 281–82.

51. *Id.* at 272.

52. *Id.* at 295.

53. McDonnell Douglas Corp. v. United States, 40 Fed. Cl. 529, 537 (1998), *vacated*, 182 F.3d 1319 (Fed. Cir. 1999).

54. *Id.*

55. *Id.* at 555–56.

ed to the Plaintiffs' ability to fulfill their obligations under the contract.[56] The court vacated the trial court's decision and remanded for a determination of whether the need to protect military secrets precluded discovery into the superior knowledge issue.[57] Upon remand, the Court of Federal Claims reaffirmed its earlier decision that the government properly invoked the state secrets privilege and that doing so invalidated the Plaintiffs' claim of superior knowledge.[58]

On appeal, the Court of Appeals for the Federal Circuit affirmed that the state secrets privilege was correctly invoked and that the privilege prevented adjudicating whether the Government's superior knowledge excused the contract default.[59] The Court of Appeals relied upon *United States v. Reynolds*,[60] which held that the defendant-government may invoke the state secrets privilege to prevent a plaintiff from discovering confidential information without having to abandon a legal defense dependent upon concealed information.[61] The Court of Appeals for the Federal Circuit remanded on other grounds, however.[62] Upon remand, the Court of Federal Claims held that the Contracting Officer had reasonably terminated the contract for default by the defense companies.[63] The Court of Appeals for the Federal Circuit affirmed.[64]

On September 28, 2010, the Supreme Court of the United States granted certiorari[65] to consider "what remedy is proper when, to protect state secrets, a court dismisses a Government contractor's prima facie valid affirmative defense to the Government's allegations of contractual breach."[66]

III. Legal Background

The holding of the *General Dynamics* case rests upon the legal background of the superior knowledge doctrine, the state secrets privilege, and the appropriate remedy when the state secrets privilege is properly invoked.

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56. McDonnell Douglas Corp. v. United States, 182 F.3d 1319, 1326–27 (Fed. Cir. 1999).

57. *Id.* at 1329–30. The Supreme Court of the United States denied the defense contractors' petition for writ of certiorari. McDonnell Douglas Corp. v. United States, 529 U.S. 1097, 1097 (2000).

58. McDonnell Douglas Corp. v. United States, 50 Fed. Cl. 311, 324–25 (2001), *aff'd in part, vacated in part*, 323 F.3d 1006 (Fed. Cir. 2003).

59. McDonnell Douglas Corp. v. United States, 323 F.3d 1006, 1024 (Fed. Cir. 2003).

60. 345 U.S. 1, 12 (1953) (holding that the state secrets privilege exempted the government from releasing a classified accident report to the widows of Air Force pilots killed in a test of a secret aircraft).

61. *McDonnell Douglas Corp.*, 323 F.3d at 1023.

62. *Id.* at 1010.

63. McDonnell Douglas Corp. v. United States, 76 Fed. Cl. 385, 437–38 (2007), *aff'd,* 567 F.3d 1340 (Fed. Cir. 2009), *vacated and remanded sub nom.* Gen. Dynamics Corp. v. United States, 131 S. Ct. 1900 (2011).

64. McDonnell Douglas Corp. v. United States, 567 F.3d 1340, 1342 (Fed. Cir. 2009), *vacated and remanded sub nom. Gen. Dynamics Corp.*, 131 S. Ct. 1900.

65. Gen. Dynamics Corp. v. United States, 131 S. Ct. 62, 62 (2010). The case was consolidated with Boeing Co. v. United States, 131 S. Ct. 62 (2010). *Id.*

66. *Gen. Dynamics Corp.*, 131 S. Ct. at 1903.

A. Superior Knowledge Doctrine

The superior knowledge doctrine permits a contractor, under limited circumstances, to assert that the government has breached a contract by not revealing information necessary for the contractor to perform the requirements of the contract.[67] To prove a breach under the superior knowledge doctrine, a contractor must produce specific evidence that it:

> *(1) undert[ook] to perform without vital knowledge of a fact that affects performance costs or direction[,]*
>
> *(2) the government was aware the contractor had no knowledge of and had no reason to obtain such information[,]*
>
> *(3) any contract specification supplied misled the contractor, or did not put it on notice to inquire[,] and*
>
> *(4) the government failed to provide the relevant information.*[68]

A contractor must prove each element to prevail on a superior knowledge doctrine claim.[69] For example, in *Helene Curtis Indus., Inc. v. United States*, a court held that the government violated the superior knowledge doctrine when the government awarded a contractor a contract to produce a disinfectant following a competitive bid process.[70] Specifically, the government failed to inform the contractor that contractual performance required the grinding of specific ingredients to produce a suitable product; the government had researched the disinfectant, which had never been mass-produced before; the government did not inform the bidders of the necessity of grinding the ingredient; and, by not grinding the ingredient, the contractor suffered financial loss when its product did not meet contractual specifications.[71]

The government, however, will not be held liable for failing to provide information to a contractor that is "readily available" from a different source.[72] For instance, in *Bradley Const., Inc. v. United States*, the Court of Federal Claims held that the federal government had not breached the superior knowledge doctrine when its contract did not stipulate that the contractor would incur additional costs for oper-

67. GAF Corp. v. United States, 932 F.2d 947, 949 (1991).
68. *Id.* (citing Lopez v. A.C. & S. Inc., 858 F.2d 712, 717 (Fed. Cir. 1988)).
69. *See id.*
70. 312 F.2d 774, 778 (Ct. Cl. 1963).
71. *Id.*
72. Petrochem Services, Inc. v. United States, 837 F.2d 1076, 1079 (Fed. Cir. 1988).

ating in Indian Tribe Territory because the additional fees were required by public law.[73]

At present, no "compartmentalized" programs exception to the superior knowledge doctrine exists.[74] In other words, the government cannot claim that it is exempt from revealing information relating to a classified program when a contractor has brought a claim regarding a different but related program on the sole basis that the information from the first program is classified.[75] Because the government's security burden does not excuse it "from liability if it breaches an independent duty to reveal information,"[76] a contractor is also able to invoke the state secrets privilege in its attempt to prove the government breached its duty to reveal superior knowledge.

B. State Secrets Privilege and the Contracting Context

The state secrets privilege in the contracting context has not significantly changed in the almost six decades since the landmark *United States v. Reynolds*[77] decision, despite the privilege's increased invocation since the end of the Cold War.[78] For example, the Supreme Court of the United States has only handled one other case regarding the issue of the state secrets privilege in a contractual dispute, *Tenet v. Doe*,[79] in which the Court simply reaffirmed its 1875 *Totten v. United States*[80] holding. Limited case law on the subject exists, at least in part, as lower courts have presumably sealed a number of cases on the narrow issue.[81]

The state secrets privilege is a well-established exception to the rules of discovery, which permits the government to prevent disclosure of certain information pursuant to trial.[82] The government may invoke the state secrets privilege whenever the "Government has a compelling interest in protecting . . . the secrecy of information important to our national security."[83] In *Northrop Corp. v. McDonnell Douglas*

73. 30 Fed. Cl. 507, 510–11 (1994).

74. Northrop Grumman Corp., Military Aircraft Div. v. United States, 63 Fed. Cl. 12, 17–18 (2004).

75. *Id.*

76. *Id.* at 18.

77. 345 U.S. 1 (1953).

78. Jason A. Crook, *From the Civil War to the War on Terror: The Evolution and Application of the State Secrets Privilege*, 72 ALB. L. REV. 57, 63–66 (2009).

79. 544 U.S. 1, 11 (2005).

80. 92 U.S. 105, 107 (1875).

81. Laura K. Donohue, *The Shadow of State Secrets*, 159 U. PA. L. REV. 77, 79–82 (2010) (discussing difficulties in attempting to understand the use and scope of the state secrets privilege because academic literature relies upon published opinions, which represent only a small portion of instances where the state secrets privilege affects the outcome of the case).

82. *Reynolds*, 345 U.S. at 6–7. The Federal Rules of Civil Procedure provide that, with exceptions, parties "may obtain discovery regarding any nonprivileged matter that is relevant to any party's claim or defense." FED. R. CIV. P. 26(b)(1). The government's privilege to conceal information dates back to at least 1827. Martin v. Mott, 25 U.S. 19, 30–31 (1827).

83. Snepp v. United States, 444 U.S. 507, 509 n.3 (1980) (per curiam).

Corp., the court held that the government properly invoked its state secrets privilege when the defense contractors in a civil suit subpoenaed certain government documents related to sales of military equipment to foreign governments.[84]

United States v. Reynolds[85] is the "leading decision" on the state secrets privilege to prevent discovery.[86] In *Reynolds*, three civilian contractors died when a B-29 aircraft crashed during an Air Force test of secret electronic equipment.[87] During pretrial, the wives of the deceased civilian contractors sought to produce the Air Force's official accident investigation report.[88] The Secretary of the Air Force objected to revealing such information on national security grounds.[89] The Supreme Court held that the government has a state secrets privilege to discovery, but that the appropriate court must determine whether the government's claim of privilege is valid.[90] In *Reynolds*, the Supreme Court determined that the government properly invoked its state secrets privilege and thus precluded plaintiffs from discovery of privileged information.[91] However, the Supreme Court noted that the state secrets privilege was an evidentiary privilege, and as such its invocation did not necessitate the cessation of litigation.[92]

Today, despite limited case law, the operation of the state secrets privilege is well understood. The state secrets privilege is a common law evidentiary privilege available only under limited circumstances.[93] Only the government may assert the state secrets privilege.[94] To invoke the state secrets privilege, the government must affirmatively assert the privilege; this right cannot be waived.[95] To assert the state secrets privilege, the head of the relevant government department must issue a formal claim of the privilege after "actual personal consideration" of the matter.[96]

The court determines whether the government's claim of privilege is valid.[97] When undertaking its analysis, a court must not reveal the information the privilege is designed to protect.[98] Courts are forbidden from maintaining any trial that will

84. 751 F.2d 395, 402 (D.C. Cir. 1984).
85. 345 U.S. 1.
86. El-Masri v. United States, 479 F.3d 296, 302 (4th Cir. 2007).
87. *Reynolds*, 345 U.S. at 3.
88. *Id.*
89. *Id.* at 4.
90. *Id.* at 6–8.
91. *Id.* at 10–11.
92. *Id.* at 12.
93. *Id.* at 7–8.
94. *Id* at 7.
95. *Id.*
96. *Id.* at 7–8; *see also* Crater Corp. v. Lucent Technologies, Inc., 423 F.3d 1260, 1266 (Fed. Cir. 2005) (holding that "actual personal consideration" was satisfied when a senior officer was informed of a potential state secrets privilege issue and made the ultimate policy determination).
97. *Reynolds*, 345 U.S. 1 at 8.
98. *Id.*

inevitably disclose privileged information.[99] This rule is "designed not merely to defeat the asserted claims, but to preclude judicial inquiry."[100] For example, in *Guong v. United States*, the Court of Appeals for the Federal Circuit held that the state secrets privilege did not require the government to reveal if the plaintiff was a former employee when plaintiff brought a breach of employment contract claim against the Central Intelligence Agency.[101]

As the state secrets privilege is an evidentiary privilege, its invocation does not alter the basic tenets of interpretation of government contracts. Interpretation of government contracts — including remedies — is normally governed by contract law, unless a statutory exception exists.[102] The Contracts Dispute Act, the relevant part presently codified as 41 U.S.C. § 7103, governs the government contracting disputes process.[103]

Under 41 U.S.C. § 7103, a government contractor must submit a contract claim against the federal government to the Contracting Officer for a decision.[104] The Contracting Officer must issue a written decision that is furnished to the contractor,[105] and the decision must state the Contracting Officer's reasons for his or her decision — although no specific findings of fact are required.[106] The Contracting Officer's decision on a claim is "final and conclusive . . . unless an appeal or action is timely commenced."[107] The Federal Acquisition Regulations System,[108] and in pertinent part the Defense Acquisition Regulations System,[109] details how remedy damages are to be calculated.[110]

Under general contracts common law, "a party has no claim in restitution for performance that he has rendered under or in return for a promise that is unenforceable on grounds of public policy unless denial of restitution would cause dis-

99. Totten v. United States, 92 U.S. 105, 107 (1875).

100. Tenet v. Doe, 544 U.S. 1, 6–7 n.4 (2005).

101. 860 F.2d 1063, 1066–67 (Fed. Cir. 1988).

102. *See* Franconia Associates v. United States, 536 U.S. 129, 141 (2002); Priebe & Sons v. United States, 332 U.S. 407, 411 (1947).

103. *See* Contracts Dispute Act of 1978, Pub. L. No. 95–563, 92 Stat. 2383 (1978), Section 6(b); 41 U.S.C. § 7103 (Supp. V. 2012).

104. 41 U.S.C. § 7103(a).

105. 41 U.S.C. § 7103(d).

106. 41 U.S.C. § 7103(e).

107. 41 U.S.C. § 7103(g). The language of the statute is substantially the same as when it was first codified. *Compare* Contracts Dispute Act of 1978, Pub. L. No. 95-563, § 6(b), 92 Stat. 2383, 2384–85 (1978), *with* 41 U.S.C. § 7103(g). The Contracts Dispute Act of 1978 was specifically enacted to enhance the government's bargaining position. S. REP. NO. 95–1118, at 1 (1978).

108. 48 C.F.R. tit. 28 (2011) (Federal Acquisition Regulations System).

109. 48 C.F.R. §§ 201–253 (2011) (Defense Acquisition Regulations System).

110. For sections relevant to termination of a fixed-price contract, see 48 C.F.R. § 52.249–2 (2011) (Termination for Convenience of the Government (Fixed-Price)); 48 C.F.R. § 52.249–9 (2011) (Default (Fixed-Price Research and Development)).

proportionate forfeiture."[111] If a court is unable to enforce a contract due to a public policy exception, the court's remedy is to leave the parties as it found them.[112]

IV. The Court's Reasoning

In *General Dynamics*, the Supreme Court unanimously held that the parties are to be left as the court found them when the government properly invokes its state secrets privilege and, as a result, the government is unable to adequately respond to a contractor's prima facie valid superior knowledge claim.[113]

As a preliminary matter, the Court assumed two prior findings by the Court of Appeals for the Federal Circuit and the Courts of Federal Claims.[114] First, government contractors properly raised the superior knowledge defense to the government's assertion that the contractor breached the contract.[115] Second, the government validly invoked its state secrets privilege, thereby preventing further discovery of particular information.[116]

The Court made four key determinations as well as an important conclusion in dicta. The Court first determined that the appropriate remedy is governed by contract common law.[117] Second, the Court reasoned that, under the circumstances, neither party could obtain judicial relief.[118] Third, the Court concluded that under contract common law, when neither party may obtain judicial relief, the appropriate remedy is for the court to leave the parties as it found them.[119] Fourth, the Court determined that the position of the parties when they filed suit was the actual possession of funds and property of the parties at the time the suit was filed, instead of the legal obligations of the parties at the time the suit was filed.[120] Finally, in dicta, the Court asserted that the purpose of the holding was to provide incentive for parties to contract around future situations where the government would invoke its state secrets privilege.[121]

111. Restatement (Second) of Contracts § 197 (1981).

112. *Id.* at cmt. a ("In general, if a court will not, on grounds of public policy, aid a promisee by enforcing the promise, it will not aid him by granting him restitution for performance that he has rendered in return for the unenforceable promise. Neither will it aid the promisor by allowing a claim in restitution for performance that he has rendered under the unenforceable promise. It will simply leave both parties as it finds them, even though this may result in one of them retaining a benefit that he has received as a result of the transaction."). The Court's interpretation of "as it finds them" is one of the principle holdings of *General Dynamics*. *See infra* Part IV.

113. Gen. Dynamics Corp. v. United States, 131 S. Ct. 1900, 1906 (2011). Justice Scalia wrote the opinion for the unanimous majority. *Id.* at 1903.

114. *See id.* at 1904–06.

115. *See id.*

116. *See id.*

117. *Id.* at 1906.

118. *Id.* at 1907.

119. *Id.*

120. *Id.* at 1908.

121. *Id.* at 1909–10.

First, the Court reasoned that the appropriate remedy in such a case is determined by contract common law instead of by the state secrets privilege.[122] The Court determined that the lower courts had improperly relied upon *United States v. Reynolds*.[123] The Court differentiated between *Reynolds* and the present case by noting that *Reynolds* "decided a purely evidentiary dispute by applying evidentiary rules," whereas in the present case the lower court had "decreed the substantive result" even though the contractors were able to establish a prima facie case.[124]

Second, the Court reasoned that "[w]here liability depends upon the validity of a plausible superior-knowledge defense, and when full litigation of that defense [would lead to disclosure of state secrets], neither party can obtain judicial relief."[125] The Court agreed with the lower court's legal and factual determinations, specifically noting that prior disclosures of state secrets had already taken place and further disclosures might result if discovery were to continue.[126] However, the Court disagreed with the lower courts application of the legal determination.[127] The Court reasoned that because "[i]t is claims and defenses *together* that establish [justification for] judicial relief . . . when public policy precludes judicial intervention for the one it should preclude judicial intervention for the other as well," allowing the claim to proceed would provide a windfall to one litigant.[128]

Third, the Court determined that the appropriate remedy when neither party may obtain judicial relief was to follow the common law, which is for the court to "leave both parties as it finds them."[129] The concern of the Court was to ensure that neither litigant gained an unfair advantage from the necessary exclusion of information due to invocation of the state secrets privilege, despite the claim being nonjusticiable.[130] The Court further reasoned that the Statute of Frauds[131] supported its

122. *Id.* at 1906.

123. *Id. See* United States v. Reynolds, 345 U.S. 1, 12 (1953) (holding defendant-government may invoke the state secrets privilege to prevent the plaintiff from discovering confidential information without having to abandon a legal defense dependent upon concealed information, when widows of Air Force pilots killed in a testing of a secret aircraft sought an accident report).

124. *Gen. Dynamics Corp.*, 131 S. Ct. at 1906.

125. *Id.* at 1907.

126. *Id.*

127. *Id.*

128. *Id.* (emphasis in original).

129. *Id.*

130. *Id.* at 1907–08 (citing RESTATEMENT (SECOND) OF CONTRACTS § 197 cmt. (a) (1981) ("In general, if a court will not, on grounds of public policy, aid a promisee by enforcing the promise, it will not aid him by granting him restitution for performance that he has rendered in return for the unenforceable promise. Neither will it aid the promisor by allowing a claim in restitution for performance that he has rendered under the unenforceable promise. It will simply leave both parties as it finds them, even though this may result in one of them retaining a benefit that he has received as a result of the transaction.")).

131. The Statute of Frauds is a common law doctrine that requires a written instrument for certain agreements so as to "prevent 'contracts' from being falsely sworn upon those who had never assented to them." 1 HAWKLAND UCC SERIES § 2-201:1 (quotes in original). The Statute of Frauds is separate from government contracting fraud or abuse claims, none of which were raised in *General Dynamics*. *See supra* Part II. For a discus-

view, as it "assumes a valid, enforceable agreement between the parties but nevertheless leaves them without a remedy absent reliable evidence" due to fear of possible injustice.[132] In other words, the Court reasoned that although the government has the right to invoke its state secrets privilege, it will not be rewarded for doing so.[133] The Court concluded that since the contractors were able to present a prima facie case and the government could not provide a defense because it invoked the state secrets privilege, it would be unfair to presume that the government should win the claim by default.[134]

Fourth, the Court determined that the "position of the parties" at the time the suit was filed was "not their position with regard to legal burdens and the legal consequences of contract-related determinations, but with regard to possession of funds and property."[135] The Court first reasoned that, although it did not hold a view on the merits of the issue, because the issue was nonjusticiable, equitable concerns mandated that the government not unduly benefit from an unfair default rule.[136] The Court determined that it would be impossible to calculate damages from the contract termination, given that the information necessary to make such a determination was privileged.[137] The Court believed that it was obligated to enforce what the "*ex ante* expectations of the parties were or reasonably ought to have been."[138] However, because both parties must have understood that "state secrets would prevent courts from resolving many possible disputes" under the contract, the parties assumed the risk of the courts being unable to enforce the contract.[139] The Court concluded that since the parties wholly assumed the risk of an unenforceable contract, and because the court did not have a knowledgeable basis to correct the issue, the parties were to be left in the position with regard to possession of funds and property at the time of the start of litigation.[140]

The Court explained that its holding did not include the Contracting Officer's determination of fault.[141] The Court reasoned that the Contracting Officer's verdict

sion of government contracting fraud or abuse claims, see generally Jeffrey L. Handwerker et. al., *Congress Declares Checkmate: How the Fraud Enforcement and Recovery Act of 2009 Strengthens the Civil False Claims Act and Counters the Courts*, 5 J. Bus. & Tech. L. 295 (2010).

132. *Gen. Dynamics Corp.*, 131 S. Ct. at 1908.

133. *Id.* at 1907–08.

134. *Id.* at 1906.

135. *Id.* at 1908.

136. *See id.*

137. *Id.* Because the issue was nonjusticiable, the Court determined that 48 C.F.R. § 52.249–2 was not applicable when determining the costs owed by the litigants. *Id.*

138. *Id.* at 1909.

139. *Id.*

140. *See id.* at 1908.

141. *Id.* Pursuant to 41 U.S.C. § 605, since recodified as 41 U.S.C. § 7103(g), "the contracting officer's decision on a claim is final and conclusive . . . unless an appeal or action is timely commenced as authorized by this chapter." 41 U.S.C. § 7103(g) (Supp. V. 2012). In *Gen. Dynamics Corp.*, if the Contracting Officer's determina-

was not binding because that decision was "merely one step in the contractual regime to which the parties had agreed," and as such would not be a final decision if litigation was pursued.[142]

The Court determined that the position of the parties at the time of the start of litigation was that the contractor had spent $3.88 billion and the government had paid $2.68 billion.[143] Given that the parties were left as they stood at the time of litigation, the parties did not owe obligations to one another.[144]

Finally, in dicta, the Court asserted that the purpose of the holding was to provide incentive for parties to contract around future situations where the government would invoke its state secrets privilege.[145] The Court believed that it attained this goal by rendering the "law more predictable and hence more subject to accommodation by contracting parties."[146] Specifically, the Court explained that the purpose of the opinion was to provide greater incentive for the government and government contractors to contract around similar types of situations in the future.[147] In response to the government's concern that a new legal standard would give litigants incentive to file frivolous superior knowledge defense claims, the Court characterized such fears as "misplaced."[148] The Court reasoned so because it believed that (1) the holding would only apply in a very narrow set of circumstances, where the contractor is able to present a prima facie case despite the government's valid use of its state secrets privilege, (2) defense contractors have incentive not to abuse the system since they are repeat employees, and (3) further legal refinement could remedy issues that would arise.[149] The Court concluded that courts should be hesitant to invoke this holding, given that it is the "option of last resort, available in a very narrow set of circumstances."[150]

The Court vacated the judgment of the Court of Appeals for the Federal Circuit and remanded.[151]

V. Analysis

In *General Dynamics v. United States*, the Supreme Court held that the parties are to be left as the court found them when the government properly invokes its state se-

tion that the contractor had defaulted was upheld, the contractor would have been required to repay the government $1.35 billion. *See* 131 S. Ct. at 1903–04.

142. *Gen. Dynamics Corp.*, 131 S. Ct. at 1908.
143. *Id.* at 1903.
144. *Id.* at 1909.
145. *Id.* at 1909–10.
146. *Id.* at 1909.
147. *Id.*
148. *Id.*
149. *Id.*
150. *Id.* at 1910.
151. *Id.*

crets privilege and, as a result, the government is unable to adequately respond to a contractor's prima facie valid superior knowledge claim.[152] Although the Court's holding appears to be a practical solution to reduce litigation involving the state secrets privilege, it is likely to lead to more litigation over the state secrets privilege.[153] Moreover, given that the Court determined the claim was nonjusticiable, the Court should have dismissed the claim, as opposed to issuing a holding that changed precedent.[154] Instead, the Court should have affirmed the Court of Federal Claims ruling that the appropriate remedy under the circumstances was to leave the parties as they were when litigation commenced — bound by the contractual agreement that the Contracting Officer's determination would be binding unless an appropriate court adjudicated otherwise.[155] To remedy the current situation, Congress should pass legislation to restore the prior precedent that relied upon the Contracting Officer's determination.[156]

This analysis section posits that the Court's holding and purpose that the Court used to justify that holding appear to be at odds.[157] The Court states its desire to reduce litigation over the state secrets privilege.[158] However, the Court's holding will likely increase litigation over the state secrets privilege because the holding, along with changes in the defense industrial market, raise the government's expected value for litigating defense acquisition claims.[159] The Court's holding — to leave the parties as they were with regard to the actual possession of funds and property of the parties at the time the suit was filed when a claim is nonjusticiable due to the invocation of the state secrets privilege under specific circumstances — is unlikely to result in decreased use of the state secrets privilege for two reasons.[160] First, the holding discourages the government from contracting around the state secrets privilege because current circumstances indicate that the DoD will very likely be able to invoke the state secrets privilege and, even if a defense contractor could provide evidence of a prima facie valid superior knowledge claim despite that privilege, the DoD — because of the habitual overruns in defense contracting — will likely be able to present enough evidence to render the claim nonjusticiable.[161] Second, the holding will likely fail to undermine the incentive of defense contractors to litigate because their expected values of litigation will still be high, even though they are less likely to succeed.[162] Overall, it is likely that the Court's holding establishes a new sta-

152. *Id.* at 1906.
153. *See infra* Part V.A.
154. *See infra* Part V.B.
155. *See infra* Part V.B.
156. *See infra* Part V.C.
157. *See infra* Part V.A.1.
158. *See infra* Part V.A.1.
159. *See infra* Part V.A.1.
160. *See infra* Part V.A.
161. *See infra* Parts V.A.2–3.
162. *See infra* Part V.A.4.

tus quo that provides strong incentive for the DoD to litigate certain claims but fails to undermine the incentive of defense contractors to litigate, thereby increasing instances of litigation.[163]

A. Although the Court's Holding, on Its Face, Appears to Be a Practical Way to Reduce Litigation Involving the State Secrets Privilege, It Is Likely to Lead to More Litigation over the State Secrets Privilege

The Court's stated purpose in *General Dynamics* is to ensure that privileged state secrets are not revealed through discovery at trial.[164] The Court believes that it achieved its goal by holding that the contracting parties assume the risk of an unenforceable contract when the parties should have reasonably foreseen the possibility of a nonjusticiable claim arising out of the government's use of its state secrets privilege.[165] By requiring the parties to assume the risk of an unenforceable contract, the Court believes that the parties will have strong incentive to contract around such foreseeable issues in the future.[166] For this reason, the Court states that the holding itself is of minor importance because it will only be applicable in very limited circumstances.[167]

On its face, the Supreme Court's logic appears sound. In situations where parties are contracting for the development of a classified military system,[168] the parties should reasonably foresee the possibility that a contract dispute could not be resolved through the courts due to the risk that litigation would reveal state secrets. Further, the Supreme Court's opinion addresses the issue in a seemingly elegant manner, by purporting to change the incentive structure of the parties to avoid litigation in the future.[169]

In contrast to the Supreme Court's expectations, however, the *General Dynamics* holding is likely to lead to more litigation over the state secrets privilege. An understanding of bargaining power and how the defense industry operates are crucial to understanding why the Supreme Court's expectations are unlikely to be met.[170] The *General Dynamics* holding provides the government with the ability and incentive to abuse its holding, does not provide the parties with sufficient incentive to contract around the issue, does not sufficiently dissuade contractors from pursuing

163. *See infra* Part V.A.

164. *See* Gen. Dynamics Corp v. United States, 131 S. Ct. 1900, 1909–10 (2011). This statement is consistent with prior precedent. *See* Totten v. United States, 92 U.S. 105, 107 (1875); United States v. Reynolds, 345 U.S. 1, 7–8 (1953).

165. *Gen. Dynamics Corp.*, 131 S. Ct. at 1909.

166. *Id.*

167. *Id.* at 1910.

168. *Id.* at 1909. As noted by the Court, even the "contract itself was a classified document at one point." *Id.*

169. *Id.*

170. *See infra* Part V.A.1.

cancelled contracts through litigation, and the Court's holding is ultimately at odds with its purpose in the present case.[171]

1. Context: Bargaining Power and How the Defense Industry Operates Today

Two concepts are important to understanding how the *General Dynamics* holding is likely to impact the defense industry: the concept of bargaining power and the current state of the defense acquisition market.

a. Bargaining Power

The first concept, bargaining power, is important to understand why, and in what ways, default rules — including both statutory rules and judicial holdings — will impact actors negotiating a contract. In short, default rules, which establish the fall back position if parties have not contracted for such a contingency, affect bargaining power, and thus outcomes, by altering the expectations and legal rights of the parties.[172]

A bargain is, in effect, a contest in which each party uses its power in an attempt to obtain a preferred outcome in a transaction.[173] In most situations, the preferred outcome is either receiving the desired product or service at the best price or otherwise capturing a greater share of the surplus generated by the transaction.[174] Depending upon the circumstances, however, a party's preferred outcome may be to not conclude a transaction — namely, when the potential cost exceeds the perceived value of the transaction.[175]

The ability to obtain one's preferred outcome is referred to as bargaining power.[176] Bargaining power is an indefinite term, but generally refers to the desire and power a party may marshal in the transaction so as to obtain the "greatest possible value from the other party at an exchange price equal to or less than their respective reserve prices."[177] Differences in bargaining power exist for a multitude of reasons.[178] Relative bargaining power depends upon the situation, but may include factors as disparate as personal preferences, information asymmetry,[179] market structure, negotiating skill, as well as legal rights and default rules.[180]

171. *See infra* Parts V.A.2–5.

172. *See* Daniel D. Barnhizer, *Inequality of Bargaining Power*, 76 U. Colo. L. Rev. 139, 169–71 (2005).

173. *Id.* at 160.

174. *Id.* at 169.

175. *See id.*

176. *Id.*

177. *Id.*

178. *Id.* at 169–72.

179. Information asymmetry refers to a situation where one party has more knowledge about a situation than the other party, and so the first party can leverage the difference in knowledge to gain a strategic advantage in the bargaining process. *See* George A. Akerlof, *The Market for "Lemons": Quality Uncertainty and the Market Mechanism*, 84 Q. J. Econ. 488, 488–90 (1970). The classic example of this situation is a customer haggling for a

Legally established default rules — determined by the legislature and judiciary — affect how contracts will be written by altering the initial bargaining position of the parties.[181] Specifically, default rules shift legal power in a way that may not have occurred but for the legally mandated default rule.[182] Default rules may be very important in that they "not only reflect the typical expectations of the parties . . . but also mold and shape them."[183] Not only are default rules likely to influence the bargaining positions of the parties, but the mere establishment of a default rule is likely to alter the substantive preferences of the contracting parties due to the status quo bias — all else being equal, contracting parties prefer the status quo to alternative positions.[184] By establishing a new default rule that alters the outcome of nonjusticiable cases from a "tie" where the Contracting Officer's determination is final to a government "win" by leaving the parties with the assets possessed at the time trial commences, *General Dynamics* has significantly increased the bargaining power of the government at the expense of the defense contractors.[185]

b. How the Defense Industry Operates Today

The second major concept necessary to properly comprehend the likely impact of the *General Dynamics* holding is to understand three vital trends in the current defense acquisition system. First, "[o]ne of the major changes taking place today in government management (federal, state, and local) is the shift *from* the government as the historic 'provider' of public services *to* the government as the 'manager of the providers' of services to the public."[186] This shift has been particularly pronounced for the Department of Defense (DoD), which has outsourced its ability to develop new weapon systems internally.[187] Reflecting this trend, the DoD lost sixty percent of its acquisition workforce — approximately 300,000 employees — between 1990 and 2006, even though the workforce's workload increased significantly due to

new car, at a point in time prior to when the customer can properly determine if the car is defective (or, a "lemon"). *Id.*

180. *See* Barnhizer, *supra* note 172, at 166, 169–72.

181. *See* Omri Ben-Shahar, *A Bargaining Power Theory of Default Rules*, 109 Colum. L. Rev. 396, 396 (2009).

182. *See* Barnhizer, *supra* note 172, at 169–71.

183. Eyal Zamir, *The Inverted Hierarchy of Contract Interpretation and Supplementation*, 97 Colum. L. Rev. 1710, 1759 (1997).

184. Russell Korobkin, *The Status Quo Bias and Contract Default Rules*, 83 Cornell L. Rev. 608, 611 (1998).

185. *See infra* Parts V.A.2–3.

186. Jacques S. Gansler, Moving Toward Market-Based Government: The Changing Role of Government as the Provider 6 (IBM Endowment for the Business of Government, 2003), *available at* http://www.businessofgovernment.org/sites/default/files/MarketBasedGovernment.pdf (emphasis and parenthesis in original).

187. Jacques S. Gansler et al., Achieving the Desired Structure of the Defense Industry in the 21st Century 51 (Naval Postgraduate Sch., Acquisition Research Program No. UMD-AM-08-125, 2008) [hereinafter Defense Industry].

post-9/11 spending.[188] Consequently, the DoD has grown increasingly reliant upon government contractors to provide needed acquisition capacity and will remain so for the foreseeable future.[189] Given the DoD's increasing reliance on contractors for acquisition services,[190] the DoD is likely to encounter a rising number of contracting issues in the near future.

Second, the defense industry has experienced significant consolidation since the end of the Cold War, shrinking from approximately fifty defense contractors to the six primary firms that operate today.[191] The defense industry undertook this consolidation at the request of the DoD, in large part due to recognition that defense budgets could not sustain the size of the industry.[192] Given defense contractors' dependence upon DoD spending, each defense acquisition contract is very important to each defense contractor.[193] In practice, defense acquisition firms have distorted incentives to bid low in order to receive initial bids that allow them to remain "locked in" when optimistic expectations are unrealized and significant cost growth occurs.[194] DoD continuously buys into the defense contractor's optimistic expectations in part because it cannot afford more consolidation or else it will lose any chance of competition for future defense acquisition projects.[195] Consequently, DoD often awards acquisition contracts to firms that promise the most performance at the lowest cost, regardless of true feasibility,[196] and so many defense acquisition contracts incur significant deficiencies that justify termination for cause.

Third, government contractors have historically experienced significant problems in developing new defense acquisition weapons, and such difficulties are likely to persist into the future.[197] Between the 1960s and the 1990s, Major Defense Acqui-

188. *Id.* at 50. In 2010, the Secretary of Defense declared that rebuilding the capacity of the acquisition workforce was a strategic priority. U.S. Government Accountability Office, GAO-12-232T, Acquisition Workforce: DOD's Efforts to Rebuild Capacity Have Shown Some Progress 1–2 (2011). However, the DoD only plans to increase the acquisition workforce by 20,000 positions by fiscal year 2015. *Id.* at 3.

189. *See* U.S. Government Accountability Office, GAO-08-572T, Defense Management: DOD Needs to Reexamine Its Extensive Reliance on Contractors and Continue to Improve Management and Oversight 1–2 (2008).

190. *See id.* at 1.

191. Defense Industry, *supra* note 187, at 15–17. The six firms are Lockheed Martin Corporation, The Boeing Company, Northrop Grumman Corporation, General Dynamics Corporation, Raytheon Company and BAE Systems Inc. *Id.* at 17.

192. See *id.* Only Boeing generates significant non-defense revenues, although defense sales represented forty-seven percent of its revenues in 2011. The Boeing Company, 2011 Annual Report ii–iii, 3 (2012).

193. Jacques S. Gansler et al., Competition in Defense Acquisitions 15 (Naval Postgraduate Sch., Acquisition Research Program No. UMD-AM-09-001, 2009) [hereinafter Competition in Defense Acquisitions].

194. *Id.*

195. *Id.* at 11–12.

196. *Id.* at 15.

197. *See* Jacques S. Gansler et al., The Effect of the Nunn-McCurdy Amendment on Unit Cost Growth of Defense Acquisition Projects viii–ix (Naval Postgraduate Sch., Acquisition Research Program No. UMD-AM-10-155, 2010) [hereinafter Nunn-McCurdy].

sition Projects (MDAPs)[198] averaged greater than fifty percent unit cost growth when compared to programs' original baselines.[199] Cost growth may have improved recently, but MDAPs currently under development are experiencing average cost growth of forty percent over the programs' original baselines.[200] Recent legislative changes,[201] along with high cost growth and a likely fall in defense spending in the near future, may result in a greater number of defense projects being cancelled. Thus, there will likely be an increasing number of defense contractors filing lawsuits in response to the cancellation of defense acquisition contracts.

Finally, DoD spending on MDAPs in the near future is likely to be significantly constrained by the stagnation or decrease in military spending along with the rise in mandatory costs such as health care[202] — trends that will likely lead to the cancelling of more defense contracts.

Overall, while DoD has become reliant upon a small number of defense contracting firms to provide it with new weapons systems, future projected budget constraints on DoD spending will likely cause more defense acquisition contracts to be cancelled. As a result, defense acquisition contracting is likely to become an increasingly contentious legal area — in part due to changes in the defense market and in part due to *General Dynamics*.

2. The General Dynamics *Holding Provides the Government with the Ability and Incentive to Terminate Most MDAP Contracts at the Fault of the Contractor*

The government could abuse the *General Dynamics* holding easily because the *General Dynamics* holding raises the government's expected value for litigating defense acquisition claims. The government has the ability to abuse the holding because the majority of MDAPs experience significant development difficulties, and every

198. Major Defense Acquisition Projects are programs that exceed either $365 million in development costs or $2,190 million in procurement costs when measured in fiscal year 2000 dollars. OBAID YOUNOSSI, ET. AL., IS WEAPON SYSTEM COST GROWTH INCREASING?: A QUANTITATIVE ASSESSMENT OF COMPLETE AND ONGOING PROGRAMS 9 (Rand Project Air Force, 2007). MDAPs represent roughly eighty percent of DoD's acquisition spending in a given year. *Id.*

199. NUNN-MCCURDY, *supra* note 197, at 9. Unit cost growth is calculated by the formula: (new baseline unit cost – original baseline unit cost) / original baseline unit cost * 100. *See id* at vi. For example, if the DoD originally estimated that the X tank would cost $1 million per tank but ultimately acquired the tank at $1.5 million per tank, X tank would have experienced unit cost growth of fifty percent over the original baseline estimate.

200. U.S. GOVERNMENT ACCOUNTABILITY OFFICE, GAO-12-400SP, DEFENSE ACQUISITIONS: ASSESSMENTS OF SELECTED WEAPON PROGRAMS 171 (2012).

201. NUNN-MCCURDY, *supra* note 197, at 23. The Nunn-McCurdy Amendment, as amended by the Major Weapons Systems Acquisition Reform Act of 2009, requires cancellation of MDAPs that exceed specified unit-cost growth metrics unless the program's costs are certified as reasonable and supported by an independent cost estimate. *Id.*

202. *See* CENTER FOR AMERICAN PROGRESS, RESTORING TRICARE: ENSURING THE LONG TERM VIABILITY OF THE MILITARY HEALTH CARE SYSTEM 1 (2011).

MDAP includes some state secrets.[203] Consequently, the government has ample opportunity to terminate a large number of MDAP contracts for fault of the contractor and reasonably rely on the state secrets privilege being properly invoked. The government also has an incentive to abuse the holding because it typically pays for development contracts in installment payments[204] that are contingent upon specified contractor performance. Thus, the government can strategically cancel programs shortly before installment payments are due in order to avoid costly losses, as shown in the *General Dynamics*[205] case.

After *General Dynamics*, the government has less to fear from litigation because it must pay the contractor for additional incurred costs only when it is both unable to invoke its state secrets privilege and loses on the merits in court.[206] In other words, the *General Dynamics* holding has changed the "tie" situation of a nonjusticiable issue being decided by a Contracting Officer — who, for various reasons, was likely to split costs — to a "win" for the government because it would not have to repay the contractor for costs incurred since the last payment date.

3. The General Dynamics *Holding Discourages the Government from Contracting Around State Secrets Issues*

The *General Dynamics* holding does not provide the parties with incentive to contract around state secrets issues in the future because government contractors do not have sufficient leverage to change the government's behavior. Under *General Dynamics*, the parties are left in the position with regard to actual possession of funds and property at the time of the start of litigation.[207] Although the Supreme Court believes this holding will provide parties incentive to contract around the potential for the state secrets privilege rendering a claim nonjusticiable,[208] the holding is unlikely to achieve the Court's goal for two reasons. First, the DoD is a monopsony[209] buyer that wields considerable market power.[210] As each government contractor is reliant almost exclusively on government contracts to survive, each individual government contractor has little power to negotiate in order to counterbalance the government's negotiating strength.[211] Second, defense contractors have strong in-

203. *See supra* Part V.A.1.a. The DoD's only countervailing interest is the desire to maintain enough firms in the defense industry to maintain at least the possibility of competition. *See supra* Part V.A.1.a.

204. The government's preferred contract type is fixed-price. 48 C.F.R. § 16.104 (2011).

205. *See* McDonnell Douglas Corp. v. United States, 35 Fed. Cl. 358, 365–66 (1996).

206. *See* Gen. Dynamics Corp. v. United States, 131 S. Ct. 1900, 1907 (2011).

207. *Id.* at 1908.

208. *Id.* at 1909.

209. A monopsony is a market in which only one buyer and more than one seller exist. Jay M. Zitter, *What Constitutes Monopsony Within Meaning of § 2 of Sherman Act*, 49 A.L.R. Fed. 2d 515 (2010).

210. Competition in Defense Acquisitions, *supra* note 193, at 11.

211. *Id.* at 5–12. A defense contractor will have to rely upon less discrete bargaining chips, namely the need for national security, the desire to preserve the defense contractor industry, and the potential release of state secrets through litigation. *See id.*

centive to negotiate terms favorable to the government to secure the first contract, or else lose the opportunity to achieve tens of billions of dollars in revenue.[212] Given the desire to reach an agreement, the contractor is unlikely to raise the state secrets privilege given the small likelihood of the event. Overall, the Supreme Court's belief that the parties will have incentive to contract around nonjusticiable claims because of the state secrets privilege is unrealistic.

4. Even Though the General Dynamics *Holding Reduces the Likelihood of Contractors Prevailing in a Contract Dispute of this Nature, the Holding is Unlikely to Reduce the Probability that Contractors Will Litigate*

Although defense contractors are less likely to prevail under the *General Dynamics* holding than under prior case law, they still have significant incentive to litigate terminated contracts. The expected value of contesting a cancelled defense contract will still almost always be worth a defense contractor's time and money because, even though the probability of success is low and the firm will incur litigation costs, the potential reward is extremely high[213] — likely a billion dollars or more. Potential rewards are even higher as the total lifecycle costs of most MDAPs runs into the tens of billions of dollars.[214] Even with a decreased probability of success after *General Dynamics*, the expected value is still likely to considerably exceed the costs and risks of litigation. Although insufficient evidence is available to make a scientific determination regarding expected value, the anecdotal evidence that a defense contractor has been willing to litigate with the government for over 20 years in hopes of retrieving one billion dollars in costs lends credence to the belief that contractors are likely to have strong incentives to continue to litigate government contracts even after the ruling of *General Dynamics*.[215]

5. The Court's Holding and Purpose that the Court Used to Justify the Holding Appear to Be at Odds in the Present Case

The Court's holding and purpose that the Court used to justify the holding appear to be at odds in the present case. The Court's holding required courts to leave the parties as they are found when the state secrets privilege prevents full judicial resolution of a dispute and asserted that the express purpose of the holding was to provide clear expectations for parties so that they could contract around such scenarios

212. *See supra* Part V.A.1.

213. *See* YOUNOSSI, *supra* note 198, at 9. This phenomenon is amplified given that only a few MDAP contracts are issued each year, making each bid process very competitive. *See* OFFICE OF THE UNDER SECRETARY OF DEFENSE (ACQUISITION RESOURCES AND ANALYSIS), SELECTED ACQUISITION REPORTS (SAR) SUMMARY TABLES AS OF DATE DECEMBER 31, 2011 2 (2012), *available at* http://www.acq.osd.mil/ara/am/sar/SST-2011-12.pdf.

214. *See generally* U.S. GOVERNMENT ACCOUNTABILITY OFFICE, GAO-12-400SP, DEFENSE ACQUISITIONS: ASSESSMENTS OF SELECTED WEAPON PROGRAMS (2012).

215. *See* Gen. Dynamics Corp. v. United States, 131 S. Ct. 1900 (2011).

in the future.[216] However, the United States Congress had already passed a rule to deal with the issue of breach of a public contract: the "contracting officer's decision on a claim is final and conclusive . . . unless an appeal or action is timely commenced as authorized by this chapter"[217] Given that the claim was dismissed,[218] the Contracting Officer's decision should have been binding.

The Supreme Court argues that this statute was not binding because the Contracting Officer's decision was "merely one step in the contractual regime to which the parties had agreed," and as such would not constitute the final decision if litigation was pursued.[219] The Supreme Court does not analyze and develop in detail, however, why the nonjusticiability of the claim rose to such a level that equitable notions necessitated a change in precedent.

Given that the nonjusticiability of an issue means that the claim is not fit for judicial determination,[220] it is not logically clear why the Contracting Officer's decision is not considered final and binding. The parties expected, or should have expected, the possibility that a judicial claim could not be resolved through the courts, and hence should have relied upon the federal rule as the default rule. Thus, the parties should have already had clear expectations regarding the outcome of a nonjusticiable claim: the Contracting Officer's determination is final unless an appropriate judicial appeal reaches a different conclusion on the merits.[221] Although the *General Dynamics* holding provides an equally bright line rule for courts to follow, it is unclear why the equitable injustice was so great so as for the Court to establish a new remedy standard.

B. The Supreme Court Should Have Affirmed the Court of Federal Claims' Ruling that Left the Parties Bound by the Contracting Officer's Determination Instead of Issuing a Decision that, in Effect, Determined the Merits of a Claim Deemed to be Nonjusticiable

Although the Court deemed that the superior knowledge issue was nonjusticiable,[222] the Court nonetheless called upon its equitable authority to issue a holding that changed the outcome of the case.[223] In other words, the Court declared that even though it did not have the authority to determine the case on the merits, it would nonetheless circumvent the merits to issue a holding that did impact the outcome.[224] The Court's attempt to claim that the holding would have an effect on the outcome

216. *Id.* at 1909.
217. 41 U.S.C. § 7103(g) (Supp. V. 2012).
218. *Gen. Dynamics Corp.*, 131 S. Ct. at 1908.
219. *Id.*
220. Black's Law Dictionary 906 (9th ed. abridged 2010).
221. 41 U.S.C. § 7103(g).
222. *Gen. Dynamics Corp.*, 131 S. Ct. at 1908–09.
223. *Id.* at 1908.
224. *See id.*

of the parties, but no affect because such was in line with *ex ante* expectations,[225] appears disingenuous.

Given that the Court determined the sole claim of the appeal was nonjusticiable,[226] the Court should not have issued a decision that implicitly determined the merits of the case. Black's law dictionary defines nonjusticiable as "not proper for judicial determination."[227] The concepts of justiciability have developed to identify appropriate instances for judicial action, acknowledging that judicial power is limited by both the Constitution and self-imposed prudential principles.[228] Specific areas recognized as nonjusticiable include "advisory opinions, feigned and collusive cases, standing, ripeness, mootness, political questions, and administrative questions."[229] Although a claim of nonjusticiability does not "wholly and immediately foreclos[e]" consideration of a matter, judicial inquiry — and judicial reach — is cut off upon a court's determination of nonjusticiability.[230] Specifically, several circuits have previously held that dismissal is the appropriate remedy when the state secrets privilege is properly invoked and continuance of the lawsuit would threaten to disclose privileged information.[231]

In the present case, the Court explicitly states the single claim of the case is nonjusticiable due to invocation of the state secrets privilege.[232] Nonetheless, the Court declares that it has the discretion, as an equity court, to issue a holding that affects the outcome of the case.[233] However, the Court does not adequately explain why its use of equitable authority was justified in a situation where it determined that the only claim in the case represented a nonjusticiable issue, aside from the argument that the Court, as an equitable court, has a duty to prevent injustice.[234] The reader is left to wonder why the Court can declare that it is unable to determine the merits of the case due to a nonjusticiable claim, but nonetheless issues a new framework[235] that will, in effect, step in for the merits to create a new regime with different results than would have occurred but for the Court's intervention.

225. *Id.* at 1909.

226. *Id.* at 1908.

227. BLACK'S LAW DICTIONARY 906 (9th ed. abridged 2010).

228. 13 FED. PRAC. & PROC. JURIS. § 3529 (3d ed.).

229. *Id.*

230. Baker v. Carr, 369 U.S. 186, 198–99 (1962).

231. Mohamed v. Jeppesen Dataplan, Inc., 614 F.3d 1070, 1083 (9th Cir. 2010) (affirming dismissal, when plaintiffs alleged torture under the Central Intelligence Agency's extraordinary rendition program); El-Masri v. United States, 479 F.3d 296, 306, 313 (4th Cir. 2007) (same); Bareford v. Gen. Dynamics Corp., 973 F.2d 1138, 1140 (5th Cir. 1992) (affirming dismissal, when plaintiffs alleged defectively manufactured and designed weapon system resulted in death and injuries).

232. *Gen. Dynamics Corp.*, 131 S. Ct. at 1908.

233. *Id.* at 1906.

234. *See id.* at 1908.

235. *See id.*

Instead, the Court should have affirmed the holding of the Court of Federal Claims, which held that the Contracting Officer's decision was final as long as that decision itself was valid.[236] Both of those holdings rested on the simple notion that the parties assumed, or reasonably should have assumed, the risk that the contract they entered into may not be enforceable due to the nature of the transaction.[237] Given that the parties assumed the risk that a court may be unable to adjudicate the claim, and that the parties understood that the Contracting Officer's decision is "final and conclusive" unless overruled by an appropriate judgment on appeal,[238] the parties expected, or should have expected, the Contracting Officer's decision to be binding.

The A-12 contract provides additional circumstantial evidence that the parties assumed the risk of a claim being deemed nonjusticiable. As noted by the Court, the agreement "authorizes a court to convert a default termination into a termination for convenience *only* if it 'determine[s] that the Contractor was not in default, or that the default was excusable.'"[239] In this case, the Court did not make such a determination.[240] Moreover, the parties had the opportunity to contract around the plausible scenario that the state secrets privilege would cause a legal claim to be nonjusticiable but chose not to do so.[241] Instead, the parties agreed, or reasonably should have assumed that they had agreed, to be bound by 41 U.S.C. § 7103, which stipulates that for all government contracts the Contracting Officer's decision on a claim is final unless judicial action determines a different outcome.[242]

C. To Remedy the Current Situation, Congress Should Pass Legislation to Restore Prior Precedent

Given the imbalance in bargaining power created by the *General Dynamics* decision, and the potential destabilizing effect upon the defense industry,[243] Congress should resolve the issue promptly via legislative reform. Specifically, Congress should amend 41 U.S.C. § 7103(g) by inserting, after the sentence ending "chapter," this

236. McDonnell Douglas Corp. v. United States, 76 Fed. Cl. 385, 388 (Fed. Cl. 2007) (holding that the Contracting Officer's determination of termination due to contractor default met the *Lisbon* standard, that "there was no reasonable likelihood that the contractor[s] could perform the entire contract effort within the time remaining for contract performance" (quoting Lisbon Contractors, Inc. v. United States, 828 F.2d 759, 765 (Fed. Cir. 1987))).

237. *Gen. Dynamics Corp.*, 131 S. Ct. at 1909.

238. 41 U.S.C. § 7103(g) (Supp. V. 2012). The language of the statute is substantially the same as when it was first codified. *Compare* Contracts Dispute Act of 1978, 95-563, § 6(b), 92 Stat. 2383, 2384–85 (1978), *with* 41 U.S.C. § 7103(g). The Contracts Dispute Act of 1978 was specifically enacted to enhance the government's bargaining position. S. Rep. No. 95–1118, at 1 (1978).

239. *Gen. Dynamics Corp.*, 131 S. Ct. at 1908 (quoting 48 C.F.R. § 52.249–9(g) (2010)) (emphasis added).

240. *See id.*

241. *See id.* at 1909.

242. *See id.* at 1908.

243. *See supra* Part V.A.

sentence: "If upon judicial review any claim is determined to be nonjusticiable, the Contracting Officer's decision on that claim is final and conclusive unless the decision was arbitrary, capricious, or without a rational basis." This legislative fix would clearly and concisely address the judicial change that the Supreme Court has created by reverting the standard to what was de facto in place before the Supreme Court ruling.[244] The amendment would thus eliminate the additional leverage granted to the government.[245] Further, the proposed amendment is narrowly tailored to address just the small number of cases wherein a government contracting case is deemed to be nonjusticiable.

VI. Conclusion

In *General Dynamics*, the Supreme Court unanimously held that a court should leave the parties as it found them when the government is unable to adequately respond to a contractor's prima facie valid superior knowledge claim because the government properly invoked its state secrets privilege.[246] Although the Court's holding, on its face, appears to be a practical solution to reduce litigation involving state secrets, the Court's opinion is likely to lead to more litigation over the state secrets privilege.[247] This expected outcome is directly contrary to the Court's stated purpose in issuing the *General Dynamics* holding.[248] Unfortunately, the Supreme Court could have achieved its desired outcome by simply affirming the holding of the Court of Federal Claims, which offered a simple solution that adhered to precedent.[249]

244. *See supra* Part V.B.
245. *See supra* Part V.B.
246. *Gen. Dynamics Corp.*, 131 S. Ct. at 1906.
247. *See supra* Part V.A.
248. *See supra* Part V.A.5.
249. *See supra* Part V.B.