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Contractor Claim

CHEROKEE NATION: MORE THAN MEETS THE EYE

Ralph C. Nash
John Cibinic
Professors Emeriti of Law, The George Washington University

The U.S. Supreme Court's decision on March 1, 2005, in Cherokee Nation of Oklahoma v. Leavitt, 125 S. Ct. 1172 (2005), 47 GC ¶ 110, may be of more interest to Government contracts practitioners than its unusual fact pattern would suggest. The case arose out of Indian Self-Determination and Education Assistance Act contracts between two Indian tribes and the Department of Health and Human Services (HHS). The Act authorizes the Government to enter into contracts in which the tribe promises to supply federally funded services, such as healthcare and education, that the Government would normally provide, and the Government agrees to pay the costs of the services as well as the tribe's "contract support costs." 25 USCA § 450j-1(a). However, the Act provides that "[n]otwithstanding any other provision of this subchapter, the provision of funds under this subchapter is subject to the availability of appropriations," and the Secretary is "not required to reduce funding for programs, projects, or activities serving a tribe to make funds available to another tribe." 25 USCA § 450j-1(b). Implementing this provision, all of the self-determination contracts incorporate a standard "availability of appropriations" clause.

The Cherokee Case

Cherokee Nation involved two cases: Thompson v. Cherokee Nation of Oklahoma, 334 F.3d 1075 (Fed. Cir. 2003), and Cherokee Nation of Oklahoma v. Thompson, 311 F.3d 1054 (10th Cir. 2002). In both cases, the HHS refused to pay the full amount promised to the tribes based on the lack of available appropriations. Although the tribes' claims were identical, there was a significant factual difference between the two cases. In the Federal Circuit case, the court found "that there were available appropriations to pay the appellee its full indirect costs, because there were no statutory caps on funding in the appropriations acts for the relevant fiscal years, and that the Secretary has not shown that full payment would require the Secretary 'to reduce funding for programs, projects, or activities serving [another] tribe.'" Accordingly, the Federal Circuit held that the HHS breached its contract by refusing to reprogram appropriations to meet its contractual obligations. By contrast, in the Tenth Circuit case, the HHS introduced an affidavit stating that all of the funds appropriated for the relevant fiscal years "was in fact spent, leaving a zero balance at the end of the year." Following the lead of three other circuits, including an earlier Federal Circuit decision in which the HHS similarly established that it had fully exhausted its lump-sum appropriation, the Tenth Circuit held that the tribes had no contractual or statutory entitlement to recover their full contract support costs (citing Shoshone-Bannock Tribes v. Secretary, 279 F.3d 660 (9th Cir. 2002), Babbitt v. Oglala Sioux Tribal Public Safety Department, 194 F.3d 1374 (Fed. Cir. 1999), and Ramah Navajo School Board Inc. v. Babbitt, 87 F.3d 1338 (D.C. Cir. 1996)).

The Supreme Court affirmed the Federal Circuit decision, reversed the Tenth Circuit decision, and remanded both cases. Curiously, the Government conceded that "were these contracts ordinary procurement contracts, its promises to pay would be legally binding," but argued, unsuccessfully, that the "the Act creates a special kind of 'self-determination contract' with a 'unique, government-to-government nature' that differentiates it from 'standard government procurement contracts.'" Consequently, the Government did not deny the following principle of appropriations law relied upon by the tribes and cited with apparent approval by the Court:

[A]s long as Congress has appropriated sufficient legally unrestricted funds to pay the contracts at issue, the Government normally cannot back out of a promise to pay on grounds of "insufficient appropriations," even if the contract uses language such as "subject to the availability of appropriations," and even if an agency's total lumpsum appropriation is insufficient to pay all the contracts the agency has made. See Ferris v. United States, 27 Ct. Cl. 542, 546 (1892) ("A contractor who is one of several persons to be paid out of an appropriation is not chargeable with knowledge of its administration, nor can his legal rights be affected or impaired by its maladministration or by its diversion, whether legal

or illegal, to other objects")....[Emphasis added.]

The Court rejected the Government's attempt to distinguish the self-determination contracts from standard Government procurement contracts, and it concluded that neither of the two phrases of the Act's "availability of appropriations" provision shielded the Government from liability.

Over Obligation

The Court agreed with the Federal Circuit that, notwithstanding the "availability of appropriations" provision, the HHS breached the contract by refusing to reprogram appropriations to meet its contractual obligations. Reprogramming is the shifting of funds within an appropriation. U.S. Government Accountability Office, PRINCIPLES OF FEDERAL APPROPRIATIONS LAW 2-30 (3d ed. 2004). The Supreme Court has held that agencies have inherent authority to reprogram funds, reasoning that "the very point of a lump-sum appropriation is to give an agency the capacity to adapt to changing circumstances and meet its statutory responsibilities in what it sees as the most effective or desirable way." Lincoln v. Vigil, 508 U.S. 182, 192 (1993). This means, for example, a contracting agency cannot use the "Availability of Funds" clause to avoid a contractual obligation as long as Congress has appropriated adequate unrestricted funds, regardless of the agency's desire to apply those funds to other purposes.

To use a simplistic hypothetical, assume an agency has a lump-sum appropriation of $200,000. The agency enters into two fixed-price contracts of $100,000 each. During performance of the first contract, there is a constructive change and the contractor requests an equitable adjustment of $50,000. If the second contractor had not yet earned the right to be paid, the agency could terminate (or partially terminate) the second contract for convenience, deobligate the funds from the second contract, and use those funds to pay the first contractor.

Over Expenditure

A more interesting hypothetical would be where the agency's contractual obligations exceed its lump-sum appropriation, and all of the contractors have earned the right to be paid and were not on notice of the over expenditure. With one exception, those were the facts presented in the Tenth Circuit case. In the Tenth Circuit case, the HHS withheld approximately 2% of its annual lump-sum appropriation for performance of its core functions and allocated the remaining 98% among the tribes. See Transcript of Oral Argument, 2004 WL 2650544, at *28 (Nov. 9, 2004). Because the tribes' contract support costs exceeded the 98% allocated, the issue was whether the HHS was required to reduce its own internal funding to meet its contractual obligations. However, because the issue arose after the end of the fiscal year, when the HHS had presumably spent the 2% withheld for performance of its own core functions, neither reprogramming funds nor terminating another tribe's contract would have resolved the problem.

In reversing the Tenth Circuit case, the Supreme Court seems to have adopted, at least implicitly, a Court of Claims exception to an otherwise harsh rule regarding contracts that violate the Anti-Deficiency Act. Two early Supreme Court cases applied the Anti-Deficiency Act with rather harsh results for the contractors involved. In Hooe v. United States, 218 U.S. 322, 334 (1910), the Court held that a contract purporting to obligate the Government in excess of available appropriations was "a nullity, so far as the government is concerned, and no legal obligation arises upon its part to meet its provisions." The Court expanded on this rule in Sutton v. United States, 256 U.S. 575, 579 (1921), holding that not only was the contractor not entitled to payments made in excess of appropriations, but the Government could recover payments already made, notwithstanding the fact that the Government enjoyed the benefit of the contractor's efforts. The Court of Claims subsequently distinguished Hooe and Sutton by drawing a distinction between contracts that exceed a specific appropriation and those that exceed a general appropriation, denying recovery in the former instance and permitting it in the latter. For example, in Ross Construction Corp. v. U.S., 392 F.2d 984 (Ct. Cl. 1968), the court stated:

For years this court has made a distinction between contractors paid out of a general appropriation and those for which a specific and limited appropriation is made by Congress. The former have been held not barred at all by exhaustion of the appropriation, on the theory that "a contractor who is one of several persons to be paid out of an appropriation is not chargeable with knowledge of its administration, nor can his legal rights be affected or impaired by its maladministration or by its diversion, legal or illegal, to other objects."

By reversing the Tenth Circuit decision in Cherokee Nation, the Supreme Court appears to have adopted the position that the "availability of appropriations" clause does not shield the Government from liability even if the Government has over-obligated its lumpsum appropriation. That is, the Court's decision seems to suggest that the tribes involved in the Tenth Circuit case are entitled to recover even if sustaining their claims would require the HHS to spend more than the funds appropriated by Congress.

SECOND OPINION • As I read the Federal Circuit decision, it says that the agency should reprogram funds to cover the

amount that the tribes say that they are entitled to receive. It can be argued that the Court's affirmation of that decision and its reversal of the Tenth Circuit decision indicates that the Court believed that the same could be done in the Tenth Circuit case.

Same Issues?

The Court considered the issues in the Tenth and Federal Circuits to be the same. For example, the Court stated: "In light of the identical nature of the claims in the two cases and the opposite results that the two Courts of Appeals have reached, we granted certiorari." (Emphasis added.) See also the following interchange with the tribes' counsel:

JUSTICE O'CONNOR: Are the circumstances any different in the two situations, the Cherokee Nation case and the one in the Federal Circuit? Are--are the circumstances, giving rise to the claim, different in any respect that could account for a difference in outcome?

MR. MILLER: No, Justice O'Connor. There--there is no difference in that respect, and there is an overlap in--in this sense. The Shoshone-Paiute contract that arose through the Tenth Circuit case did involve fiscal year 1996, the same fiscal year as the Cherokee contract that covered fiscal year 1996. So in that sense, both cases involved the--the same relevant issues.

Transcript of Oral Argument, 2004 WL 2650544, at *5-6 (Nov. 9, 2004) (emphasis added).

Government counsel attempted to make a distinction between the two cases based on the declaration referred to by Karen:

JUSTICE GINSBURG: On--on that point--on that point, in the Federal Circuit Judge Dyke expressed considerable displeasure with the Government because he said three times I said, tell me what existing programs with other tribes would have been reduced if these contract support costs are paid in full. And he said, I asked them again and again and again, and they were unresponsive. So since the Government declined to tell the court what programs--existing programs with other tribes would have been reduced, mustn't we assume, as I think the Federal Circuit did, that the proof is unavailable and no existing program with other tribes would have been diminished?

MR. SRINIVASAN: I don't--I don't think so, Justice Ginsburg. I mean, one straightforward reason why you don't have to take that assumption is that it's not only the Federal Circuit case that's before the Court, it's also the Tenth Circuit case. And there's--there are declarations in the Tenth Circuit case that specifically assert that diverting funding for--to pay for the contract support costs of these tribes would have required reducing funds for programs, projects, or activities serving a tribe.

JUSTICE GINSBURG: Now, what does that mean?

2004 WL 2650544, at *50-51. However, the discussion that followed failed to provide any definitive indication of the status of the funds in the Tenth Circuit case and how the status of those funds differed from the funds in the Federal Circuit case.

Uncertainty Of Funds' Status

One of the problems with this case is that imprecise characterizations of the status of funds abound. For example the terms "spend" and "spent" are used. These terms could mean that the funds were obligated or expended (paid out). Similarly, the term "exhausted" is used to describe the funds' status. Again, this could mean either obligated or expended. The declaration that Karen refers to is similarly ambiguous, failing to indicate whether the funds were obligated or expended. It stated:

As the attached budget tables show, all of the money reserved by IHS Headquarters for fiscal years 1996 and 1997 for allocation to the Area Offices on a nonrecurring basis spent for these and the other purposes listed on the budget tables during the fiscal year, leaving a zero balance at the end of the fiscal year.

Joint Appendix, Vol. I, 2004 WL 2326784, at *217 (June 18, 2004) (emphasis added). The terms "spent" and "zero balance" could refer either to an obligation or an expenditure.

A Case Of "Contract Authority"

Agencies are authorized to enter into contracts incurring obligations either through the passage of an appropriation act or by a statute granting such authority without the necessity of an appropriation. The latter type of authority is called "contract authority." See 2 USCA § 622(2)(A):

The term "budget authority" means the authority provided by Federal law to incur financial obligations, as follows:

* * *

(iii) contract authority, which means the making of funds available for obligation but not for expenditure;...

It appears that this is the type of authority involved in these tribal contracts. In procurement contracts, it has been held that where obligations have been incurred under such "contract authority," the Government is bound to those promises even though a subsequent appropriation is insufficient to cover the authorized obligations, New York Airways, Inc. v. U.S., 177 Ct. Cl. 800, 369 F. 2d 473 (1966). Perhaps this is what the Government was referring to when it argued that although the tribes would have had a valid claim under a procurement contract but not under their contracts. The Court rejected the Government's contention and outlined the ways in which the Government's obligations could be satisfied. In doing so, it cited New York Airways favorably:

We recognize that agencies may sometimes find that they must spend unrestricted appropriated funds to satisfy needs they believe more important than fulfilling a contractual obligation. But the law normally expects the Government to avoid such situations, for example, by refraining from making less essential contractual commitments; or by asking Congress in advance to protect funds needed for more essential purposes with statutory earmarks; or by seeking added funding from Congress; or, if necessary, by using unrestricted funds for the more essential purpose while leaving the contractor free to pursue appropriate legal remedies arising because the Government broke its contractual promise. See New York Airways, Inc. v. United States, 177 Ct. Cl. 800, 808-811, 369 F.2d 743, 747-748 (1966); 31 U.S.C. § § 1341(a)(1)(A) and (B) (Anti-Deficiency Act); 41 U.S.C. § 601 et seq. (Contract Disputes Act); 31 U.S.C. § 1304 (Judgment Fund); see generally 2 General Accounting Office, Principles of Federal Appropriations Law 6-17 to 6-19 (2d ed. 1992) (GAO Redbook). The Government, without denying that this is so as a general matter of procurement law, says nothing to convince us that a different legal rule should apply here.

Summary

Viewed as a case involving "contract authority" and in light of the ambiguous indications of the status of funds, Cherokee Nation should not be cited for broader propositions. Thus, we will have to wait for another day to see if the Court would permit recovery where an agency's obligations exceed the amount of a general appropriation without having "contract authority."

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