



UNITED STATES
CIVILIAN BOARD OF CONTRACT APPEALS

GRANTED IN PART: March 6, 2017

CBCA 3860

1441 L ASSOCIATES, LLC,

Appellant,

v.

GENERAL SERVICES ADMINISTRATION,

Respondent.

Brett D. Orlove, Matthew S. Kirsch, and Nicholas J. Larson of Grossberg, Yochelson, Fox & Beyda, LLP, Washington, DC, and Benjamin A. Klopman of Benjamin A. Klopman, Chartered, Rockville, MD, counsel for Appellant.

Elyssa Tanenbaum and Justin Hawkins, Office of General Counsel, General Services Administration, Washington, DC, counsel for Respondent.

Before Board Judges **VERGILIO**, **DRUMMOND**, and **ZISCHKAU**.

VERGILIO, Board Judge.

On May 16, 2014, the Board received a notice of appeal from 1441 L Associates, LLC (lessor) (the successor to 9th & D Joint Venture; “lessor” denotes the appropriate entity as distinctions between the original and successor are not material) concerning its lease contract, GS-11B-20810, with the General Services Administration (agency or GSA). The parties entered into a three-year lease extension of a twenty-year lease. The extension agreement specifies that the annual rent shall be \$7,394,982 (or \$616,248.50 per month) “plus accrued operating costs.” After noting that the current annual escalated operating costs amount is \$1,696,355.10, the agreement provides that the Government shall continue to pay to the lessor the cumulative operating expense adjustments over the original base year; that is, annual adjustments to operating costs based upon changes in price indexes. The agreement does not contain a dollar figure for those adjustments.

At issue in this dispute is the interpretation of the extension agreement as it relates to the cumulative operating costs to be paid by the agency. The plain language of the agreement supports the general position of the lessor. The monthly rental payment is to include the basic rental rate (\$616,248.50 per month) plus the cumulative operating expense adjustments over the original base year. That monthly adjustment amount was \$52,470.97 in the first year of the extension. The agency concludes that the monthly adjustment amount was \$31,691.24, as it looks to operating costs established ten years into the underlying lease as the base; that position is inconsistent with the plain language. The agreement requires the agency, in the initial year, to pay more than the basic rental rate. The reference to the original base year clearly does not reference adjustments accumulated from a different time period. Contrary to the position of the agency, parol evidence is consistent with the plain language of the extension agreement. The record reveals that the lessor rejected agency attempts to alter the base for calculating adjustments to the operating costs. The contracting officer was unable to obtain lessor agreement with attempts of the agency to change the operating costs base; thus, that the contracting officer put forward a per square foot figure to reflect operating costs and taxes does not evidence an interpretation to be imputed to the lessor when the lessor rejected such an approach. Moreover, a draft of the extension agreement specified that the basic rent included the new operating costs base; that language did not survive the negotiation process.

After its initial claim, the lessor has altered the amount sought, in part based on amounts paid (or to be paid) by the agency, the passage of time with indexed increases definitized, and a reduction in rental space. The lessor now seeks \$249,356.63 for each of the three years, plus accrued interest. The lessor is entitled to this amount for the first year (less amounts already paid for the initial months of year one of the extension); for the second and third year, the lessor is entitled to this amount less any necessary adjustments because of a space reduction. Given the dispute over payment, the lessor has not discussed or shown entitlement to recover interest under the Prompt Payment Act, 31 U.S.C. § 3901(d)(5) (2012). The lessor is to recover interest under the Contract Disputes Act, 41 U.S.C. § 7109, calculated from April 8, 2014. The Board grants in part the appeal to this extent.

Findings of Fact

Terms of the contract relevant to the positions of the parties

1. On October 30, 1992, the parties entered into a lease contract for a fixed ten-year period. Exhibit 3 at 1 (all exhibits are in the appeal file). The annual rent was \$3,777,857.06 (or a monthly rent of \$314,821.42), with options available for the agency to increase the rental space. The lease also provided for adjustments in the agency's obligations

to pay real estate taxes and operating costs. Exhibit 3 at 1, 11-12. This agreement reflects an initial annual payment of approximately \$32.51 per net usable square foot (nurf).

2. The agency had the right to renew the lease for a ten-year period:

The Government has the right to renew this Lease for a period of ten (10) years. The rent for this option term shall be \$30.80 /NUSF, (i.e., the base rental for the space to be leased only, not counting the base cost of services and its corresponding escalations, shall be \$1.80/NUSF more for the option term than for the firm term).

Exhibit 3 at 1 (¶¶ 1, 5).

3. Paragraph 3.4, an Operating Costs clause from the General Services Administration Acquisition Regulation (GSAR) (June 1985), 48 CFR 552.270-23, provides as follows, with the added, agreed-upon sentence next to paragraph (A) that “The base cost of services is \$798,220.00.”:

- (A) Beginning with the second year of the lease and each year after, the Government shall pay adjusted rent for changes in costs for cleaning services, supplies, materials, maintenance, trash removal, landscaping, water, sewer charges, heating, electricity, and certain administrative expenses attributable to occupancy. Applicable costs listed on GSA Form 1217, Lessor’s Annual Cost Statement, when negotiated and agreed upon, will be used to determine the base rate for operating costs adjustment.

- (B) The amount of adjustment will be determined by multiplying the base rate by the percent of change in the cost of living index. . . .

- (C) If the Government exercises an option to extend the lease term at the same rate as that of the original term, the option price will be based on the adjustment during the original term. Annual adjustments will continue.

. . . .

- (E) The offer must clearly state whether the rental is firm throughout the term of the lease or if it is subject to annual adjustment of operating costs as indicated above. If operating costs will be subject to adjustment, it should be specified on block 19 of GSA Form 1364, proposal to lease space, contained elsewhere in this solicitation.

Exhibit 3 at 12. The parties understood that rental was subject to annual adjustments of operating costs; as specified in paragraph (A), the lessor provided a completed GSA Form 1217. Exhibit 3 at 187-88. The \$798,220 amount reflects annual base operating costs of approximately \$6.87 per nusf ($\$798,220 \div 116,206$ nusf).

4. The ten-year, firm term of the lease commenced on June 13, 1993, and ended on June 12, 2003. Within the first year, the agency exercised options to increase its leased space while increasing the base cost of services for which it was liable; the agency also added fully serviced space through bilateral amendments effective in 1995, 1996, 1997, and 2000. Adjustments were made to the total annual rent and to the operating costs. Exhibits 6-9, 13-14, 16, 21. During the initial ten-year term the parties entered into bilateral modifications adjusting the agency's payments for operating costs; these adjustments were made to base operating costs as adjusted for the additional space, not the \$798,220 figure in the lease identified as the base cost of services (finding 3). The agency paid adjustments to operating costs, which by the end of the period were \$20,779.72 monthly. Exhibits 10, 12, 15, 17-20, 22-23.

5. In a letter, the agency unilaterally exercised its renewal option for a ten-year term, through June 12, 2013:

the option is for a ten (10) year term at a rental rate of \$30.80/nusf for 156,206 NUSF of office and related space. This rental rate includes base operating costs. As stated in your letter dated June 12, 2002, the original base year operating costs and real estate taxes shall be the same base year for the 10 year option period.

Exhibit 24. Bilateral supplemental lease agreement (SLA) 50 amended the lease to reflect the agency's exercise of the option. The new annual rental rate was \$5,060,501.43 (or \$421,708.45 monthly), composed of an annual base rent of \$4,811,144.80 (or \$400,928.73 monthly) and a monthly adjustment of \$20,779.72, to reflect escalations and adjust for an error correction. The new base operating costs became \$1,316,060.13 or approximately \$7.66 per nusf. The contractor submitted its annual operating cost statements on GSA Form 1217 in support. Exhibit 26. By bilateral SLA 51, effective in November 2004, the annual rent was reduced to correct for errors. Exhibits 27, 31. For the second ten-year term, lease payments were adjusted annually to reflect index adjustments to operating costs. Exhibits 28-30, 32-38.

6. Bilateral SLA 81, dated September 18, 2012, amended the lease. Terms included the following:

1. In compliance with paragraph 3.4 of lease attachment A. (SFO #91-158) the rental rate will be adjusted for increased operating costs following the instructions for adjustment in paragraph 3.4(B).
2. Annual Cost of Services will increase from \$1,669,060.70 to \$1,696,355.10 minus the previous increase of \$1,669,060.70 specified in SLA 78 to equal \$27,294.40 increase annually. The monthly amount of \$2,274.53 increases the monthly payment from \$443,065.57 to \$445,340.10 (exclusive of any SLA for overtime utility services).

Exhibit 38 at 1. The agreement sets forth the calculations, identifying the base cost of services as \$1,316,060.13 (referencing SLA 50).

The particular language in dispute and payments

7. The lease was to end on June 12, 2013. Finding 5. A bilateral modification extended the lease for three years, from June 13, 2013, to June 12, 2016, for a stated square footage of office and related space. Pertinent terms of the agreement follow:

2. The annual rent for the extension term commencing, June 13, 2013, shall be \$7,394,982.00, payable at a rate of \$616,248.50 per month, in arrears (based on 176,071 RSF [rentable square feet] times \$42.00 per RSF / 156,206 NUSF times \$47.34 per NUSF) plus accrued operating costs. Said rental is inclusive of all HVAC overtime or extended hours per SLA #9 . . . with the exception of Rent shall continue to be adjusted for operating costs escalations as provided in SFO [solicitation for offers] #05-028, Section 2.2 for the second and third years of the extension period.

....

4. The current annual escalated operating cost amount is \$1,696,355.10 (Per SLA #81). The Government shall continue to pay to Lessor the cumulative operating expense adjustments over the original base year. The base year shall remain unchanged. The next such increase is due on June 13, 2014.

5. The real estate tax base is \$585,044.16 (Per SLA #33) and shall remain unchanged. The percentage of occupancy will remain the same at 100%.

All other terms and conditions of the lease shall remain in full force and effect.

Exhibit 39. The agency executed the agreement on June 17, 2013. Exhibit 39. The parties have stipulated that the reference to section 2.2 of SFO #05-028 is a typographical error for the intended reference of section 3.4 of SFO #91-158, that of the underlying contract quoted in finding 3. Exhibit 56.

8. The agency paid the lessor the total of \$616,248.50 and \$52,470.97, for initial months under the extended lease, but \$616,248.50, for the remainder of the initial extension year. Complaint and Answer (¶ 10); Finding 11.

Claim and contracting officer decision

9. By submission dated November 26, 2013, the lessor submitted a certified claim seeking \$104,941.94 said to be due and payable under the lease, plus interest accrued and payable under the Prompt Payment Act, as set forth in section 28 of the lease. The claim specifies that in November 2013, the lessor received \$1,232,497 (two monthly payments of \$616,248.50 each, for October and November payments). The lessor deemed these to be partial payments, deficient because the payments only included the monthly base rent due under the lease, and not the cumulative operating costs adjustments based on the index. The claim references two statements in supplemental lease agreement 83: “the annual rent for the extension term commencing, June 13, 2013, shall be \$7,394,962.00, payable at a rate of \$616,248.50 per month . . . **plus accrued operating costs**” and the “Government shall **continue to pay to Lessor the cumulative operating expense adjustments over the original base year**” (emphasis added). Further,

The monthly amount of the CPI [consumer price index] Increases due to Contractor under the Lease is currently \$52,470.97 per month. Accordingly, the Government owes the Contractor \$104,941.94 (the “Delinquent Amount”). Notably, from the date SLA 83 was signed (June, 2013) until the date of the October and November 2013 payments, the Government had paid the CPI Increases correctly.

Exhibit 40 at 1-2. In the absence of evidence and argument on this point, the Board concludes that the contracting officer received the claim on April 8, 2014, one day before issuing a decision on the claim.

10. In a decision dated April 9, 2014, the contracting officer concluded that the lessor is owed \$31,691.24 per month since June 2013, and that \$1,316,060.13 is the operating cost base for adjustments beginning in June 2014 (when the next adjustment is to be made). Exhibit 41; Agency Post-Hearing Brief at 12 (¶ 39) (agency confirmed this position, conceding lessor entitlement generally to \$31,691.24 monthly for cumulative operating costs, as well as indexed adjustments for years two and three, but not an additional \$20,779.72 monthly, or \$249,356.73 annually). On May 16, 2014, the lessor filed a notice of appeal with this Board, seeking operating costs under the lease, including annual index adjustments, and interest under the Prompt Payment Act.

11. From October 2013 to May 2014, the agency paid the lessor \$616,248.50 per month. From June 2014 through March 2015, the agency paid the lessor \$647,939.74 per month. This amount includes \$616,248.50 (basic rent) and \$31,691.24 (operating cost adjustments from SLA 50 forward). Amended Complaint and Amended Answer (¶¶ 22, 25). On September 28, 2014, the agency reduced the space being leased. Amended Complaint and Amended Answer (¶ 27).

Facts relating to the extended lease and arguments of the parties

12. In a draft of the lease extension agreement, the agency included a paragraph that set the annual rent, with the rate “inclusive of the new operating cost base” and with the statement, “Rent shall continue to be adjusted for operating costs escalations as provided in SFO #05-028, Section 2.2 [sic] for the second and third years of the extension period.” On February 5, 2013, in marking up that draft, the lessor inserted a figure of \$1,828,306.58 into a sentence establishing a new operating costs base. Exhibit 47 at 3 (¶¶ 2, 4).

13. Thereafter, with negotiations ongoing, the lessor deemed all negotiations null and void as of May 3, 2013. The lessor specified a basic objection to any changes in the operating costs and present tax bases. Exhibit 48 at 2. Later, the lessor provided a draft agreement extending the lease with a monthly rent of \$49.14 per RSF plus accrued operating expenses. As in the final version, rent would continue to be adjusted for operating costs escalations in the second and third years of the extension period. The specific language found in paragraphs four and five of the extension agreement, finding 7, was in the draft; the paragraphs obligated the agency to continue to pay the cumulative operating expense adjustments over the original base year. Exhibit 49 at 3.

14. After reviewing the draft, on May 10, 2013, the agency contracting officer sent the lessor a two-sentence email message:

The Congressionally approved Prospectus does not give me the authority to execute a lease above \$50.00 and your offer of \$49.14 plus the accrued passthroughs (tax and operating expense) of approximately \$4.15 equaling \$53.29.

It appears that we are wasting each other's time.

Exhibit 50. In arriving at the \$4.15 figure, the contracting officer was assuming a base year amount of \$1,316,060.13, as found in supplemental lease agreement 50, at the start of the second ten-year term, Exhibit 26, as defining the operating costs to be added to the basic rent. Transcript at 77, 175-76 (all transcript references are to volume one).

15. During the negotiation process, the contracting officer “tried to go back to a new [operating costs] base and he [lessor's president/owner] didn't want anything to do with it.” Transcript at 232-33. The contracting officer did not get the lessor's agreement to insert a reference to the operating costs base found in SLA 50 into the extension lease language; despite the attempts of the contracting officer to update the base year for escalation purposes, the lessor insisted upon utilizing the original base year for operating costs. Transcript at 234-37, 242-46, 251-52, 265-66, 268-69. Even if the contracting officer considered the phrase “original base year” utilized during negotiations and in the agreement as referencing \$1,316,060.13, Transcript at 253-54, 271-72, and the contracting officer determined that the lessor knew (or should have known) this from the message referring to \$4.15, as the operating costs and tax bases, finding 14, the \$1,316,060.13 figure is not found in the agreement as the operating costs base, and the \$4.15 figure is not found in the agreement. The contracting officer did not obtain what he sought through the negotiation process; rather, the lessor insisted that the lessor continue to receive adjustments over the original base year.

Discussion

The lessor now seeks \$249,356.63 per year for each of the three years of the extension lease as payment of accrued operating costs unpaid or disputed by the agency, plus accrued interest. Lessor Post-hearing Brief at 24. This appeal presents no novel legal principle. The lessor bears the burden of proof. The Board conducts a de novo review of a contracting officer's decision. 41 U.S.C. § 7103(d). The plain language of an agreement typically prevails in matters of contract interpretation. *McAbee Constr., Inc. v. United States*, 97 F.3d 1431, 1435 (Fed. Cir. 1996).

Interpretation

At issue in this dispute is the interpretation of the extension agreement as it relates to the cumulative operating costs to be paid by the agency. The lessor contends that it is entitled to cumulative operating costs beginning in year one of the extension, calculated from the start of the twenty-year lease, with index adjustments for the final two years of the extension period. The agency contends that for the first year of the extension period the lessor is entitled to operating costs adjustments calculated utilizing an operating costs base established ten years into the underlying lease, and index adjustments calculated utilizing that figure for the final two years of the extension period. The agency contends that a portion of the operating costs are included in the \$616,248.50 monthly figure, such that any additional payment would represent duplicative recovery of operating costs by the lessor.

The extension agreement specifies that the annual rent for the extension term shall be payable at a rate of \$616,248.50 per month plus accrued operating costs. Further, the rent shall continue to be adjusted for operating costs escalations. The agreement both recognizes that the current annual escalated operating cost amount was \$1,696,355.10 and that the agency shall continue to pay to the lessor the cumulative operating expense adjustments over the original base year. Finding 7.

The plain language of the written agreement dictates the result. In addition to the basic rent, the lessor is to receive accrued operating costs, also referred to as cumulative operating expense adjustments. No adjustment would be made for year one; however, indexed adjustments would be made for years two and three. The monthly adjustments over the original base year were \$52,470.97. The phrase “original base year” does not mean a figure utilized at the ten-year period of the lease.

The agency requests that the Board consider parol evidence to support its interpretation. It is permissible to consider parol evidence if such supports the plain language of an agreement. Here the parol evidence indicates that the lessor did not agree to agency attempts to alter the original base year of operating costs as the starting point for payments to supplement the basic rent. The formulation of an agreement with operating costs included in the basic rent was considered, but was not adopted. The contracting officer did not establish an interpretation that was consistent with the negotiations to reflect a mutual intent. Findings 12-15.

Finally, the agency suggests that the lessor would receive a windfall if its interpretation is adopted. The bilateral written agreement provides for payments during the extension period. The agency is obligated to pay in accordance with the agreement. However, the agency also has not demonstrated that the lessor’s interpretation would result

in a windfall or duplicative payments. While the agency and this contracting officer harken back to SLA 50 as resetting the operating costs base, in fact, that SLA noted the basic rent and the adjustments of the accumulated operating costs, which for ease of calculations resulted in a single number for calculations from that point forward; however, the agency was obligated to pay the accumulated operating costs adjusted from the start of the lease. Finding 5. Nothing changed through SLA 81. Finding 6. The lease extension did not alter this agency obligation to pay cumulative operating costs.

Payment

The lessor seeks \$249,356.63 annually, for the entire extension period, plus accrued interest. This roughly represents the originally sought \$52,470.92 per month as the cumulative operating costs less the amount the agency concedes it is obligated to pay, \$31,691.24 per month. Findings 10-11. The plain language of the lease supports the entitlement sought by the lessor. However, the lessor already received payment of a portion of the \$249,356.63 for some months during year one of the extension, finding 8, such that a reduction must be made. Further, a reduction to operating costs payments may be required for years two and three after the space reduction during year two, finding 11.

The parties have offered no substantive discussion on the calculation of interest under the Prompt Payment Act, 31 U.S.C. § 3901 et seq. (2012), or the Contract Disputes Act, 41 U.S.C. § 7109. Given the dispute over payment, the lessor has not articulated a basis to recover interest under the Prompt Payment Act, 31 U.S.C. § 3901(c)(5) (interest penalty not required on payment not made because of a dispute over the amount of payment). The lessor has prevailed in this dispute. It is entitled to recover interest under the Contract Disputes Act calculated from April 8, 2014 (the date the contracting officer received the underlying claim), until the date of payment.

Decision

The Board **GRANTS IN PART** the appeal.

JOSEPH A. VERGILIO
Board Judge

We concur:

JEROME M. DRUMMOND
Board Judge

JONATHAN D. ZISCHKAU
Board Judge