BEFORE THE ARMED SERVICES
BOARD OF CONTRACT APPEALS
Falls Church, Virginia 22332

WORK COPY

APPEAL OF:	)	
	)	ASBCA NO. 43965
FREEDOM N.Y., INC.	)	
CONTRACT NO. DLA13H-85-C-0591	)	

APPELLANT'S CORRECTED POST-HEARING BRIEF

Norman A. Steiger, Esquire
Goldberg & Connolly
66 North Village Avenue
Rockville Centre
New York, NY 11570

Bruce M. Luchansky
Kollman & Sheehan, P.A.
Sun Life Building
20 S. Charles Street, 8th Floor
Baltimore, MD 21201
(410) 727-4300

Counsel for Appellant

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APPELLANT'S POST-HEARING BRIEF

This is an appeal pursuant to the Contracts Disputes Act of 1978, 41 U.S.C. §601 *et seq.*, from the contracting officer's final decisions dated June 22, 1987 and October 7, 1991, under Contract No. DLA13H-85-C-0591 (the "MRE-5 Contract," or the "Contract"). Pursuant to the Board's June 1, 2000 order, Appellant Freedom N.Y., Inc. ("Appellant" or "Freedom"), hereby submits its post-hearing brief in the above-captioned matter.

I. INTRODUCTION

Appellant has always believed that the majority of public servants are of the highest character and go about their jobs with integrity and compassion. Their decisions are sometimes misguided, sometimes even wrong, but usually well-intended. Appellant, however, is forced to present a case that is the exception. The proposed Findings of Fact describe pervasive, unrelenting, and intentional conduct by Government officials, particularly Mr. Marvin Liebman, the ACO, and Mr. Frank Bankoff, the PCO, that was calculated to prevent Freedom from performing the Contract. The facts lead to only one inescapable conclusion -- acts of bad faith and abuse of discretion were perpetrated by Government officials on the Appellant.

The Government's conduct not only caused Appellant to incur additional costs of performance of the MRE-5 Contract, but it also caused the complete demise of Appellant's

business as an Industrial Planned Producer and deprived Appellant of its opportunity to earn profits on the MRE-5 Contract, and on subsequent MRE contracts.

Not all of the damages Appellant seeks, however, require a showing of bad faith. Appellant's initial claim is for customary relief under the Contract for increased costs incurred by the Appellant as a result of Government acts and omissions which constructively changed the Contract, and which caused extensive and costly program delays. These constructive changes alone, without regard to recovery for the Government's breach of the Contract, entitle the Appellant to damages of approximately $9 million.

Based on the evidence presented, the Board should conclude that the Government breached Contract No. DLA13H-85-C-0591, caused Appellant to incur increased costs not anticipated at time of Contract, and committed acts in bad faith. Appellant requests appropriate relief for the claims arising from the Government's conduct throughout the life of the Contract.

II. PROPOSED FINDINGS OF FACT

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The MRE Program Is Part Of The IPP Program

1. The Meal, Ready-to-Eat (MRE) ration was a mobilization essential item that could be procured by negotiation pursuant to 10 U.S.C. § 2304(a)(16), in effect in the early 1980s. Section "(a)(16)" was an exception to formally advertised contracting. Hearing Transcript ("Tr.") 50.

2. Beginning in 1980, the Department of Defense ("DoD") undertook to develop and maintain three MRE assemblers to meet DoD's Industrial Planned Producer ("IPP") requirements. *Id.*[1]

3. In order to qualify as an MRE assembler, a contractor had to meet stringent requirements. This effort required substantial start-up costs. Tr 50-51.

4. MRE assemblers had to qualify as manufacturers under the Walsh Healey Act, 41 U.S.C. § 35 *et seq*, and, therefore, had to have "retort" capability, *i.e.*, the ability to manufacture entrees. Tr. 44. The process involved preparing the food (dicing, chopping, slicing, and partially or fully cooking it), putting it into a pouch, sealing the pouch, and placing the pouch into a retorter machine for pressurized cooking and sterilization. Tr. 43-44. The retort area had to be approved by and remain under the establishment seal of the U.S. Department of Agriculture. Tr. 45. Just becoming a "retorter" required an investment of $2 - $3 million. Tr. 71.

5. Assemblers also performed all of the other supporting functions necessary to produce cases of MREs, including two subassembly operations. Tr. 41. Crackers arrived in bulk and had to be packaged individually. *Id.* Accessories such as matches, chewing gum, and toilet tissue had to be sealed in pouches. Tr. 41-42. The retort and subassembly pouches were then gathered in an assembly area and placed into the main MRE component, the MRE pouch. Tr. 42.

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[1]Initially, DoD developed three assemblers and three retorters (manufacturers of entrees). Tr. 50-52. Shortly thereafter, DoD phased out its separate retort contracts and, beginning with MRE 5, contracted with the three assemblers for all of its MRE requirements. Tr. 55-56.

6. The MRE meal pouch had rigid logistical requirements -- it had to be air droppable, have a five-year shelf life, and be fully protected from any type of contamination, including insects or biological/chemical contaminants. Tr. 46.

7. Twelve meal pouches were placed in each case. Tr. 41. The cases were made of thick, solid fiberboard which required a machine to fold it over and glue it shut. Tr. 46. The cases then were covered with a fiberboard sleeve, strapped, carted off to another area for palletizing and then warehoused. Tr. 41.

8. MRE contractors had other substantial requirements imposed by the Government. A quality assurance lab was required to assure compliance with the military's rigid production standards for food prep and handling. Tr. 45. An inventory control area was necessary to fulfill the Government's first-in, first-out (FIFO) requirement for use of components. *Id.* The contractor had to be able to keep track of all of the components received, including the date received and the place stored, in order to comply with this FIFO requirement. *Id.* Office space was also required for the contractor's administrative operations. *Id.* The contractor's subassembly, main assembly, and warehouse areas had to meet specific sanitary requirements, pursuant to inspections by the Army Veterinary Inspectors. ("AVI"). Tr. 46.

The Government Paid For The MRE Contractors' Start-Up Costs

9. DPSC had broad authority under 10 U.S.C. § 2304(a)(16) and DAR 3-216.2 to award contracts to more than one contractor and to provide incentives necessary to establish MRE suppliers for the MRE program. Tr. 52.

10. In 1980, during the initial MRE procurement, the Government established three MRE contractors, Southern Packaging Company ("Sopakco"), American Pouch Foods ("APF"), and Right Away Foods ("Rafco"). Tr. 40.

11. APF was a small, minority-owned, start-up business with no other contracts. Tr. 58, 221. To establish APF as an MRE contractor, the Government granted substantial incentives to APF for MRE 1. For example, since MRE 1 was APF's only contract, DPSC agreed that all of APF's costs were "direct" costs. Therefore, APF could expense rather than depreciate all of its start-up costs, including such "capital"items as their lease costs and the costs of all their equipment. Tr. 58. Moreover, progress payments were paid on all of these costs. Tr. 59.

12. Rafco also received Government incentives to establish itself as an MRE supplier. The Government negotiated a fixed-price contract with Rafco for MRE 1 even though it had never produced MREs and had no production facilities at the time of contract award. Rule 4 (hereinafter, "R4"), tab FT010, Bates 00073.[2] To enable Rafco to perform MRE 1, the Government agreed to pay for Rafco's leasehold expenses. Tr. 59-60; R4, tab FT010, Bates 00073-74. DPSC agreed that Rafco could expense these costs as one-time costs to the contract and that these costs would be treated as direct costs for purposes of that contract. *Id.* Rafco received progress payments for these costs. Tr. 61.

Freedom Attempted To Enter The MRE Program

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[2]The record consists of five different document submissions, which will be cited in this Brief as follows. The Government's initial Rule 4 submission will be cited as a tab without a preceding letter designation, *e.g.*, "R4, tab 1." The Government's supplemental Rule 4 submission will be designated with a "G," *e.g.*, "R4, tab G1." Appellant's Rule 4 submissions will be designated with an "F," "M," or "FT," as appropriate. Periodically, reference will be made to the specific page of an "FT" document by Bates stamp number, *e.g.*, "R4, tab FT001, Bates 00001."

13. In 1980, Freedom Industries, Inc. ("Freedom Industries")[3] was a small, but profitable minority-owned food service company that provided school lunches to the Paterson, New Jersey public schools. Tr. 218; R4, tab FT036, Bates 00517. Freedom Industries and its president, Henry Thomas, developed expertise in food processing, developed a 15,000 square foot processing plant in Mount Vernon, N.Y. and a 25,000 square foot plant in Lodie, N.J., both of which met the rigid health, quality, and operational standards imposed by the USDA. R4, tab FT036, Bates 00517.

14. Freedom Industries was willing to make whatever effort was necessary to become an MRE assembler. DPSC agreed to award Freedom Industries two retort pouch contracts so that Freedom Industries could meet the Walsh Healey prerequisite for becoming an MRE assembler. Tr. 68-69, 231; R4, tab FT015(b,c), tab FT023.

15. The Government knew that Freedom Industries was investing in the retort contracts only in order to become qualified as an assembler. The Government stated that if Freedom Industries performed the contracts, it would qualify as a manufacturer under Walsh Healey, it would be put in the IPP program as an MRE assembler, and the PCO would award sustaining contracts as with Sopakco and Rafco. Tr. 234, 246.

16. To become an assembler, however, the PCO required that Freedom Industries give up its school lunch business and devote its full efforts to MRE production. Tr. 232. Freedom

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[3]Freedom Industries, Inc. was the entity that contracted with the Government to perform the MRE-5 Contract. On April 17, 1985, the Contract was novated to a corporate affiliate of Freedom Industries, Inc., known as H.T. Food Products, Inc. In anticipation of this novation, on April 3, 1985, H.T. Foods amended its Articles of Incorporation to change its name to Freedom NY, Inc. R4, tab 61. The Government approved this name change. R4, tab 61, tab 62. This Brief refers to the contractor before the novation as "Freedom Industries." It refers to the contractor after the novation as "Freedom."

Industries agreed. Tr. 233.

17. At the time Freedom Industries was awarded the retort pouch contracts, it had no resources in place for the production of MREs. It had no lease for an MRE facility, it had no financing commitments, and the Government did not agree to provide financing. Tr. 234-35, 238. The Government did not pay for Freedom Industries' costs for production facilities under these contracts. Freedom Industries bore all of these costs by itself. Tr. 70.

18. In reliance on the Government's promise of future MRE assembly contracts, Freedom Industries eliminated its school lunch business and invested a staggering amount of time and money into performing the retort contracts in order to become an MRE assembler, which would receive annual follow-on contracts. Tr. 232.

19. Freedom Industries invested approximately $2 million to obtain the facility and equipment necessary to become an MRE assembler. Freedom Industries leased a 200,000 sq. ft. facility at Hunts Point in the Bronx in order to be able to perform as an MRE assembler. *Id.* Freedom only needed a 20,000 square foot plant to perform the MRE 3 retort contracts. Tr. 233. The lease was a ten-year lease because Freedom understood that it would receive follow-on assembler contracts. Tr. 146. Freedom Industries obtained three Rotomats for retort pouch production. Tr. 240-42, 247. This was the same number of retort machines that Rafco, an MRE assembler, had. Tr. 63.

20. Freedom Industries obtained approximately $1.4 million of its investment in the MRE program from Dollar Dry Dock Savings Bank ("Dollar"),[4] which received preferred stock in Freedom Industries in consideration for its investment. Tr. 239; R4, tab FT016(a-m). As an investor in Freedom Industries, Dollar's interests were aligned with Freedom Industries'. Dollar's return on its investment depended on Freedom's success.

21. Freedom Industries obtained three of the Rotomats through the investment of William (Zev) Robbins, an entrepreneur who agreed to purchase the Rotomats and lease them to Freedom Industries. Tr. 241-42, 245. Robbins also remained interested in providing additional financing to Freedom Industries if the need arose. Tr. 242, 244.

22. The retort contracts alone were not profitable for Freedom Industries because of the significant investment costs required to perform them. Tr. 72. All parties were aware that follow-on contracts were necessary for Freedom Industries to recoup its initial investment in these contracts. *Id.* Freedom Industries developed this 200,000 square foot processing plant (R4, Tab FT 020) and made this investment in the MRE 3 retort contracts only so that it would qualify as an MRE assembler and obtain future MRE assembly contracts. Tr. 246, 253.

23. The Government knew that Freedom Industries was making this investment for purposes of becoming an IPP producer. Government officials from DLA, a team from the

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[4]Dollar made available to Freedom Industries far more financing than Freedom Industries actually used. Dollar made available at least $5 million in financing. R4, tab FT016f. The figure of approximately $1.4 million was the amount that Freedom Industries actually "drew down" from its credit line with Dollar. Tr. 239.

Pentagon, and other inspectors performed an IPP facility survey of the Hunts Point plant. Tr. 253. The facility passed. *Id.* As a result, the Government approved Freedom Industries as an IPP contractor "with this facility and this capability."

24. Freedom Industries developed and provided this 200,000 square foot USDA facility in consideration for the Government's promise to establish and maintain Freedom Industries as an MRE assembler under the IPP program. Tr. 246.

25. Freedom Industries successfully performed both MRE 3 retort pouch contracts (Tr. 247) and stood ready to receive MRE assembler awards, as promised by DPSC. The D&F issued on December 16, 1982 for MRE 4 included Freedom Industries as one of the three IPP contractors to which awards could be made. R4, tab FT018.

26. Freedom Industries submitted a proposal for an MRE 4 prime assembler award. Tr. 248. A pre-award survey was performed, and Freedom Industries received a positive recommendation for an MRE 4 prime assembler award. *Id.*; R4, tab FT442. Moreover, Freedom Industries submitted the lowest price proposal of the three IPP qualified contractors, Sopakco, Rafco, and Freedom Industries. Tr. 250.

27. Nevertheless, DPSC did not negotiate with Freedom Industries and did not award an MRE 4 contract to Freedom Industries. Tr. 248. Sopakco and Rafco received MRE 4 contracts. Tr. 251. Freedom Industries was forced to shut down its operations and laid off all its employees. Tr. 252.

28. The Government subsequently recognized that it had failed to perform its promise to establish and maintain Freedom Industries as an MRE assembler. The Government agreed to make good on its promise and award an MRE assembler contract to Freedom Industries under

MRE 5 in exchange for Freedom Industries' dismissal of a lawsuit that Freedom Industries had brought. Tr. 278.

29. DoD issued two separate D&Fs for the MRE 5 procurement. On December 9, 1983, Billy B. Williams, Acting Executive Director of Contracting, issued a D&F requiring awards under the MRE-5 procurement to all three qualified MRE assemblers. R4, tab FT028. These awards were critical to the Government because the current MRE industrial base was

> *not adequate to meet the mobilization requirements*. For this reason, efforts must be made to retain all three contractors as viable producers. The award of contracts to all three producers will accomplish this purpose.

Id. (emphasis added).

30. This position was reiterated on February 7, 1984 by James P. Wade, Acting Under Secretary of Defense, in another D&F issued for MRE 5. R4, tab F7. Wade emphasized the critical nature of the Government's need to develop another supplier of MREs. The Government only had 5.9 million cases of combat rations on hand, yet the Government would need approximately 18.4 million cases at M+180 "*and approximately 5.3 million cases each month during mobilization.*" *Id.* (emphasis added). For that reason, the D&F authorized an increase in the MRE procurement from 2.3 million cases for MRE 3 (R4, tab FT011) and MRE 4 (R4, tab FT018) to 3.1 million cases for MRE 5 (R4, tab F7; Tr. 263-266), and it was determined that awards should be made to all three assemblers:

> It is in the interests of national defense and industrial mobilization that **existing industrial preparedness planned producers be awarded contracts** in accordance with Finding 1 above **and be kept available** for furnishing the above described supplies in the

> event of a national emergency and acquisition by negotiation is necessary to that end.

Id. (emphasis added).[5]

31. This language reflected the understanding of the Government and of Freedom Industries that, as a qualified MRE assembler, Freedom Industries would receive an award of a portion of each future year's MRE solicitation based on mobilization capacity. Tr. 278, 281. *See* Tr. 271-72.

32. On March 15, 1984, after receiving these D&Fs and the MRE 5 solicitation, Freedom Industries dismissed its lawsuit. R4, tab FT034.

The MRE 5 Solicitation

33. On February 15, 1984, the Government issued Solicitation No. DLA13H-84-R-8257 for MRE 5 to the three MRE IPP-approved contractors, Sopakco, Rafco, and Freedom Industries (the "Solicitation"). R4, tab 2. The total procurement was to be divided among the three contractors. The size of each award would be based on production capability first and then price, and would be tied to the offeror's pre-established minimum sustaining rate for a 12 month period. *Id.*

33.a. On February 24, 1984, Freedom Industries, a socially and economically disadvantaged small business received its SBA 8(a) certification from the U.S. Government. R4, tab FT031.

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[5]Once again, the awards would be divided among the three contractors based on production capability and price. R4, tab F7.

34. The Solicitation incorporated the DAR Progress Payment Clause, thereby making progress payments available to the contractors as a means of financing the contracts awarded under the Solicitation. R4, tab FT030, Bates 00418. The provision that applied to Freedom Industries, DAR 7-104.35(b), Progress Payment for Small Business Concerns, provided for progress payments equal to "ninety-five percent (95%) of the amount of the Contractor's **total costs incurred** under this contract . . . . " DAR 7-104.35(b)(1)(emphasis added).[6]

35. The Solicitation, however, contained a clause that ostensibly placed a "ceiling" lower than 95% on total progress payments. Clause L-4 stated that a "total progress payment ceiling for the entire contract is established at $9,000,000 or 50% of the contract value whichever is lesser." R4, tab FT030a, Bates 00400. The "ceiling" described in Clause L-4 deviated from the 95% "ceiling" provided by DAR 7-104.35(b), as incorporated into the MRE-5 Contract's Progress Payment Clause. Tr. 1475. Yet, there is no evidence that the Government ever obtained a DAR Deviation authorizing DPSC to include the L-4 limitation in the Solicitation. *See* Tr. 1475-76. Indeed, the Government is unable to explain the precise source of the L-4 clause, describe how or why it was developed, or identify the basis of its alleged authority to use the L-4 "ceiling" in the Solicitation. Tr. 1171-72, 1476, 1884.

36. By its terms, the L-4 clause provided a mechanism for increasing its "ceiling." To do so, the contractor simply was required to submit a request for an increase "accompanied by a cash flow analysis, detailing impact over and above that on profit." R4, tab FT030a, Bates 00400.

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[6]For small business concerns, such as Freedom Industries, progress payments are paid on costs as they are incurred and before they are paid by the contractor, rather than as reimbursements for costs paid, as was the case with large business concerns. Tr. 1633-34. *Cf.* DAR 7-104.35(b)(1), *with* 7-104.35(a)(1).

The L-4 clause did not contain any language providing the contracting officer with the right to reject a reasonable request for an increase in the progress payment ceiling, provided that the required cash flows were submitted. Tr. 1893; R4, tab FT239, Bates 01636. Based on the language of the clause, Freedom Industries did not understand this provision to impose a finite ceiling on progress payments. Tr. 291. Rather, Freedom Industries understood that this "limitation" would be increased upon a showing of need as supported by cash flows. *Id.*

37. The Solicitation required Freedom Industries to submit highly technical and detailed information about its plans to perform the offered contract. This information included complete manpower build-up charts, milestones, purchase orders, financing data including sources and uses of funds, and cash flows. Tr. 293-94, R4, tab FT030a, Bates 00409-10. Freedom Industries relied on The Government's representations that these documents would reflect the parties' intent regarding performance of the solicited contract. Accordingly, Freedom Industries intended to manage and run this contract in accordance with the documents it submitted and the information contained in them. Tr. 294, 295.

Freedom Industries' Negotiations

38. Freedom Industries submitted a best and final offer to DPSC on August 2, 1984.[7] R4, tab FT047a. Freedom Industries proposed an award of 620,304 cases at $34.81 per case for a total contract price of $21,593,000, to be performed over a period of 24 months. Tr. 296-297. The proposal was supported by, among other things, a Contract Pricing Proposal, Form DD633,

[7]Although Freedom Industries first submitted a proposal on April 11, 1984 (R4, tab 002), Freedom Industries later withdrew that proposal and substituted a proposal at $34.81 per case on July 18, 1984. Tr. 296-297. This proposal was formally resubmitted on August 2, 1984 as a best and final offer. R4, tab FT047, tab 9, tab F11.

and supporting data showing that Freedom Industries sought payment not only for its production costs, but also for its "start-up costs," including such items of a capital nature as quality control equipment, building repair, an automated building management and control system, and lockers. R4, tab FT047.

39. As part of its solicitation requirements, Freedom Industries submitted spreadsheets, which showed Freedom Industries' projected cash flow during the MRE-5 Contract. R4, tab FT047a. The spread sheets also showed that: (1) Freedom Industries anticipated receiving 95% progress payments on its costs (except for the cost of its production equipment) up to a contract maximum of $9,000,000; and (2) that payment of progress payments would begin months before Freedom Industries began to incur direct material and direct labor costs. R4, tab FT047a, Bates 00646. Based on these assumptions, Freedom Industries projected that it would require outside working capital financing of $5,874,210.[8] *Id.* at Bates 00646. Such financing would incur interest costs in the amount of $481,275. *Id.*

40. Freedom Industries' pricing was based on specific plans it provided the Government concerning its anticipated production schedule. Tr. 327-28. Specifically, Freedom Industries intended to purchase high tech, state-of-the art production equipment for its operations.

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[8]Freedom Industries' President, Thomas, and Freedom Industries' CFO, Pat Marra, had different views on how much outside financing Freedom Industries would need to perform the MRE 5 contract. Marra did not believe the Government would pay on time. His position was to take an ultra-conservative stance. Thomas believed that the government would pay in 5-10 days, as required, and therefore outside financing would be further reduced by carefully timing Freedom Industries' payment obligations, *i.e.*, 40-45 day terms. Marra's view was more conservative. Marra preferred to obtain more outside financing than was strictly necessary in order to allow for unexpected financial contingencies. Marra's more conservative and worst case view is reflected on the cash flow sheets that were submitted to the Government. Thomas's best case view, that the Government would pay in 5-10 days, compared to his favorable vendor payment terms, is illustrated in other documents. R4, tab FT443.

Tr. 328-29. Such equipment was highly automated and, therefore, would substantially reduce the labor costs needed to run more antiquated machinery. *Id.* In addition, Freedom Industries planned for the use of a highly-computerized facility that would utilize an automated lot tracking system to keep track of the myriad components of GFM and CFM involved in the contract, and accounting software that would optimize Freedom Industries' accounting system. If Freedom Industries had not planned to use these and other state-of-the-art items, Freedom Industries' proposal would have been substantially higher because of the resulting increase in labor and operational costs. Tr. 328-29. Freedom Industries told the Government the specific type of equipment it intended to use. Tr. 327.

41. Dollar was willing to issue a conditional commitment letter to Freedom Industries to provide $7.244 million in financing "[i]n the event Freedom Industries . . . is awarded a contract . . . in the amount of $21,593,000" and did so by a letter dated August 9, 1984 (the "Commitment Letter"). R4, tab 5. The need for this amount of financing was based on a faulty calculation made by Government Accountant Stokes. Tr. 309. At Stokes's direction, Thomas recorded this calculation on Freedom Industries' cash flow projections while Stokes explained it. R4, tab FT047a, Bates 00645; Tr. 790.

42. The financing requirement being imposed by Stokes was intended solely for the performance of the Contract (Tr. 381, 978-79) and not for the purpose of paying off existing creditors. R4, tab F14; Tr. 978-79.

43. Stokes, who was aware of Freedom Industries' existing indebtedness, made a calculation that concluded that $7.2 financing that was required. The calculation was inaccurate. Tr. 961. For example, it incorrectly assumed that the L-4 ceiling could not be increased, which

would have lowered substantially Freedom Industries' need for financing. Tr. 960-61. It also incorrectly subtracted out Freedom Industries' anticipated profit -- twice in the same calculation -- as if it were a cost. *Id.*

44. Freedom Industries did not, in fact, need $7.2 million in outside financing to perform the MRE 5 contract. Tr. 361, 965. Indeed, a businessman with good cash management skills could have performed the contract with far less financing even than the $1.8 million reflected in Freedom Industries' final, negotiated cash flows -- a number that "could be best described as conservative." Tr. 964-65. Freedom Industries' outside financing requirements, however, depended on the Government's meeting its contractual obligations under the progress payment clause.

45. On August 10, 1984, Dollar Drydock sent DPSC another copy of the August 9, 1984 commitment letter that added a paragraph intended to protect Freedom Industries' SBA 8(a) status. R4, tab 6; Tr. 315-20. The stated condition of an award at $21,593,000 remained unchanged. R4, tab 6.

46. The Government knew that this conditional language in both the August 9 and August 10 letters meant that the Dollar commitment of $7.2 million would not be binding if Freedom Industries' actual contract price was less than $21 million. Tr. 1172-73. The PCO, Mr. Thomas Barkewitz ("Barkewitz"), discussed this issue with the ACO, Liebman, on several occasions during contract negotiations. R4, tab G71, p.2.

47. A finding of responsibility does not require a contractor to have financial resources in place at the time of the determination. Rather, a contractor either must "have adequate financial resources, or the ability to obtain such resources as required during performance of the

contract." DAR 1-903, Minimum Standards for Responsible Prospective Contractors.

48. Freedom Industries had high start-up costs because the Hunts Point facility had been lost and Freedom Industries had no other contracts over which it could spread its expenses. R4, tab FT051a; Tr. 295. Freedom Industries learned that the Government had paid for Rafco's start-up costs and requested that the Government also pay Freedom Industries' start-up costs. Tr. 336. Navy Captain Donald B. Parsons, Jr., Chief of the Contracting and Production Division ("Captain Parsons"), and PCO Barkewitz advised Freedom Industries to include these costs in its progress payment requests and to identify them in Freedom Industries' proposed cash flow statements under general and administrative expenses (G&A) and manufacturing overhead (O/H). Tr. 295.

49. Captain Parsons advised Freedom Industries that it must drop its price from $30.12 to $27.00 per case. If it did so, Freedom would receive an award. Tr. 330. Freedom Industries explained that to do so, it would have to lower the cost of its financing from the $7.2 million then being required by the Government. Tr. 332-33. To reduce its price sufficiently to meet the Government's stated price parameters, Freedom Industries stated that it required 95% progress payments on all of its costs. *Id.* Captain Parsons agreed, stating "that Freedom Industries could receive Extraordinary Progress Payments for 100% of allowable costs." *Id.*; R4, tab FT051a. Freedom stated that it did not require extraordinary progress payments; it would be satisfied with the 95% progress payments on all its costs, as provided by the Progress Payment Clause. *Id.*

50. In reliance on its discussions with Navy Captain Parsons and PCO Barkewitz , on September 7, 1984, Freedom Industries lowered its price from $34.81 per case to $30.12 per

case, for a total contract price of $18,686,500. Tr. 194; tab FT051b. The offer was expressly conditioned on Freedom Industries' receipt of progress payments on all of its incurred costs "including purchases of machinery, equipment and other tangible fixed assets necessary for the performance under this solicitation." R4, tab FT051(B); Bates 00689 & 91.

50.a. On September 16, 1984, DPSC offered Freedom Industries a letter contract to start performance. R4, tab FT056. Freedom refused the letter contract. R4, tab FT058.

51. On October 16, 1984, Freedom Industries submitted a Contract Pricing Proposal, Form DD633, together with supporting data and a full set of revised cash flow spread sheets modified to reflect the $30.12 per case proposal. R4, tab FT060a.

52. The projections showed that Freedom Industries required progress payments to be liquidated at a rate of 84.6%. R4, tab FT060a, Bates 00823. They also confirmed that progress payments would be paid on Freedom Industries' pre-production costs. *Id.* at Bates 00821.

53. The Government invited Freedom Industries to Philadelphia to participate in face-to-face negotiations. Tr. 130-31. DPSC and DCASMA-NY representatives met in New York on November 5, 1984 to prepare for these negotiations. R4, tab FT060e. The Government used Freedom Industries' October 16, 1984 proposal, including its cash flow projections, for these preparations for negotiations. *See* R4, tab FT060d, Bates 00842-60.

Freedom And The Government Reached An Advance Agreement On Treatment Of Costs

54. Freedom Industries and DPSC conducted face-to-face negotiations on November 6, 1984. Tr. 338. These negotiations involved the parties going over Freedom Industries' last proposal line-by-line and agreeing on an amount for each element of cost. Tr. 132.

55. The negotiations resulted in an agreement on the basic terms of a contract for the MRE 5 procurement. The amount that the Government agreed to pay for each element of cost was set forth in a Memorandum of Understanding executed by both parties on November 6, 1984. R4, tab FT062. The specific costs that made up the MOU totals were set forth on a set of final spreadsheets that "back up" the MOU. *Id*; Tr. 133.

56. Freedom Industries' Chief Financial Officer, Patrick Marra ("Marra"), prepared the spreadsheets. The spreadsheets memorialized the parties' agreement that all costs would be treated as direct costs, progress payments would be paid at the rate of 95%, and progress payments would be liquidated at the rate of 82.6%. Tr. 134-36. These spreadsheets were required by the Solicitation and were made a part of Freedom Industries' proposal. *Id.*

57. The elements of cost identified on the MOU tied in directly with the details of those costs on the spreadsheets. Tr. 348. For example, the agreed costs for Manufacturing Overhead in the amount of $3,627,530 and for G&A in the amount of $1,840,824 set forth on the MOU were broken out in painstaking detail on Exhibit 9 of the spreadsheets. R4, tab FT062, Bates 00917; Tr. 348. The spreadsheets showed all of Freedom Industries' anticipated costs and payments on a month by month basis, starting in November 1984, and reflected performance milestones for Freedom Industries. Tr. 338. The cash flow spreadsheets showed how much money Freedom Industries required and when it would need it -- occupancy costs, quality control

equipment, automated building management equipment, salaries, travel costs, office supplies, accounting and legal expenses. *Id.*

58. During negotiations, the parties reached an advance agreement on the treatment of costs for this contract (the "Advance Agreement"). Because the MRE 5 contract would be Freedom Industries' only contract, the parties agreed that all of Freedom Industries' costs would be "direct" costs allocable to this contract, rather than "indirect" costs that would be apportioned among more than one contract by use of a rate or rates. Tr. 190 (Government stipulation that all costs under this contract were direct), 136-37, 140, 388, 1516, 1517-18, 1623-26. *See* R4, tab F25; R4, tab F77, tab F85, tab 75.[9]

59. The Advance Agreement incorporated key elements of Freedom Industries' performance of the contract, all of which were reflected on the final spreadsheets. Progress payments would be paid on all of Freedom Industries' incurred costs at the rate of 95%, up to a projected total of $13,326,175 in progress payments. R4, tab FT062, Bates 00910, 00912; Tr. 136. By increasing the progress payments limitation in Clause L-4 from $9 million to $13 million (after the first two shipments), Freedom Industries' need for outside working capital

[9]Even without the Government's agreement, which Freedom Industries had received, all of Freedom Industries' costs were considered "direct" simply by operation of Section 15 of the DAR Cost Principles. DAR 15-109(f) defined a direct cost as "any cost which is identified specifically with a particular final cost objective . . . . Costs identified specifically with a contract are direct costs of that contract." All of Freedom Industries' costs were identified with a particular cost objective -- the performance of the MRE-5 Contract. Thus, both by negotiation and by operation of Section 15 of the DAR Cost Principles, all costs incurred by Freedom Industries in connection with the MRE-5 contract were confirmed to be "direct" costs.

financing was reduced from $4,061,904 with interest costs of $385,983 (R4, tab FT060a, Bates 00820) to outside financing of $1,798,936 with interest costs of $171,664. R4, tab FT062, Bates 00910 – a savings of more than $200,000 in costs.[10]

60. The costs on which progress payments would be paid included approximately $522,000 in costs often considered to be "capital costs," but which were treated as direct costs for this contract. Tr. 1516-17; R4, tab FT062, Bates 00917. Freedom Industries expressly discussed with the Government that all of these expensed costs could be submitted for progress payments. Tr. 193. This was critical to Freedom Industries because that was the consideration it required to be able to reduce its price, as Captain Parsons had insisted. Tr. 194.

61. The parties also agreed that progress payments would begin in December 1984, although costs for direct materials and direct labor would not be incurred until February and May 1985, respectively. Tr. 191, 340-41; R4, tab FT062, Bates 00910. Freedom Industries told DPSC that it required a substantial pre-production period to prepare the facility for production. Tr. 326, 346. One of the first and most pressing tasks would be to renovate the facility to meet Health Services Command requirements. Tr. 341-42. GFM and CFM could not be accepted until that approval was obtained. *Id.*

62. The 82.6% liquidation rate that was reflected on the spreadsheets (R4, tab FT062,

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[10]These projections by Pat Marra were extremely conservative and worst case. They assumed receipt of progress payments within 30 days and payment to vendors within the same month that the invoice was received. However, if progress payments were received within 5-10 days, as required (R4, tab F2), and vendors agreed to be paid within 40-45 days (as Thomas arranged), the need for outside financing could be almost eliminated. R4, tab FT443 (showing less than $400,000 of 5% financing necessary with projections using these assumptions. These were Freedom Industries' good cash management and best case spreadsheets). Tr. 964-65 (Fishbane opinion that "much less" than $1.8 million in financing necessary with good cash management).

Bates 00912) was discussed and agreed to by the parties. Tr. 134-36, 187. During negotiations, the PCO had informed Freedom Industries that the 82.6% liquidation rate was authorized by DAR based on the contractor's proposed profit rate of 14.8%. Tr. 300. Once Freedom Industries' profit rate was established during final negotiations, the parties consulted DAR Appendix E-512.3 and identified the applicable liquidation rate – which was 82.6%. Tr. 127-28, 188-89, 211-12; R4, tab F114.

63. Freedom Industries made copies of the supporting spreadsheets and provided a copy to the Government negotiating team as required by the terms of the Solicitation. *Id.* On December 13, 1984, Freedom Industries sent a copy of those spreadsheets to the ACO, noting that they reflected sales, costs, profits, and cash flow as negotiated between Freedom Industries and DPSC. R4, tab FT072. Freedom Industries noted its intention to adhere to the projections and suggested that the ACO:

> use the projections as guidance in monitoring our progress on the MRE project and in evaluating the propriety of 'incurred costs' that will be submitted to you monthly for reimbursement as progress payment, determined under the contract.

Id. Indeed, the ACO and DCASMA-NY did use these final negotiated cash flows to gauge Freedom Industries' progress during its performance of this contract. Tr. 1863.

64. The MOU and the supporting spreadsheets for Freedom Industries' proposal became an integral part of the Contract. Tr. 194-95. This understanding is confirmed in Box 18 on the face sheet of the Contract, which states that the Contract "consists of the following documents: (a) the Government's solicitation and your offer, and (b) this award/contract. No further contractual document is necessary." R4, tab 10. The spreadsheets were submitted and

negotiated as part of Freedom Industries' offer, as required by the Solicitation (R4, tab 2, p.74 of 96) and, as indicated in Box 18, comprised part of the Contract.

Freedom Industries Promptly Seeks To Finalize Its Outside Financing

65. Since the final negotiated Contract price of $17,197,928 was substantially less than the $21,583,000 price in Dollar's $7.2 million Commitment Letter, Dollar was no longer legally bound to provide financing to Freedom Industries. Nevertheless, Freedom Industries first turned to Dollar, Freedom Industries' stockholder, to pursue outside financing. On November 8, 1984, Thomas sent a copy of the MOU to Wilmot Wheeler, Chairman of Dollar, confirming that Freedom Industries had agreed with the Government on the terms of an MRE contract. R4, tab FT064. Freedom requested finalization of financing. *Id.*

Contract Award

66. The Government accepted Freedom Industries' offer with all Freedom Industries' conditions and awarded the MRE-5 Contract to Freedom Industries on November 15, 1984. R4, tab10. There was no demand for the withdrawal of conditions that Freedom Industries had experienced on its earlier retort contracts. The contract award documents did, however, amend clause L-4 of the solicitation to increase the "ceiling" on progress payments from $9,000,000 to $13,000,000 *(i.e.,* $9m, with an increase of $2m after each of Freedom Industries' first two deliveries*)*. The contract award did not change the portion of the L-4 provision that required the contracting officer to increase the "ceiling" upon submission to the PCO of cash flows demonstrating a need for an increase.

Liebman Was Familiar With All Of The Government's Negotiations With Freedom Industries

67. Liebman was directly involved in the Government's negotiations with Freedom Industries for the MRE-5 Contract.

68. Specifically, Liebman was responsible for arranging the Government's analysis of Freedom Industries' price proposals. Liebman coordinated the review of Freedom Industries' August 2, 1984 price proposal by DCASR (R4, tab FT047c), and by DCAA (R4, tab FT047b). Tr. 1600-03. Liebman also became the focal point for coordinating the review of Freedom Industries' October 16, 1984 price proposal with its supporting spreadsheets (R4, tab FT060a), by DCAA (R4, tab 11), and by DCASR (R4, tab 19). Tr. 1621-23. At that time, DCASMA and DPSC had copies of Freedom Industries' Lease Agreement with Richard Penzer, which they reviewed, in part, during this briefing session. R4, tab 11, p. 2 ("upon review of the lease agreement . . . ").

69. Liebman even participated in briefing the DPSC negotiating team on November 5, 1984 to prepare the team for final negotiations with Freedom Industries. R4, tab FT060e, tab FT070; Tr. 1628-29. Liebman's group presented the results of both DCASR's analysis of Freedom Industries's October 16 price proposal and DCAA's audit of that price proposal. R4, tab11.

70. Captain Parsons was so impressed with Liebman's presentation as proposal coordinator, he wrote a letter of appreciation to DCASR-NY, in which he complimented the entire staff, but commended only two individuals by name, DCASMA's Commander, Col. Hein, and Liebman. R4, tab FT070.[11]

71. As a result of his involvement in negotiations, Liebman was aware at time of Contract award of all material facts pertaining to Freedom Industries' plans for financing the Contract. Liebman knew that Dollar was only willing to provide a financing commitment to Freedom Industries if it was conditioned on an award of a contract at a specific price. Tr. 1705-1706. He knew that, since Freedom Industries' price had been reduced from the $21,593,000 proposal on which Dollar's Commitment Letter had been conditioned, the Commitment Letter was no longer legally binding. *Id.* Liebman also knew that Freedom Industries had no sources of income other than the MRE-5 Contract. Tr. 1624. Liebman knew that Freedom Industries intended to finance the start-up phase of the MRE-5 Contract with the progress payments provided for in the Solicitation, and that without these payments, Freedom Industries would have to obtain additional outside financing than what was planned. Tr. 1633-34, 1639-41.

72. Liebman also was aware of the parties' Advance Agreement regarding the treatment of costs. Liebman knew that Freedom Industries had included its start-up costs under General and Administrative Costs and Manufacturing Overhead and that these costs were to be expensed to the MRE-5 Contract because it was Freedom Industries' only contract. Tr. 1623-24.

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[11]At trial, Liebman tried to minimize his involvement in this briefing. He claimed that on behalf of DCASMA, Colonel Hein (Liebman's boss), and Colonel Hein's deputy, "ran the show." Tr. 1628. Captain Parson's letter demonstrates that it was Colonel Hein and Liebman who ran the show. R4, tab FT070.

73. Liebman knew that DCAA concurred that these costs – including costs for items that normally would be considered to be "capital" in nature – would be treated as direct costs of the MRE-5 Contract. Tr. 1624; R4, tab 11, p.9. These costs included such items as quality control equipment and supplies, maintenance equipment, building repairs, automated building management and control system, and lockers. *Id.* Liebman also knew that Freedom Industries intended to purchase a computerized job-order costing system to track and identify all costs from receipt of material to finished product. R4, tab11, p.15.

74. Liebman knew that in the pre-award phase, DCAA found Freedom Industries' accounting system to be adequate for all purposes, including progress payments. Tr. 1626-27; 1644-45; R4, tab 11, p. 15.

75. Finally, Liebman was aware of Freedom Industries' exact financial condition at the time of award. Liebman knew that Freedom had a negative net worth and owed creditors (primarily Dollar) several million dollars. R4, tab FT050. He knew that Freedom Industries' performance of the MRE-5 Contract was entirely dependent on the timely payment of 95% progress payments on all costs incurred (other than specified production equipment), which progress payments would be liquidated at a rate of 82.6%. Tr. 299. Liebman also knew that the progress payments were to be paid to Freedom Industries for costs incurred from the beginning of the Contract, notwithstanding that it would be several months before Freedom Industries would incur costs for direct materials and direct labor. R4, tab FT0060a, Bates 00820; tab FT062, Bates 00910.

Liebman Did Not Like Or Trust Thomas, And He Refused To Administer The Contract As Negotiated

76. Liebman served as the ACO for Freedom Industries' MRE 3 retort contracts. Tr. 71. Liebman caused Freedom Industries to be defaulted for reasons that DPSC quickly determined were without basis. Tr. 98-99. DPSC reprocured the same contracts back to Freedom Industries the following day. *Id.*

77. Liebman considered Thomas to be an unethical business man who obtained the MRE-5 Contract through political pull, rather than because it was in the legitimate interests of the United States to establish a third MRE supplier. Liebman told a Government investigator in March 1987 that:

> Thomas is a shrewd businessman, wheeler dealer. He believes he can do anything he wants. He feels he can get away with the violation of normal business practices and government regulations. He feels that through the use of political clout he can get whatever he wants. . . . [H]e (Henry) had a 'godfather' who wanted him to get a contract. There were Congressmen (especially Congressman Addabbo) and state politicians that I believe put pressure on DLA Headquarters' general officers to put Henry (minority South Bronx) in business.

R4, tab FT338, Bates 02342.

78. Liebman's views were unfounded and prejudicial. Freedom Industries received an MRE 5 award because it was the intention of the parties to establish a third planned producer on a warm base, because it was in the best interests of the United States to establish this third source of MREs, and because Freedom Industries met all of the Government's rigid requirements to qualify as an MRE assembler. R4, tab FT028, tab F7. Thomas had no special relationship or political "pull" with any elected officials. Tr. 260. Any concern expressed by elected officials, such as

Congressman Joseph Addabo, then Chairman of the Armed Services Appropriations Committee, about awarding a contract to Freedom Industries related to a legitimate concern over the adequacy of food supplies for national defense in the event of a national emergency or declaration of war, and not political patronage. Tr. 260-61.

79. Liebman's prejudiced views echoed those of his superiors. For example, during a meeting on June 19, 1985 with Freedom Industries, Julius Wrubel, DCASMA Chief Financial Analyst, disdainfully referred to progress payments as "hand-outs," rather than as the Government's preferred form of financing that they truly were. R4, tab F084, p.2, Tr. 1768. Freedom Industries objected to the prejudiced overtones of Wrubel's remark. *Id.*

80. The DCAA-NY team that was appointed after Contract award to audit Freedom Industries' progress payment requests, as led by auditor Guy Sansone, also held a severe bias against Freedom Industries and its black owner, Thomas. DCAA returned every Freedom Industries progress payment request between November 1984 and December 1985 unaudited, or with a recommended payment of $0. *See* R4, tab F21 (Freedom Industries PP#1), tab 15 (Freedom Industries PP#1Resub), tab 21 (Freedom Industries PP#1Resub), tab F41 (Freedom Industries PP#2), tab 49 (Freedom Industries PP#3), tab FT422 (HT PP#1), tab 54 (PP#2), tab FT422 (PP#3), tab 60 (PP#4), tab 66 (PP#6), tab 76 (PP#7)("We do not recognize the costs claimed for Progress Payments under the present terms of the Contract") and tab 80 (PP#8). DCAA's first recommendation of any payment did not occur until Progress Payment #9. R4, tab FT422. Even then, the recommendation was made only after a high level DCAA auditor from Washington D.C. met with the New York auditors and told them that they were wrong in refusing to approve progress payments. Tr. 795-96; 1785.

81. On February 26, 1985, DCAA issued a Report on Contractor in Financial Jeopardy, in which the New York auditors further revealed their bias against Freedom Industries. R4, tab 35. Essentially, DCAA believed that Freedom Industries never should have received an MRE 5 award. The report emphasized that an award had been made to Freedom Industries over DCAA's objections about Freedom Industries' "financial instability." *Id.* at p.1. DCAA repeated its erroneous assertions that Freedom Industries was not entitled to progress payments until production of the MRE product began and that costs incurred before production were "indirect in nature and not necessarily related to the progress of contract performance." *Id.* The report further speculated "how Freedom Industries will be able to finance the contract until such time as they qualify for progress payments." *Id.* at p.2. DCAA ignored DPSC's agreement to provide working capital for Freedom Industries through progress payments, claiming that "Freedom Industries does not have the financial capability to perform the contract and is now looking to the Government for the necessary working capital to remain in business." *Id.* at p.1.

82. DCAA also created a baseless fear about Freedom Industries' creditors, claiming, without support, that "any monies received by Freedom Industries and deposited to a Freedom account would most likely be attached by the creditors who have judgements [sic], etc." *Id.* DCAA impugned Freedom's honesty, claiming that, "To avoid this, Freedom is trying to establish various obstacles to delay and circumvent paying the creditors . . . . " *Id.*

83. DCAA gratuitously and inaccurately reported on matters that were reviewed and decided upon during the negotiation of the MRE 5 contract. *Id.* at pp.3-4. After reviewing the

same information that DPSC analyzed before awarding a contract to Freedom Industries, DCAA now concluded: "In our opinion, the contractor cannot perform this contract based on its current financial position." *Id.* at p. 4. Moreover, DCAA slandered Freedom Industries, stating that:

> We recommend that the Government exercise extreme caution in its consideration of any financial arrangements with Freedom especially since the practices employed by the contractor are designed to deliberately delay and circumvent existing obligation to it's [sic] creditors.

Id.

84. DCAA's bias against Freedom Industries reinforced Liebman's prejudices. Liebman relied principally on DCAA's reports to justify his own refusals to pay progress payments to Freedom Industries. Tr. 1783. Liebman relied entirely on DCAA's declaration of an inadequate accounting system to suspend progress payments (for a second time) on August 23, 1985. Tr. 1839-40.

85. It appeared to Jordan Fishbane, an expert witness for Freedom Industries concerning all of the financial aspects of this case, that Liebman and DCAA "went out of their way not to pay" Freedom Industries' progress payments. Tr. 968-99. They ignored the spreadsheets that were incorporated into the contract; they used trite reasons as a basis for not paying progress payment requests at all, rather than pay as much as possible for each request; they disregarded previous DCAA findings that determined that Freedom Industries's accounting system was adequate. *Id.* Fishbane believes that these actions amounted to collusion. *Id.*

Liebman Develops A Campaign To Eliminate Freedom Industries From The IPP; In Order To Stifle Cash Flow, The Lifeblood Of Any Contractor, Liebman Wrongfully Refuses To Pay Progress Payments And Abuses The Audit Process

86. Because of the prejudicial opinions that Liebman and DCAA held against Thomas and Freedom Industries, Liebman decided to avoid paying Freedom Industries any progress payments. Through a series of feints and excuses, Liebman successfully avoided paying Freedom Industries a single penny in progress payments until May 6, 1985. R4, tab FT422 (PP Chart). These actions are described below.

Liebman Intentionally Delays The Processing Of Progress Payment No. 1

87. Freedom Industries hand delivered its first progress payment request to Liebman on November 16, 1984, the day after Freedom Industries received the award of the MRE-5 Contract. Tr. 369-70, 385. Freedom Industries requested payment for $100,310, representing 95% of the costs it had incurred for rent and real estate taxes. R4, tab FT422 (Freedom PP#1,A). These costs were reasonable, allowable, and allocable to the Contract, and Liebman should have paid this request within 5-10 days. R4, tab F2.

88. Liebman refused to accept the request, claiming that he had not yet received the formal Contract. Tr. 369. Thomas, however, had a duplicate copy of the Contract with him and gave it to Liebman with the progress payment request. *Id.* Nevertheless, Liebman still insisted that he could not process the progress payment request until he received the Contract through "official channels." Tr. 369-70. Freedom had no choice but to leave the Contract and the progress payment request with Liebman and ask him to process it promptly. *Id.*

89. Liebman finally acknowledged formal receipt of the Contract and, therefore, formal receipt of the progress payment request on November 29, 1984. Rule 4, tab F20; Tr. 386. This action alone caused a two-week delay in payment.

90. Liebman did not pay within 5-10 days of submitting Progress Payment No. 1, as expected. R4, tab F2. Instead, Liebman held the request "in abeyance" and ordered a pre-payment audit. R4, tab F22; Tr. 386, 1646-47. Liebman expected that "final action will be accomplished on or about 21 December 1984," an unnecessary delay of another three weeks beyond the proper 5-10 day payment date. R4, tab F20.

91. Liebman claimed that a pre-payment audit was necessary to test the adequacy of Freedom Industries' accounting system. Tr. 1509. This was untrue; a pre-payment audit was unnecessary. Liebman was aware that DCAA had declared Freedom Industries' accounting system to be adequate "for all purposes" less than two weeks earlier in connection with DCAA's review of Freedom Industries' October 16, 1984 price proposal. R4, tab11, pp.3,16, Tr. 1644-45. Liebman also was aware that the DLA required an ACO to consider whether a pre-award survey had been recently performed before deciding to audit progress payments. Tr. 1614. Liebman knew that when an accounting system and controls are deemed adequate based on a positive pre-award survey, normally there should be no audit of the first progress payment, according to the DLAM. Tr. 1615-16, 1648-49.

92. Freedom Industries' first progress payment request was only for rent and taxes. Tr. 422. Freedom Industries called Liebman when it entered into the MOU on November 6, 1984 and told Liebman that Freedom Industries would be submitting a request for payment of rental costs when the contract was signed. Tr. 1668-69.

93. Liebman knew from his review of Freedom Industries' cash flow spreadsheet that Freedom Industries would be incurring only building renovation and occupancy costs during the first four or five months of the Contract. Tr. 1743. Freedom Industries did so and submitted complete supporting documentation for these costs. Tr. 394. Liebman could have performed a desk audit. *Id.*

94. Liebman had no rational basis to delay payment on Progress Payment No. 1 so that DCAA could perform an audit. Liebman admitted at trial that when ordering a pre-payment review, the ACO must document the contract file with his rationale. Tr. 1652. No such rationale exists in the record, and Liebman could not recall at trial whether he ever did so. Tr. 1652-53.

Liebman Wrongfully Ordered Pre-Payment Audits Of All Of Freedom Industries' Progress Payments, Knowing That DCAA Would Recommend That Nothing Be Paid

95. Liebman wrongfully subjected Freedom Industries to consistent pre-payment audits. Tr. 1661. Under the DAR and DLAM, reviews after the first progress payment request are limited to circumstances where either: (1) the ACO has reason to doubt the contractor's certification; or (2) the ACO believes it will be a loss contract. DAR Appendix E-520; DLAM 32.590-5b[12]; Tr. 1661-62. Although Liebman knew that the DLAM required him to document

[12]Throughout these proceedings, both parties have cited to the December 1984 DLAM as the document upon which Liebman relied in administering the MRE-5 Contract. The Government not only produced this version of the DLAM during discovery, but the Government submitted into evidence portions of that version at trial before Judge Grossbaum. Based upon these representations by the Government, and having been unable to locate a copy of the DLAM in effect immediately prior to the December 1984 DLAM, all references to the DLAM in this Brief are to the December 1984 version of that document.

the file with his rationale any time he ordered a pre-payment audit after the first request (Tr. 1662), the record is devoid of any such documentation.

96. Beginning with Freedom Industries' very first request, the New York office of DCAA wrongfully concluded that no progress payments could be paid to Freedom Industries until it made physical progress on the contract, *i.e.*, began production of the MREs. R4, tab F21. Accordingly, DCAA refused to recommend payment of any of Freedom Industries' progress payment requests. R4, tab 15. Liebman testified that he knew that DCAA's position was consistently wrong. Tr. 1719-20, 1777-1778, 1783. Nevertheless, Liebman continued to send Freedom Industries' requests to DCAA for audit, knowing full well that DCAA would recommend payment of $0. Tr. 387.

97. Liebman admitted at trial that Freedom Industries began making progress on the Contract immediately after award. Tr. 388-89, 1885. Thus, while Liebman delayed paying Freedom Industries, Freedom Industries properly was incurring reasonable costs.[13] During the first week of December 1984, Freedom Industries asked Liebman how to handle the submission of its second progress payment request, since the first request still had not been paid. Tr. 390. Liebman told Freedom Industries to withdraw its first progress payment request, combine the two requests into one, and resubmit the request. Tr. 1658-59.

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[13]The fact that these costs were proper is demonstrated by the fact that Liebman finally paid them on May 6, 1985. Tr. 1694; R4, tab FT422. By then, however, the damage had been done – Freedom Industries received this first payment only one month before Freedom Industries was scheduled to begin *making deliveries of MREs*. R4, tab FT062.

98. In doing so, Liebman admits that he lengthened the time for payment of the original progress payment request. Tr. 1659; R4, tab FT074, tab 15. Liebman, however, did not inform Freedom Industries that this procedure would delay payment of its initial costs.

99. Freedom Industries followed Liebman's instructions. On December 7, 1984, Freedom Industries resubmitted its first progress payment, requesting payment of $252,150 on total costs incurred of $265,421. R4, tab FT422(PP#1(Resub)). Liebman deemed the original request to be withdrawn. R4, tab FT095. Officially, Liebman attempted to hide any responsibility for this delay. When reporting that Freedom Industries withdrew its original request, Liebman carefully avoided noting that Freedom Industries did so at Liebman's suggestion. R4, tab FT095.

Liebman Pretends Falsely To Be Uncertain About The Direct Nature Of Freedom Industries' Costs In Order To Delay Paying Freedom Industries

100. On December 7, 1984, DCAA responded to Liebman's request to audit Freedom Industries' first progress payment request. DCAA returned the progress payment without auditing it, claiming that it "is requesting monies for costs which are indirect in nature." F21. DCAA was taking the position that progress payments were not authorized until "direct" costs were incurred, *i.e.*, until actual production of the product began. Tr. 1673.

101. Liebman admitted at the trial that DCAA was wrong. Tr. 1719-20, 1778. He testified that, under general cost accounting principles, all costs are direct when a contractor has only one contract. Tr. 1672, 1685. He admitted that, in connection with Freedom Industries' Contract, he was aware that these costs had been expressly negotiated as direct. Tr. 1623-26.

102. Liebman testified that he knew that he had the authority to overrule DCAA's conclusion and declare Freedom Industries progress payment request as being valid for payment. Tr. 1784. Nevertheless, he did not do so.

103. Liebman received advice from legal counsel during that time period confirming that all costs were negotiated as direct and that progress payments should be made. Liebman spoke by telephone with legal counsel, Deputy Counsel Carl Heringer, DCASR-NY, on December 6 and 7, and met with him in person on December 7, to discuss this issue. R4, tab F22. Liebman admitted at trial that as a result of these conversations, he understood that all of Freedom Industries' costs were to be considered direct. Tr. 1723. According to Liebman, "The issue was dead before [Heringer] issued his [written] legal opinion." *Id.*

104. Nevertheless, on December 10, 1984, Liebman required Heringer to do precisely that – issue a formal, written legal opinion about this matter. R4, tab F22. Liebman should have admitted then, as he did at trial, that he actually was clear on this issue, and he should have paid Freedom Industries. Instead, Liebman allowed Heringer to continue with the needless exercise of investigating and issuing a formal legal opinion.

105. Several days later, Liebman again unnecessarily delayed resolution of this issue. A Post-Award Conference was scheduled with Freedom Industries for Friday, December 14, 1984. R4, tab FT073, tab FT074, tab 15. On the day before that meeting, Thursday, December 13, 1984, Liebman conducted a meeting of DPSC and DCASMA representatives to prepare for the Post-Award Conference. *Id.* Liebman chaired the meeting. Heringer again advised Liebman that all costs were negotiated as direct and subject to progress payments. R4, tab FT074, Bates 00961. Liebman insisted that the Government representatives avoid disagreements at the Post-

Award Conference and speak with one voice (*i.e.*, his); and he announced that "as ACO, he had the final responsibility for determining if a Progress Payment was payable." R4, tab FT074, Bates 00960, 00961.

106. Freedom Industries' urgent need for progress payments to pay its rent required that this issue be resolved at once. Nevertheless, Liebman deferred decision on the issue of payment and instructed those present simply to advise Freedom Industries the next day that "payment was under consideration." R4, tab FT074.

107. No reasonable conclusion can be drawn from this action but that Liebman intentionally deferred making this decision in order to further delay in making any payment to Freedom Industries.

108. On December 14, 1984, Freedom Industries resubmitted Progress Payment No. 1. Liebman rejected Freedom Industries' resubmitted progress payment request twice (Tr. 1674-75) for insufficient and petty reasons. Liebman rejected the request on December 18, 1984 (R4, tab 12) for ridiculous reasons. For example, Liebman stated that Freedom Industries had incorrectly referred to the total contract price as $17,197,928, instead of $17,197,929, explaining that "all amounts ending in cents must be rounded to the next dollar (example: $3.01 becomes $4.00)." *Id.* Liebman objected that Freedom Industries had left blanks and inserted "-------" instead of using "0"s. *Id.* Liebman also instructed Freedom Industries to include a 95% liquidation rate, instead of the 82.6% rate that was negotiated with DPSC, incorporated on the spreadsheets that were a part of the Contract, and included in the payment request. *Id.*

109. DCAA performed an audit of Resubmitted Progress Payment No. 1 and reported its finding to Liebman on December 20, 1984. R4, tab 15; Tr. 1689. DCAA recommended that

$0 be paid. R4, tab 15. Liebman testified that the reasons for DCAA's conclusions were not a valid basis for rejecting progress payment requests. Tr. 1690-92. For example, DCAA recommended that salary costs not be paid because there was "no evidence that the contractor has paid or will pay these salaries." *Id.* Liebman agreed that this contradicted the progress payment regulations that required only the incurrence of costs by Freedom Industries. Tr. 1690. DCAA also complained about all of the costs being "unbooked," claiming that Freedom Industries did not provide books of account during the audit. R4, tab 15. In fact, DCAA did not ask to review Freedom Industries' books during the audit. Tr. 445. When Freedom Industries learned of DCAA's claim of unbooked costs, Freedom Industries immediately carried the company's books to Liebman in a snowstorm. *Id.* DCAA performed another audit and admitted that Freedom Industries' costs were, in fact, recorded on the company's books. Tr. 1697; R4, tab 21.

110. In the meantime, Heringer further investigated the factual basis for his legal opinion. On December 18, 1984, Heringer and DPSC's counsel, Chuck Wright, called DPSC and confirmed (again) that all costs had been negotiated as direct costs. R4, tab FT078. Wright agreed with Heringer that there was no legal impediment to considering all costs as direct and paying progress payments, provided that "some progress has been shown." R4, tab F28. Accordingly, on December 27, 1984, Heringer issued his legal opinion to Liebman, confirming that Freedom Industries needed its money, that all Freedom Industries' costs were direct for purposes of this Contract according to the DAR and as agreed upon in the negotiations, and that Freedom Industries should be paid progress payments on those costs. R4, tab F25.

When Liebman No Longer Could Defer Action On Freedom Industries' Progress Payment Request, Liebman Contrives A Proposed Suspension Of Progress Payments To Freedom Industries

111. The formal written legal opinion stripped Liebman of the excuse he had been using up to that point to delay progress payments to Freedom Industries. Liebman now was forced to find another reason to deny payments to Freedom Industries, and he did so. Liebman proposed suspending progress payments to Freedom Industries.[14]

112. Liebman testified that at the time he received Heringer's December 28 letter, he was not even considering suspension of progress payments. Tr. 1738. He said he first began considering suspension during the New Year's holiday (Tr. 1735), *right after he received Heringer's letter*. Tr. 1739-40, 1730. Upon returning from the holiday, Liebman called an emergency meeting of the Government Review Board that must be convened to approve proposed suspensions. Tr. 1739. Ordinarily, it takes time to convene such a board, but Liebman went around personally to gather the Board members on the day after he returned from the New Year's holiday for a "hurry-up meeting" so that he could propose suspension. *Id.*

113. Without the benefit of Freedom Industries' position, Liebman received approval from the Board to suspend progress payments. Tr. 1503, 1504.

114. Liebman did not contact Freedom Industries first to say that he intended to propose a suspension, or how Freedom Industries could prevent such action from being taken. Tr. 1727, 1738-39. Liebman simply sent a letter to Freedom Industries on January 4, 1985 (the "Proposed Suspension Letter") stating that he was considering returning Freedom Industries'

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[14]Since Liebman had not yet paid any progress payments to Freedom Industries, Liebman's action merely formalized the *de facto* suspension he already had imposed on the contractor.

progress payment request unpaid and suspending progress payments. *Id.*; R4, tab 16. The Proposed Suspension Letter set forth three reasons for the proposed suspension: (1) a claim that Freedom Industries was in unsatisfactory financial condition because Dollar purportedly changed the terms of its commitment from the August 9 and 10 commitment letters; (2) several minor issues identified by DCAA during their audit; and (3) a claim that Freedom Industries had not made physical progress on the Contract (*i.e.*, the old argument that Freedom Industries had not begun production). R4, tab R16.[15]

115. At trial, Liebman testified that the first reason, concerning Freedom Industries' financial condition, was the only reason for the proposed suspension. Tr. 1702. Liebman now concedes that the second and third reasons, although included in the letter, were not reasons that would support suspension. Tr. 1687-88, 1740-41.[16] As explained below, Liebman's first (and, according to Liebman, only) reason also was completely devoid of merit and revealed that Liebman's true intention was to avoid payment to Freedom Industries.

Liebman's Professed Concern About Dollar's Willingness To Provide Financing Was Invented To Deliberately Harm Freedom Industries

116. The Proposed Suspension Letter set forth only one reason why Liebman considered Freedom Industries to be in "unsatisfactory condition":

> Specifically, Dollar Dry Dock Commercial, which committed itself to extend Freedom Industries credit in the performance of the contract, has stated that no credit will be forthcoming until such

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[15]The reasons Liebman gave were the same as the ones given by DCAA in their audit report. Tr. 1690.

[16]Indeed, Liebman admitted at trial that some of these reasons contradict the DAR (*e.g.*, refusal to pay progress payments because of no proof that salaries have been paid violates progress payment clause requirement to pay on costs *incurred*). Tr. 1690.

> time as an 'arrangement' is in place to settle the amounts owed by Freedom Industries to creditors for debts incurred prior to the subject contract. (See copy of my letter (attached), dated 4 January 1985, to Mr. Noel Siegert, Dollar Dry Dock). [R4, tab17]

R4, tab 16.

117. Liebman contended that he first learned of this professed concern during a December 17, 1984 phone call with Dollar. R4, tab FT095; tab FT338.[17] He claimed that by requesting a plan to pay off creditors, Dollar was imposing conditions that contradicted Dollar's Commitment Letters of August 9 and 10, 1984, on which the Government "relied" in making an award. *Id.*

118. Liebman misinformed Government personnel about the December 17th call. He told them that Dollar had "withdrawn" its August 9, 1984 commitment letter, leaving Freedom Industries without financing. R4, tab 25. In fact, Liebman went so far as to report that Dollar had withdrawn its "$7 million line of credit . . . *prior to award* of contract, leaving contractor insolvent and without source of credit." R4, tab F182, p.41(10/10/86 Liebman Memo re: MRE 7 pre-award survey). That Liebman was successful in damaging Freedom Industries is evidenced by Colonel Holland's investigative report in 1987. After hearing from Liebman, Colonel Holland

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[17]On December 17, 1984, four Government representatives called Noel Siegert, the Senior Vice President and Loan Officer at Dollar, to question him about Freedom Industries' financing. The Government representatives were Leonard Gutfleisch, Deputy Commander, DCASMA-NY; Samuel Stern, Chief, Contract Management Division, DCASMA-NY; Liebman; and Heringer, Deputy Counsel, DCASR-NY. R4, tab 17. The call took place without warning to Dollar, and without notice to, or the permission of, Freedom Industries. The evidence suggests not only that such a call was improper, but that Liebman scared off Dollar by discussing $7.2 million of financing for the $17 million contract and stating that progress payments would not be made until direct costs are incurred many months into the contract. Tr. 436-39. In Liebman's subsequent dealings with Freedom Industries, Liebman did not inform Freedom Industries that he had spoken with Dollar. Tr. 426.

concluded:

> The bottom line is it appears that Henry Thomas did not have any financing from Dollary Drydock or any other viable creditor at the time of the contract award and that he falsely represented his position to the government of having sufficient financial backing for an award of this size.

R4, tab FT338, Bates 02344.

119. Freedom Industries was awarded a contract with everybody's knowledge -- DPSC's, DCASMA's, Dollar's, and Freedom Industries' -- that the Dollar Commitment Letter was not binding in connection with the award of a $17 million contract. Its importance for purposes of finding Freedom Industries to be a responsible contractor was that it demonstrated that Freedom Industries had the *ability to obtain financing*, not that financing was necessarily in place at the time of the award. DAR 1-903, Minimum Standards for Responsible Prospective Contractors. Yet, Liebman insisted that the basis for suspension was the Government's professed surprise that financing was not already in place at the time of the award. Tr. 1707, 1737; R4, tab F182, p.41.

120. At trial, Liebman admitted that Dollar's request that an "arrangement" be put in place to pay creditors did ***not*** constitute a "withdrawal" of the commitment letter. Tr. 1753-54.

121. Furthermore, Liebman admitted at trial that he did ***not*** first learn of Dollar's desire to have an arrangement in place for creditors from Dollar, as he claimed in his official reports at the time. Indeed, it was Freedom Industries that explained this fact at the Post-Award Conference -- three days **before** Liebman's December 17th call to Dollar. Tr. 1707-09.[18]

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[18]Freedom Industries had learned that Dollar was having financial difficulties. Tr. 412-13. Thomas explained this to Liebman and gave Liebman a copy of the newspaper article he had read about these problems. *Id.*, R4, tab FT73, Bates 00959. Freedom Industries still could have

Freedom Industries also stated that it was considering using a different source of financing than Dollar to finance the contract, including Broadway Bank and/or H.T. Food Products, Inc. ("HT Foods"). *Id.*

122. Freedom Industries provided Liebman with information concerning potential sources of outside financing by letter dated December 26, 1984. R4, tab 13. Freedom Industries specified the precise amount of financing that it believed it would require, $415,000, and the intended sources of that financing. *Id.*

123. Liebman admitted at trial that he did not investigate the sources that Freedom Industries provided and did not know at the time he issued the January 4 Proposed Suspension Letter whether the sources were valid. Tr. 1736-37. Liebman also admitted he did not even tell Freedom Industries that it needed to *provide* proof positive of financing to avoid suspension. Tr. 1738.

124. In Heringer's opinion letter, which was issued after the December 17th call in which he participated, Heringer noted that there had been no change in Freedom Industries' financial position:

> As has been noted in the Government's post award conference, ***and subsequent meetings***, there has apparently been no change in the contractors [sic] financial position from the time of the award of the contract to the present. This should be taken into account by the ACO in weighing any financial basis for non-payment of the progress payment.

R4, tab F25 (emphasis added).

125. No reason existed for the Proposed Suspension Letter other than to intentionally

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obtained financing from Dollar, but Freedom Industries now was considering using Broadway Bank instead. Tr. 412.

delay making any progress payments to Freedom Industries.

Freedom Industries Promptly Protests The Proposed Suspension Letter And Demonstrates That No Basis Existed For The Proposed Suspension

126. Liebman hand-delivered the Proposed Suspension Letter to Freedom Industries on January 10, 1985. R4, tab 26. Freedom Industries responded in writing on January 18, 1985, refuting the claims in the Proposed Suspension Letter and submitting a packet of alternate sources of financing. R4, tab 22; Tr. 1755.

127. Freedom Industries had many other sources of contract financing available. These lenders sought to contact Liebman to confirm that progress payments would be forthcoming if the Lenders provided financing.[19] However, Liebman made sure that this proposed financing would be unavailable by refusing to confirm that progress payments would be paid promptly and by refusing to accept financing from any source other than a financial institution.

Wrongful Interference

128. Freedom Industries had arranged for the availability of financing from other banks and from private investors, including Broadway Bank, Richard Penzer, Zev Robbins, and

[19]Such a precaution was particularly well-advised in light of Liebman's refusal to pay any progress payments to date.

Citibank. Liebman deliberately interfered with Freedom Industries' financing from these sources. Indeed, Liebman first was responsible for driving Dollar away from its dedicated financial support of Freedom Industries.

129. Dollar was Freedom Industries' first choice for financing. Tr. 353-54. On November 8, 1984, Freedom Industries wrote to Dollar's Chairman, enclosing a copy of the MOU and the final cash flow projections supporting the MRE contract, and requested "that finalized bank financing be solidified rapidly." R4, tab FT064.

130. Just before the award of the Contract, Freedom Industries informed Dollar that it would be submitting a progress payment request for $100,000 which should be paid in a short time frame. Tr. 357-58. Freedom Industries expected that payment of this request would allay Dollar's concerns about the Government's role in providing financing for the Contract. *Id.*

131. At the same time, Dollar's proposed interest rate was exceedingly high. In order to be able to negotiate a lower rate, Freedom Industries wanted to determine whether alternative, less expensive financing was available. Tr. 356. Freedom Industries also had concerns about Dollar's financial condition. R4, tab FT037, Bates 00959.

132. Freedom Industries consulted with other potential lenders. They included: (1) Broadway Bank, which had financed Freedom Industries' school lunch business in Paterson, New Jersey (Tr. 356, 359); (2) Zev Robbins, who had been interested in investing in Freedom Industries since MRE 3, and who was willing to provide financing at a lower interest rate than Dollar (Tr. 356); (3) Clarence Stanley, a loan officer at Citibank, which had loaned Freedom Industries money for the school lunch program, and also expressed an interest in providing financing (Tr. 359); and Richard Penzer, the owner of Freedom Industries' building. Tr. 360.

133. Liebman scuttled Freedom Industries' ability to obtain financing from Dollar. During Liebman's December 17 call to Dollar (Finding 117), Liebman asked Siegert about Dollar's continued willingness to provide $7.2 million in financing (R4, tab 17; Tr. 448-50), and Liebman told Siegert that progress payments would not be paid until direct labor and direct material costs would be incurred a number of months into the Contract. Tr. 449-50.

134. After the phone call by Liebman, Dollar began to reconsider its willingness to finance the MRE-5 Contract. Tr. 424-25.

135. Dollar became reluctant to provide financing to Freedom Industries only after Liebman: (1) failed to pay Freedom Industries' first progress payment; and (2) called Dollar and incorrectly represented that the Government still expected Dollar to provide $7.2 million in financing and that progress payments would not be paid until many months into the contract.

Liebman Interfered with Freedom Industries' Alternative Lenders

136. As Freedom Industries explained to Liebman on December 14, 1984, whether Dollar was available or not at that point was unimportant -- financing was available from Broadway Bank and others. Tr. 450. Broadway Bank offered a favorable interest rate (Tr. 451), and Freedom Industries' attorney, Dante Alberi, drafted a Notice of Assignment (R4, tab FT087) to formalize the financing with Broadway Bank. Tr. 451-52.

137. In mid-January 1985, Thomas met with Dick Lanza at Broadway Bank to execute the financing documents. Tr. 451, 453. Lanza already had reviewed the final Freedom Industries negotiated cash flows and other information. Tr. 452. Lanza asked for Government confirmation that the information he had received from Freedom Industries regarding cash flows, *i.e.*, progress payments was valid. *Id.*

138. Thomas called Liebman with Lanza from Lanza's office. *Id.* Thomas told Liebman that he was at Broadway Bank and that Thomas wanted Liebman to confirm the cash flows for the benefit of Broadway Bank. *Id.* Liebman refused to do so. *Id.* Thomas was humiliated. *Id.* As a result of Liebman's refusal to cooperate with the contractor's reasonable request, Freedom Industries was unable to obtain financing from Broadway Bank. Tr. 453.

139. Freedom Industries had similar experiences with Liebman in connection with its other sources of financing. The owner of Freedom Industries' facility, Mr. Penzer, was a successful, wealthy real estate developer. Tr. 799-800. Before Penzer leased the Bronxdale Avenue facility to HT Foods in September 1984,[20] Penzer investigated Freedom Industries' claims that it was party to a Government contract. Tr. 801-02. Penzer called Philadelphia and Washington and spoke with high level officials, who confirmed that the Government would be paying the rent and all related occupancy costs every month, on a net, net lease basis. Tr. 802-03. Penzer leased the facility to Freedom Industries in reliance on the Government's representations. Tr. 803.

140. Thomas later approached Penzer and asked if he would be willing to provide equipment financing and working capital financing. Tr. 804-05. Penzer had advanced funds "many times" to other commercial tenants, large and small, for many different purposes. Tr. 805. Penzer was willing to provide financing to Thomas. Tr. 811-12. Liebman, however, was not

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[20]The contractor arranged to obtain use of the facility through a sublease from HT Foods. Penzer leased the facility to HT Foods on September 12, 1984. R4, tab FT052. The lease acknowledged that HT Foods intended to sublease the facility to Freedom Industries. *Id.*, Bates 00740. On September 14, 1984, HT Foods subleased the facility to Freedom Industries. R4, tab FT054. This arrangement assisted in protecting the MRE-5 Contract from claims by Freedom Industries' past creditors.

paying progress payments at the time, and Penzer was not being paid his rent and occupancy costs. Tr. 807-08. Penzer went to the facility dozens of times and complained to Thomas about the unpaid rent. Tr. 808. Penzer called Liebman direct numerous times and asked to be paid. Tr. 808, 810.

141. Penzer told Liebman that he would be willing to lend money to Freedom Industries. Tr. 810. Liebman, however, refused to accept financing from a "private person." Tr. 810-11 (Liebman "wouldn't accept it. . . . He wanted a bank"). Penzer made one last attempt to obtain Liebman's approval. Tr. 816-17. Penzer offered to deposit his funds into Chemical Bank and have Chemical Bank involved in the loan process. *Id.* Penzer had Chemical Bank bankers call Liebman. Tr. 817. Nevetheless, Liebman refused to respond to these overtures. Tr. 817.

142. Penzer was so frustrated with Liebman that he decided to sell the building. Tr. 808-09. The lease had a clause in it that granted HT Foods an option to purchase the building. R4, tab FT052, Bates 00739-40. Penzer paid HT Foods $400,000 for its option in order to enable Penzer to sell the building to a third party for approximately $5.5-$6 million. Tr. 819. The purchase of the option was an independent transaction. Tr. 824. Penzer never forgave any rental payments that HT Foods owed him. *Id.*

143. Thomas had the same experience with another private investor. Thomas also approached Mr. Robbins about providing $2-$2.5 million of financing for the Contract. Tr. 863-64. Robbins was a wealthy entrepreneur who had financed Freedom Industries' acquisition of retort equipment for MRE 3. Tr. 854-861. In 1984, Robbins was looking to invest the substantial proceeds he had received from the sale of a business. Tr. 861-62. Robbins reviewed the cash flow projections that Freedom Industries had negotiated with DPSC. Tr. 862.63. After

being satisfied that the projections were reasonable, Robbins told Thomas that he required confirmation from Liebman that the contract would be administered in accordance with the cash flow projections. Tr. 864.

144. Thomas arranged a conference call with Liebman. Tr. 864-65. Liebman asked if Robbins was a bank. *Id.* Robbins said that he was not, but that he was an investor with a sizeable amount of money that he was interested in investing in Freedom Industries. *Id.* Liebman said that he was not interested in Robbins if he was not a bank. According to Robbins, "That was it. He did not want to speak to me as an individual." *Id.*

145. Robbins was prepared to immediately withdraw his offer to finance Freedom Industries. Tr. 866. At Thomas's suggestion, however, Robbins agreed to deposit his funds into Citibank (where Freedom Industries banked), if that would cause Liebman to confirm Freedom Industries' eligibility for progress payments. Tr. 867.

146. Thomas arranged for Citibank's branch manager, Clarence Stanley, to meet with Liebman. Tr. 879, 468. Thomas explained the reason for his visit was that he wanted Liebman to confirm to Stanley that the Government would be paying 95% progress payments on Freedom Industries' costs. Tr. 468-69.

147. Liebman refused to confirm that Freedom Industries was even eligible for progress payments. Tr. 882, 468-69.

148. The Government does not dispute that these calls and meetings with Freedom Industries' potential lenders occurred. On the contrary, Liebman conceded at trial that he was receiving calls during this time period from possible financing sources, including a financial

institution and vendors. Tr. 1746. Liebman also recalled that Freedom Industries was seeking financing from private investors at the time. Tr. 1757-58.[21]

Freedom Industries Continued To Perform

149. Despite Liebman's interference, Freedom Industries continued to perform the Contract to the best of its ability. R4, tab F39.

150. Freedom Industries was negotiating for the purchase or lease of high-tech assembly equipment, either from Koch Multivac or T.W. Kutter. *Id.* Freedom Industries had already agreed to purchase 12 Doboy Model Continuous Band Sealers, plus conveyors from S&B Conveyor Company, equipment that alone would cost $1,000,000. *Id.*; R4, tab FT086.

151. Freedom Industries prepared and submitted a Plan for Inspection Job to the Veterinary Service, detailing Freedom Industries' proposed procedures for inspecting all aspects of its production operation. *Id.*[22] Also, Freedom Industries "had scheduled to steam clean and paint the entire production area beginning February 1, 1985. *Id.*

152. These efforts cost money -- money that the Government had agreed to pay as progress payments. At that time, Liebman had not made a single payment to Freedom Industries. R4, tab FT422(PPChart). Instead, Penzer was financing all of the rent and related costs, such as taxes, electric, heat, insurance, and guard services. Tr. 809, 456. Freedom Industries' employees continued to work without being paid, and they even laid out their own money for out of pocket expenses. *See, e.g.*, Tr. 164; R4, tab 22. Liebman knew that Gemini Remodeling was willing to

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[21]Liebman could not, however, remember the specific details of these calls, except that they wanted him to "guarantee" that he was going to make progress payments. Tr. 1747.

[22]The Plan for Inspection Job was approved by the Veterinary Service on March 13, 1985. R4, tab FT106.

finance the renovations to the building and that there were other vendors willing to provide financing. Tr. 1762. Liebman also knew that HT Foods was willing to provide $400,000 that it expected to receive from the sale of its lease option to Penzer. *Id.*

153. On January 14, 1985, Freedom Industries submitted Progress Payment Request No. 2, requesting payment of $299,683. R4, tab FT422(PPChart).

154. Liebman did not pay this request. R4, tab FT422(PPChart). Instead, he ordered another pre-payment audit. In response, DCAA again returned Freedom Industries' progress payment request, maintaining that Freedom Industries was ineligible for progress payments until it incurred costs for direct materials and direct labor. R4, tab F41.

155. Despite the Government's refusal to pay any of the financing it had promised, by January 16, 1985, Freedom Industries reached the major milestone of completing its first articles. Tr. 1764. Freedom Industries reported this achievement to Liebman. R4, tab 22.

156. Freedom Industries' cost proposals and cash flow projections were based on the production rates and maintenance estimates for the state of the art equipment by DoBoy, Koch, and International Paper that Freedom Industries intended to use in its operation. Tr. 327-28. This equipment was specially manufactured and required between six weeks and four months for delivery, depending on the piece of equipment. Tr. 527-29. Freedom Industries ordered the equipment in January in order to have it delivered, set up, tested, and ready for production by April 1985, as reflected in the negotiated cash flows. *Id.*, R4, tab FT086.

Liebman, Acting In Bad Faith, Formally Suspends Progress Payments

157. Liebman, nevertheless, ignored these extensive efforts. On February 6, 1985, Liebman wrote to Freedom Industries and formally suspended progress payments (the "Suspension Letter"). R4, tab 26.[23] Liebman claimed that Freedom Industries was in "such unsatisfactory condition as to endanger performance of this contract." *Id.*

158. Liebman gave five inappropriate reasons in the letter to support his conclusion: (1) Dollar's advice that no credit will be forthcoming until an "arrangement" is in place to settle creditors (precisely as stated in the Proposed Suspension Letter); (2) Freedom Industries "has advised that it has not applied for/received loans from any other financial institution"; (3) Freedom Industries' financial statements indicate that Freedom Industries is "insolvent with a deficit net worth of about $3.7 million"; (4) Freedom Industries has revealed that it is a defendant in numerous claims for non-payment; and (5) HT Foods, which has committed to provide financial support, "has no bank of record [and] has not presented adequate proof that it is a viable concern." *Id.* The Suspension Letter also noted "as a further consideration" that "there has been no physical progress . . . to date." *Id.*

159. As discussed below, these reasons contained not even a shred of support. On the contrary, they eradicated any possible doubt that Liebman's actions were based on spite, ill will, and bias toward Freedom Industries.

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[23]Ironically, Freedom Industries received another offer to provide financing the very next day. On February 7, 1985, Suburban Bank sent Freedom Industries a letter offering $1,500,000 in accounts receivable financing. R4, tab F44.

160. **Dollar's Requirement For An Arrangement To Pay Creditors** – This "requirement" was not an impediment to Freedom Industries' obtaining financing from Dollar. Liebman never investigated what type of an "arrangement" would satisfy Dollar and whether Freedom Industries would be able to develop such a plan. Tr. 1746. Liebman admitted that the arrangement might have been as simple as confirming to Dollar that creditors would be paid out of the profits of the MRE-5 Contract. Tr. 1745-46. This was not a justifiable reason to suspend progress payments to Freedom Industries; it merely was an excuse.

161. **Freedom Industries Advised That It Had Not Applied For Loans From Other Financial Institutions** – This reason was false. Freedom Industries prepared financing documents that Broadway Bank was prepared to sign, until Liebman refused to confirm the Government's commitment to pay progress payments. R4, tab FT087; Tr 450-453. The Suspension Letter also shows that Liebman wrongfully considered only financing from "financial institutions" to be acceptable. Alternative financing was available in abundance, until Liebman refused to cooperate with these Lenders.

162. **Freedom Industries Is Insolvent With A Deficit Net Worth Of About $3.7 Million** – Liebman's assessment of Freedom Industries' "solvency" was nothing less than an attempt to reevaluate the conditions of awarding a contract to Freedom Industries. Freedom Industries' financial condition was fully disclosed to the Government during pre-award surveys. R4. Tab FT078, tab F28. The Government knew that Freedom Industries had a negative net worth prior to award of the MRE-5 Contract and awarded the Contract to Freedom Industries with that knowledge. *Id.* Any increase to that "deficit" was the result of Freedom Industries' herculean efforts to perform the MRE-5 Contract in the absence of any Government financing.

Freedom Industries should have been rewarded for those efforts (by paying progress payments), rather than penalized (by suspending them).

163. **Claims Against Freedom Industries For Non-Payment** – Freedom Industries' financial statements did not indicate, and Liebman did not identify, how many claims had been filed and in what amounts. Liebman had no basis for assessing the practical importance of this issue. Once again, this position was lifted directly from DCAA's audit reports. R4, tab 21. Contrary to DCAA's biased conclusions, the Government's best mechanism for protecting against these claims would have been to pay Freedom Industries to perform the contract so that it could use the progress payments to pay its current creditors and use its profit to pay its past creditors. The information on which Liebman relied provided no basis for formally suspending progress payments to Freedom Industries.

164. **HT Foods' Involvement In The Freedom Industries Contract** – There is no rational reason for considering HT Foods' financial condition as a basis for suspending progress payments to Freedom Industries.

165. **Failure To Make Physical Progress** – Once again, Liebman refused to acknowledge then what he now admits he knew at the time – that Freedom Industries' "progress" included its pre-production efforts. Liebman had reviewed Freedom Industries' cash flows. Tr. 1741. Liebman knew that during the first four or five months of the Contract, Freedom Industries would be incurring primarily building repair and occupancy costs (Tr. 1743) and that progress payments should be paid on them. R4, tab F25. In December 1984, Heringer advised Liebman that "progress" did not necessarily mean physical progress R4l, tab F25. Liebman admitted at trial that Freedom Industries was making progress at the time Liebman suspended progress

payments. Tr. 1770. Liebman proved it to be so by paying these costs on May 6, 1985, before production had begun. R4, tab 422 (PP Chart). This reason to suspend progress payments was specious.

Freedom Industries Obtained Financing From Performance And Bankers - Unnecessary Novation

166. On February 11, 1985, Freedom Industries reached an agreement with Warren Rosen, President of Performance Financial Services ("Performance"), to finance the acquisition of Freedom Industries' high-tech Doboy and Koch production equipment. R4, tab F46.

167. On February 11, 1985, Freedom Industries received a letter of commitment from Bankers Leasing Association ("Bankers"), the lender for whom Performance served as an agent, to provide accounts receivable financing to Freedom Industries. R4, tab FT094.

168. Freedom Industries' ability to obtain financing threatened Liebman's plan to avoid paying progress payments to Freedom Industries. Liebman needed to find a new device to keep the progress payment suspension in place. The opportunity arose during a meeting held at DLA Headquarters, where Liebman seized on the concept of a time-consuming and costly novation of the contract to HT Foods, a company owned by Mr. Thomas but with no known existing debt.

169. Freedom Industries arrived at the meeting at DLA Headquarters on February 14, 1985 with a letter of commitment for contract financing from Bankers. Bankers was a lender that regularly financed government contracts. Tr. 486. Bankers understood that Freedom Industries did not require millions of dollars of financing, but they had no objection to making such amounts available for a fee, if that is what the Government demanded. *Id.*

170. Liebman was faced with a dilemma. Freedom Industries had resolved Liebman's

concerns from the Suspension Letter by producing financing from a financial institution. DLA also confirmed, in Liebman's presence, that physical progress was not a prerequisite to paying Freedom Industries. R4, tab FT338. Liebman now would have to conjure up a different problem to delay making progress payments to Freedom Industries. Liebman resorted to the remaining issue that he had raised in the Suspension Letter -- Freedom Industries' past creditors. R4, tab 26.

171. The Government was fully aware of Freedom Industries' past creditors -- they accrued as a result of Freedom Industries' MRE 3 retort pouches contract (for which Liebman was the ACO), and they were fully-disclosed during negotiations of MRE 5. R4, tab FT037, tab FT050. Nevertheless, Liebman now postured these creditors as a threat to Freedom Industries' performance of the contract.

172. The creditors were not a concern. All Freedom Industries needed to satisfy all of its creditors, past and present, was to receive payment of its progress payments. Freedom Industries had Bankers' financial backing. Freedom Industries was under pressure to provide Liebman with any arrangement that would eliminate his excuses for not paying Freedom Industries.

173. During a February 14, 1985 meeting at DLA, it became clear that Liebman simply did not want to continue the contract through Freedom Industries. Tr. 2040-41. Liebman professed to be "concerned" that Freedom Industries' creditors could attack the progress payments. Tr. 489. In response to Liebman's objections at the meeting, the suggestion was made

that the Contract be novated to HT Foods. Tr. 2040-41.[24] Freedom Industries did not want to novate the Contract. Tr. 2042. Novating the Contract did not make sense from a business standpoint. Tr. 2042-43. Nevertheless, Liebman would not pay any progress payments until the Contract was novated. Tr. 1807; R4, tab FT104.

174. The February 14 meeting concluded as follows: Liebman insisted that Freedom Industries/HT Foods obtain $3.8 million in financing. R4, tab F49. This amount of financing, he said, was required both to meet the Contract financing requirements not covered by progress payments and to protect the Government from unsubordinated creditors. Rule 4, tab F86; Tr. 1798. This requirement was a change from the Government's demands at the time of award, which required financing only to cover the cost of performing the Contract, not to protect against past creditors. Tr. 978-79.

175. Liebman admitted at the trial that the novation was unnecessary. Tr. 1805-06.[25] Once Bankers' financing was available, Liebman says he would have been willing to release progress payments even in the absence of a novation. Tr. 1806. Nevertheless, Liebman never

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[24]It is unclear from the record precisely how the concept of a novation came about. Liebman testified that he "wasn't sure who brought up the issue." Tr. 1793. A letter from Neil Ruttenberg, Freedom Industries' attorney, to Bankers later stated that Ruttenberg suggested and developed the novation. R4, tab 94. At trial, Ruttenberg explained, however, that in suggesting the mechanism of novation, he was only putting a label on the concept that Liebman was insisting upon at the meeting. Tr. 2040-43. Who suggested the novation, however, is unimportant. What is important is that: (1) Liebman would not release progress payments unless a novation occurred (Tr. 1807; R4, tab FT104); and (2) as Liebman now admits, a novation was not necessary once Freedom Industries secured financing from Bankers -- a fact that Liebman never told Freedom Industries at the time. Tr. 1805-06.

[25]The Philadelphia office of DCAA reached the same conclusion on March 12, 1985. That DCAA office was satisfied that HT Foods' proposed Assignment of Monies to Broadway Bank in exchange for Broadway's financing of the Contract was adequate to protect the contractor without the need for a novation. R4, tab FT 104.

told Freedom Industries that he would accept Bankers' financing without a novation. *Id.*

Bankers Provided Accounts Receivable Financing To Freedom Industries In Consideration For An Assignment of Claims

176. A commitment letter from Bankers that Liebman deemed acceptable was issued on March 20, 1985. *Id.* On March 25, 1985, Bankers, at the demand of Liebman, issued an addendum to its commitment letter, further confirming that Bankers was making available $5 million worth of financing for Freedom Industries in consideration for the assignment to Bankers of all proceeds of the Contract. R4, tab 42.

Liebman's Campaign Continued With Progress Payment Delays And Interference With Equipment Suppliers

177. Liebman refused to pay any progress payment requests while the novation was pending. Tr. 1807. On February 8, 1985, Freedom Industries submitted Progress Payment Request No. 3, seeking payment of $231,555. R4, tab FT422(Freedom IndustriesPP#3,A). Liebman ordered another pre-payment audit, and DCAA recommended that $0 be paid to Freedom Industries. R4, tab 49.

178. Despite Liebman's roadblocks, Freedom Industries continued to perform. Freedom Industries arranged with AT&T for the installation of its networked computer system. Tr. 504. The system was planned as the backbone of Freedom Industries' operation. Tr. 500-04. The computers would act as an automated job-segregating accounting system. *Id.* Further, it would automatically track the multitudinous items of CFM and GFM received by Freedom Industries. Tr. 500-04. Liebman knew that such a system was essential for Freedom Industries' successful performance of the Contract. Tr. 1812-13; R4, tab F87.

179. After installation began, AT&T contacted Liebman to confirm progress payment

eligibility. Liebman refused to provide it. AT&T immediately repossessed the system. R4, tab 38. Freedom Industries then tried to finance this acquisition through Performance, the agent for Bankers. R4, tab FT112. Liebman struck again. He acted to destroy Freedom Industries' relationship with Performance by refusing to provide Performance with a letter acknowledging that the Government intended to pay progress payments. Tr. 506-08. Freedom Industries was not able to obtain state of the art equipment and the lot tracking computer system on which it relied as a result of these actions. Tr. 513.

180. Freedom Industries struggled to perform, but Liebman's actions were taking its toll. By April 1985, five months into the contract period, Freedom Industries had not yet received a single payment from the Government. R4, tab 422(PPChart). By that time, Freedom Industries was scheduled to have completed the necessary building repairs in order to have the building ready to receive GFM. Liebman's refusal to provide progress payments caused Freedom Industries, among other consequences, to put its renovation of the facility on hold. R4, tab FT428. This delay prevented Freedom Industries from having the building ready to receive GFM in April 1985. The Government was responsible for Freedom Industries' inability to have the building ready to receive the GFM.

181. Freedom Industries requested an extension to the GFM (receipt) delivery schedule twice, once on March 28 and again on April 2, 1985. R4, tab 46. DPSC knew that Liebman was improperly withholding progress payments. As the command authority and the office of the PCO, it could have acted to assure Liebman's compliance with the Contract. Even more directly, DPSC could have granted an extension to the GFM delivery schedule. Instead, on April 10, 1985, DPSC issued a cure notice to Freedom Industries for failure to accept GFM because the building

was not ready to receive deliveries. R4, tab 44.

182. The issuance of this cure notice had disastrous consequences. It provided Liebman with an "excuse" to extend the suspension of progress payments. Liebman had told Freedom Industries that the suspension would be lifted upon the novation of the Contract to HT Foods (which had changed its name to Freedom NY, Inc.; hereinafter, "Freedom").[26] Liebman executed the novation documents, thereby completing the novation process, on April 17, 1985. R4, tab FT113a. Four and one half months after Contract award, all of the impediments to payment that Liebman had created appeared to have been removed.

183. Instead, on April 18, 1985, Liebman reported internally that "payment of Progress Payment request No. 1 [is] to be held in abeyance until Freedom responds to the Cure Notice and DPSC's intended course of action is known." R4, tab FT116.

184. Liebman went further. He created uncertainty with Bankers that Freedom would be paid its full progress payment even after the Cure Notice issue was resolved. On April 19, 1985, Liebman wrote to Citibank (which was serving as Bankers' local agent) and advised them of the Cure Notice. R4, tab F69. Liebman stated that no progress payments would be made until Freedom responded to the Cure Notice. *Id.* In addition, Liebman stated that, of the $1,766,923 requested, only "approximately $620,000 for Occupancy and Tax Escrow costs would, barring any unforseen developments, otherwise appear payable." *Id.* As a result, Citibank contacted Bankers and acknowledged that it would not advance any funds to Freedom unless expressly authorized by Bankers. R4, tab FT119. Having insisted that Freedom obtain $3.8 million in

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[26]On April 3, 1985, HT Foods amended its Articles of Incorporation to change its name to Freedom NY, Inc. R4, tab 61. The Contract later was modified to approve this change of name. R4, tab 61, tab 62.

financing, Liebman now had cut off Freedom's ability to access that financing.

185. That interference proved costly. On April 19, 1985, Thomas responded to the Cure Notice by advising DPSC that it had made substantial progress with the building repairs. R4, tab F70. Thomas stressed, however, that the company had incurred costs over $1.7 million and needed Liebman to pay progress payments **or provide Bankers with the information it needed to advance funds**:

> Although we continue to perform under this contract, it is necessary for us to either receive partial or full payment of 95% reimbursement under progress payment #1 ***or receive the necessary documentation from administrative contracting officer in order to utilize our $5 million line of credit from Bankers Leasing Association, Inc.*** in order to fully expand efforts to correct plant deficiencies.

R4, tab F70 (emphasis added). For a third time, and desperate for payment, Freedom proposed an extension of the schedules for accepting GFM and for deliveries of product and agreed to pay a nominal consideration of $5,000 for these extensions. *Id.*

186. DPSC refused. R4, tab F71. After a telephone conversation between Thomas and the PCO, DPSC would only agree to extend the GFM and product delivery schedule if Freedom paid $100,000 consideration and paid for storage of the GFM during the extension. R4, tab F71, tab F73. Freedom had no choice, even though the condition was created by Liebman's actions. Freedom agreed, but it emphasized that its agreement was not an admission of responsibility for delay under the contract. R4, tab F71.

187. Eventually, this money was returned to Freedom as part of Modification P00025 (R4, tab 119) — money that Freedom never should have been required to pay in the first place.

188. Liebman finally made his first payment on May 6, 1985, almost six months after the Contract was awarded to Freedom. R4, tab FT422. Of the $1,766,923 to which Freedom was entitled, Liebman paid $1,700,730. *Id.* The $66,000 that Liebman withheld proved to be the next battle ground for the withholding of progress payments from Freedom .

Finally Forced to Pay Progress Payments, Liebman Continued His Assault On Freedom By Conjuring Up Inappropriate Deductions

189. Once Liebman ran out of excuses to refuse progress payments in their entirety, Liebman undertook an unrelenting program to deduct significant amounts from them. Liebman did make a payment on May 6, 1985 for costs incurred since November 14, 1984. Liebman, however, continued his scheme by refusing to pay progress payments on items he deemed "capital" in nature.

190. The PCO had agreed to pay Freedom for the cost of the following items as part of the contract price:

Item	Cost
Quality Control Equipment and Supplies	$ 54,000
Maintenance Equipment	$ 25,380
Building Repairs	$160,000
Building Management and Computer Systems	$177,838
Lockers	$ 25,000
	$522,218

R4, tab 75.

191. These items often are considered "capital" in nature, *i.e.*, they ordinarily are depreciated over the life of the equipment with portions of the cost charged to future contracts.

Liebman conceded at trial, however, that the PCO did agree to pay these costs to Freedom as operating expenses, *i.e.*, entirely within the performance of this one contract. Tr. 1516, 1623-24.

192. Nevertheless, when it came time to pay for Progress Payment No. 1, Liebman claimed that the DAR Progress Payment clause prohibited him from paying these costs in their entirety as progress payments. Tr. 1516. Rather, Liebman claimed he was only allowed to pay the depreciable portion of these costs as progress payments. *Id.* To pay the full amount as progress payments, Liebman claimed, he needed a DAR deviation. Tr. 1517-18.

193. Liebman's position defied logic. Liebman claimed that he could not pay the full cost of this equipment because it was a capital cost that needed to be depreciated over the life of the equipment. Nevertheless, Liebman agreed that in this case, the full cost of the equipment would, in fact, be paid during the course of this single contract, *i.e.*, expensed. Tr. 1837. Payment for just the depreciable portion fully undermined Liebman's justification for not paying progress payments – the impropriety of expensing these costs. Moreover, Liebman recognized that the equipment he refused to pay for was "absolutely necessary" for MRE production. Tr. 1918-19; R4, tab FF87. Yet, Liebman insisted that he would not pay for this equipment until Freedom first produced and delivered the MREs. Tr. 1919. When asked how Freedom was to accomplish this feat, Liebman revealed his true agenda -- "outside financing." *Id.*

194. On May 23, 1985, Freedom complained to Peggy Rowles, Chief, Operational Rations, DPSC and interim PCO. Freedom asked Rowles to review Liebman's deduction, stating that these costs had been negotiated to be expensed to the Contract, not depreciated. R4, tab R50.

195. Freedom also warned Rowles that its "arrangements with the office automation equipment company have been held up based upon their being told by Mr. Liebman that office automation equipment represented a non-allowable expenditure." *Id.* Freedom specified the critical importance of resolving this issue to its performance of the Contract:

> It is necessary for us to expeditiously resolve this issue. We must complete our quality control sampling and tracking system, our inventory control system, our security control system for which this office equipment is absolutely essential, as well as our obligation to Health Services Command to provide a computer for their office.

Id. Even Liebman recognized that Freedom's failure to obtain this equipment could result in Freedom's "inability to successfully perform the contract." R4, tab F87.

196. Rowles called Liebman on June 4, 1985 and advised that DPSC had contracted to pay the costs as a "one time cost." R4, tab F77. Liebman already knew this from his participation in the negotiations that led to the contract with Freedom. Tr. 1516-17.

197. On June 5, 1985, Rowles sent a telex to Liebman, confirming their conversation from the day before. *Id.* Liebman understood that Rowles was telling him that these costs should be paid by means of progress payments. Tr. 1833-34.

198. Liebman, in pursuit of his campaign to starve Freedom, chose to delay compliance with the Government's admitted contractual obligation. On June 12, 1985, Liebman wrote to the Deputy Counsel for DCASR-NY, Michael Montefinise, and advised him that DPSC had confirmed the "negotiation of Quality Control Equipment and Supplies, Automated Building Management and Control Systems and Office Equipment as one-time costs rather than expiration of these costs over the useful life of the equipment by means of depreciation." R4, tab F079. Nevertheless, Liebman claimed that he required a legal opinion because of a single reason: "The

Defense Contract Audit Agency has questioned these costs in their entirety." *Id.*

199. On July 15, 1985, Montefinise issued his legal opinion to Liebman. R4, tab F85. In it, Montefinise confirmed from his own investigation: (1) that the equipment in question was essential for Freedom 's successful completion of the contract; and (2) that the PCO had agreed during Contract negotiations that the equipment would be treated as direct costs "for the purpose of both price determination and progress payments." *Id.*

200. Montefinise opined that whether the equipment should be treated as capital equipment or could be classified under another category to permit treatment as a direct expense[27] was an accounting question. *Id.*

201. Montefinise also recognized that, regardless of the accounting treatment of these costs, the Government could be bound legally by its undisputed promise to pay progress payments for these costs "based upon a theory of estoppel." *Id.*

202. Montefinise's opinion provided Liebman with the opportunity to pay Freedom for these costs. The equipment in question was specialized equipment that was purchased for the performance of this Contract. Its cost was negotiated to be paid as a direct expense to the MRE-5 Contract.

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[27]One example of such a category mentioned by Montefinise was "specialized equipment obtained only for this contract." Clearly, machinery, equipment and other tangible assets necessary for performance (R4, tab FT051(B)) were "specialized equipment."

203. Nevertheless, Liebman never sought accounting advice to confirm that this equipment could be so categorized. Instead, Liebman took the position that he could only pay progress payments on the depreciable portion of these costs which amounts he never paid.

204. Liebman also took the position that, in order to pay progress payments on the full cost of these items, a DAR Deviation would be necessary. Tr. 1517-18. On July 18, 1985, Liebman submitted a request for a DAR Deviation. R4, tab F87. The request acknowledged that the Government's failure to pay Freedom for this equipment could lead to Freedom 's failure to obtain the equipment, and that its failure to obtain the equipment could lead to a failure to perform the Contract. *Id.*

205. On September 4, 1985, Liebman's DAR Deviation Request was denied. R4, tab FT168. For months, correspondence was exchanged among the various Governmental agencies regarding this request, stressing Freedom's negotiation of these items as direct costs and that Freedom "planned on receiving Progress Payments for these expensed items." R4, tab FT195. The Government made efforts to renew the request, recognizing that the Government risked breaching the Contract if it failed to pay these costs. R4, tab FT233 (Conversation Record noting "Because of Breach of Contract issue, get advice from DCASR/DCASMA and/or DPSC attorneys"). The request was never approved.

206. When a new PCO, Frank Bankoff, was assigned to the Contract, Bankoff claims that he also told Liebman to pay for these costs. Tr. 1425. When Liebman refused to do so, the PCO did not overrule him. *Id.* Instead, Bankoff simply submitted his own DAR Deviation Request. R4, tab F91.

207. Significantly, during the ten months that Liebman's request was pending, Liebman never even paid Freedom progress payments for the depreciable portion of these costs. Rather, in May 1986, Liebman paid Freedom the full amount of these costs as progress payments upon submission of an invoice – precisely as Freedom had asked Liebman to do from the outset – but only after Freedom signed a contract modification, Modification P00025, that purports to contain a waiver of claims. Tr. 1562-65; R4, tab 119.

208. Liebman interfered with Freedom's ability to obtain an automated building management and control system to permit Freedom to keep track of the GFM and CFM it was receiving under the Contract. R4, tab F84; Tr. 513. As a result, Freedom had to track these components manually, "wasting an exorbitant amount of man hours which was not part of our budget since everything was programmed and negotiated for an electronic state of the art quality control system." R4, tab F84.

Liebman's Interference With Freedom's Acquisition Of Its Production Equipment Causes Freedom To Incur Substantial Additional Costs

209. Freedom's costs for labor depended substantially on the speed and reliability of the production equipment being used. The labor costs that Freedom included in its budget were based on Freedom's anticipated purchase of high-speed, state of the art production equipment. *See* Findings 211-217.

210. Production of MREs involves three distinct production operations: retort, sub-assembly, and main assembly.[28] The "retort" operation is the preparation of the MRE entrees on which Walsh-Healey qualification was based. Sub-assembly involves two different operations:

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[28]These production operations are in addition to the equally important functions of quality control (*i.e.*, inspection) and storage.

(1) filling the accessory bag with accessories, including gum, matches, and toilet paper; and (2) filling the crackers bag into an air-tight pouch. Main assembly also involves two different operations: (1) taking the entree, accessory, and cracker pouches and sealing them in a meal bag (*i.e.*, a 12" long, thick plastic brown bag) using a special "band sealer"; and (2) enclosing the correct number of meal bags in a case, and gluing and strapping the case. Tr. 42-43.

211. Freedom intended to buy high-tech Koch Multivac equipment for its sub-assembly production. Tr. 327-29, 521-23; R4, tab FT427. Accessory pouches could then be formed using a machine that created 12 accessory pockets at a time using vacuum technology. Tr. 521-23. A single employee could fill these pockets with a particular accessory component as the pouches move past in assembly line fashion to the next employee. This technique was a vast improvement over alternative bag-filling operations. *Id.*

212. Cracker assembly would also be streamlined using a Multivac R5100MC automatic rollstock packaging machine. R4, tab FT427. Traditionally, MRE assemblers would use cracker bags, and employees would fill and seal one bag at a time. The Koch machine was designed to use two layers of film, plastic and foil, to form and seal the bag around the crackers on all four sides as the crackers moved along on an assembly line. Rather than fill one bag at a time, this machine would fill 6-8 at a time with the same, or even less, input of labor.

213. Freedom also intended to buy Doboy continuous band sealers for its assembly operations. Tr. 327-29, 515-17; R4, tab FT425. Traditionally, assemblers would place the meal components in a meal bag and use a hot band sealer to close it. Tr. 516. The older equipment did not have an adequate cooling component to create a secure seal. Tr. 516-17. The Government recognized that the previous MRE contractors had problems with these seals. R4, tab FT022,

Bates 00193. By contrast, the Doboy continuous band sealer would roll the meal bags through a special band sealer that applied the heat and cold components automatically. Tr. 516. The process was both quicker and more reliable, resulting in a better seal. Tr. 516-17. Freedom placed a purchase order with Doboy for the continuous band sealers on January 16, 1985. R4, tab FT086.

214. Freedom also intended to buy case forming equipment from International Paperboard Company to assist in the forming and sealing of the MRE cases, which were manufactured by the same company. Tr. 327, 517-19. The cases themselves were made of thick fiberboard that was difficult to bend manually into a case ready to pack with meal bags. *Id.* Freedom intended to purchase a case erector and top and bottom case sealer machines from International Paperboard specifically designed to form and seal these cases. *Id.*; Tr. 1739-42.

215. Freedom planned to purchase top-of-the-line conveyor belts from S&B Conveyors. Tr. 515. Freedom received a price quote from S&B Conveyors, Inc. for the purchase of a top of the line conveyor system on January 30, 1985. R4, tab FT426.

216. Freedom placed a purchase order with Koch for the Multivac R5100TF MC Fully Automatic Rollstock Cracker Vacuum Packaging Machine and the Multivac R5100MC Fully Automatic Rollstock Accessory Packaging Machine on January 31, 1985. R4, tab FT427.

217. On February 20, 1985, Freedom confirmed its agreement with Performance to finance the acquisition of this equipment, as well as the other production necessary for the

Contract, including food production equipment such as stock rotomats, automatic seamer, kettles, pouch sealer, carton machine, and boiler. R4, tab FT098. The total purchase price for this equipment was approximately $1,600,000.

218. Liebman then acted to destroy Freedom's relationship with Performance and Bankers, which led to the loss of this financing for Freedom's production equipment.

219. The Government had agreed to pay Freedom $333,333 for production equipment which would be paid to Bankers for lease payments between April and December 1985. Bankers was thus willing to finance the balance for the acquisition of this equipment. *Id.*

220. After Freedom submitted Progress Payment No. 2 on May 15, 1985, Performance attempted to verify the progress payment invoice with Liebman by telephone. At that point, Performance "encountered a problem" with Liebman:

> Upon contacting Mr. Liebman, our administrative person in Chicago, a Ms. Linda Polhemus, was told by Mr. Liebman that although this invoice had been signed off on and approved, **he advised Bankers Leasing not to advance any monies as there were problems with this invoice and payment was not forthcoming.** Since we had received an approved voucher, Linda was quite surprised when Mr. Liebman instructed her not to advance any monies due to this change of posture regarding approval. . . . Needless to say, this situation created a tremendous amount of paranoia on the part of our lender.

Id.(emphasis added); Tr. 507-08.

221. Performance sought a comfort level that it would receive payment by requesting a list of routine items that would be paid by Liebman without dispute. *Id.* Performance had obtained such a list routinely on other government contracts it had financed. *Id.*

222. A meeting was held on June 19, 1985 for the Government to discuss these financial matters with Performance. Tr. 510-11; R4, tab F81. Attendees included representatives of Performance, Freedom, and DCASMA-NY, including Liebman. R4, tab F81.

223. The "primary concern" expressed by Performance was Liebman's change of mind on Progress Payment No. 2. Performance's President, Mr. Warren Rosen, informed the Government that, as a result of Liebman's actions, the "leasing arrangement for production equipment was cancelled [sic] pending a higher level of comfort on the part of the financial institution." *Id.*

224. Performance also expressed concern about the length of time between the submission of progress payment requests and the payment of any portion of those requests.[29] Liebman claimed that Freedom did not qualify for the 5-10 day payment period that resulted from the automatic payment system because Freedom "was on the manual system which required a pre-approval audit from DCAA before payment could be made." *Id.* However, it was Liebman who ordered both the manual processing of Freedom's requests and the regular pre-payment audits of these requests. Tr. 1661, 1676. While Liebman blamed these conditions for the delay in making progress payments, Liebman ignored the fact that he was the one who unjustifiably imposed these conditions.

225. It was suggested that a list of routinely payable costs be established. Liebman objected to two items on the proposed list, including "salaries" because "the auditor found that back salaries had not been paid from November 1984 through March 1985." This exchange well-

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[29]Liebman's payments on Progress Payment No. 2 and Progress Payment No. 3 averaged three weeks between submission and payment. R4, tab FT422(PPChart).

represents Liebman's malevolence. Liebman knew that Freedom's progress payments were to be paid on costs incurred, not on costs paid. Tr. 1637-38. He knew that to deny progress payments because the costs had not yet been paid was a violation of the progress payment clause. Tr. 1690. Yet, Liebman intentionally took that position in order to interfere with Freedom's ability to obtain its production equipment.

226. Liebman also knew that the reason Freedom did not and could not pay these salaries during this period was not Freedom's fault, but because Liebman had refused to pay any progress payments until May 6, 1985. R4, tab FT422(PPChart).

227. Liebman promised that (1) he would provide a list of routine costs and would advance 80% of the costs (not 95%, as required) represented on the list; and (2) he would pay the $333,333 allowed as depreciation for certain production equipment as an allowable cost." *Id.* "With this confirmation, Mr. Rosen was willing to support the leasing of equipment by Bankers Leasing." *Id.* Bankers also relied on this promise to continue advancing working capital financing to Freedom. R4, tab 318.

228. Liebman failed to follow through on either of these two promises. Liebman never produced a list of routine costs that would be paid with every progress payment. Tr. 512; R4, tab F92, tab 318. Moreover, Liebman refused to pay any portion of the next three progress payments, which were submitted on July 5, July 28, and August 8, 1985. R4, tab FT422. The next payment Freedom received was not until October 11, 1985. Accordingly, for more than three (3) full months, July, August and September, Freedom was starved for money. *Id.*

229. By that time, Performance was long gone, and with Performance went Freedom's production equipment. Tr. 513, 530. On June 22, 1985, Koch notified Freedom that it was

canceling Freedom's purchase order for failure to make the necessary down payment. R4, tab FT136. As a result, Freedom lost its "place in line" for this equipment, which was on back order, and could not obtain this equipment in time for MRE 5 production. The same occurred with Doboy and the rest of the equipment Freedom had arranged to finance through Performance. Tr. 530.

230. On August 8, 1985, Freedom solicited Performance to obtain alternative production equipment for Freedom. R4, tab FT139. Instead of a Koch Multivac to package and seal accessory pouches, Freedom had to settle for 6 "lazy susan" type turntables that would spin while employees stationed around the table drop an accessory into each pocket. *Id.*; Tr. 523-24. Instead of Doboy state of the art band sealers, Freedom was forced to order 14 Model 552 horizontal band sealers and 10 Model B band sealers and 6 model 18V vacuum sealers from Production Packaging Equipment, Inc. – a "mix and match" group of equipment pieces. R4, tab FT139; Tr. 517, 519-521. Instead of an International Paper case sealer, Freedom settled for one by Marq Packaging Systems. R4, tab FT139; Tr.525-27. The Marq equipment was designed for corrugated cardboard, not for the heavy duty fiberboard materials used for MRE cases. Tr. 525-26. It flexed and imperfectly formed the cases, which caused sleeving problems, and it broke down frequently. *Id.* Even Freedom's conveyor equipment was downscaled. R4, tab FT139.

231. Performance was not interested in assisting with financing. Freedom eventually persuaded Bankers to provide financing for this equipment through a corporate affiliate of Freedom, Teknic Corporation, which served as the leasing agent for this equipment. R4, tab FT153.

231.a. On August 13, 1985, Freedom Industries requested that the Government perform tests on the less efficient equipment to determine if the equipment could perform in excess of the manufacturer's guaranteed rate and to the level Freedom Industries required. Tests were performed and the equipment failed twice in front of Government inspectors. The Government knew the equipment was not capable. R4, tab 193 (8/13/85 Plant Visit Report, submitted at trial by Appellant to supplement tab 193).

232. This alternative equipment was barely adequate for its purpose. It was slower and less efficient, and it required frequent repairs. Tr. 513-31, 904-08, 1039-42. Often, Freedom was unable to pay for parts and service, leading to refusals to repair its equipment until payment was made. R4, tab FT215, tab FT216. Moreover, Bankers delayed payment on this equipment because of the Government's delay in providing progress payments for these costs. R4, tab FT225. As set forth in the Quantum section below, Freedom's costs of production were greatly increased by this Government caused delay and disruption.

Liebman Continued To Make Unjustified Deductions To Impede Freedom's Performance

233. On July 5, 1985, Freedom submitted Progress Payment No. 4, requesting payment of $807,348. R4, tab FT422.

234. By this time, Liebman knew that DCAA's interpretation of the Contract had been discredited. Indeed, he complained that DCAA had stopped being of any assistance whatsoever. R4, tab FT338.

235. Nevertheless, Liebman relied on DCAA's faulty audit of Progress Payment No. 4 for the purposes of: (1) reversing a $400,000 of progress payments previously made to Freedom (in violation of the rights of Freedom's assignee under the Assignment of Claims Act); (2)

declaring Freedom's cost accounting system inadequate; and (3) again suspending progress payments to Freedom for the same erroneous reasons.

The $400,000 Disallowance.

236. Liebman deducted $400,000 from Progress Payment No. 8 that Freedom previously had billed and received in progress payments for rental expenses. Liebman claimed that a $400,000 payment Freedom received from the sale of a real estate purchase option actually should be considered a reduction in rent. Tr. 1821-23. Liebman based his conclusion on DCAA's claim that, "We saw no evidence of this informal agreement." R4, tab 60. Liebman therefore deducted the $400,000 as an offset for occupancy costs that Liebman previously paid in Progress Payment No. 1. Tr. 1821-23.

237. This retroactive deduction was improper. The agreement was not informal and it was fully documented. The lease with Penzer for the production facility contained a purchase option. R4, tab FT052. At trial, Penzer testified that this was a legitimate transaction. Tr. 818-19, 824. Freedom's expert financial witness testified that the option was valid, that the transaction made sense from a business standpoint, and that the reduction of Freedom's progress payments by $400,000 was "180 degrees wrong." Tr. 986-89. The $400,000 payment was reported as income on Freedom's balance sheets. R4, tab FT162. Even Liebman admitted that the sale of this lease option was a legitimate transaction. Tr. 1823-24, 1874. Liebman had no basis for disallowing this cost.

238. This retroactive deduction violated the "no off-set" right of Freedom 's assignee of claims (Bankers) and was illegal under the Assignment of Claims Act, 31 U.S.C. § 203, 41 U.S.C. §15.

The So-Called "Inadequate" Accounting System.

239. DCAA also concluded, for the first time, that "the contractor's current cost accounting system is not considered adequate for accumulating contract costs in support of progress payment requests." R4, tab 60. This conclusion had no rational basis -- DCAA had approved Freedom's cost accounting system in Freedom's pre-award surveys and in all of its previous audit reports that addressed this issue. *See, e.g.*, R4, tab FT047b, tab 11, tab 49, tab 54, tab FT422(HT PP#1, B), and (tab FT422(HT PP#3). Liebman should have placed no reliance on this about-face by DCAA.

240. Mr. Jordon Fishbane, Freedom's expert financial witness, testified that DCAA's findings of "deficiencies" did not relate to Freedom's cost accounting *system*, but rather to purported errors in recording. R4, tab 60. Such alleged problems do not support a determination that Freedom's accounting system was inadequate nor any reasonable basis to withhold progress payments. Tr. 983-85.[30]

241. DCAA's other allegations -- lack of supporting documentation and lack of a "cash disbursements journal" -- were equally baseless. Mr. Fishbane reviewed all of Freedom's records. Mr. Fishbane testified that Freedom's accounting system "was really good." Tr. 986. Freedom showed it spent the money and that it spent it on this job, and that it was all supported by documentation. *Id.* Furthermore, the term "cash disbursements ledger" is synonymous with a check register and Freedom had a check register. *Id.*

242. DCAA's bias against Freedom was obvious. Liebman knew that he had the right

[30]Mr. Fishbane further opined that, even assuming Freedom's accounting system was inadequate (which it was not), the progress payment requests were so well-documented that the Government still could have paid Freedom. Tr. 985.

to challenge DCAA's determination. Tr. 1939. He did not do so. *Id.* Instead, Liebman claims that he made an independent determination that DCAA was right. *Id.*

243. On August 19, 1985, the parties met to discuss the audit report and Freedom's response. R4, tab FT163. Freedom complained that it did not have its automated accounting and lot tracking system because of Liebman's failure to pay progress payments as negotiated. *Id.* The Government complained about Freedom's failure to have its production equipment in place – a situation caused by Liebman. The meeting ended with Liebman proposing the suspension of progress payments for a second time.

Liebman Proposed Suspending Progress Payments For A Second Time

244. Despite Liebman's admission that DCAA's various positions against Freedom were incorrect (*e.g.*, Tr. 1778, 1869), Liebman proposed suspending progress payments for a second time based entirely on DCAA's audit report, R4, tab 60; Tr. 1839-40. Although Liebman recognized that there were procedures necessary to propose such a suspension (Tr. 1739), Liebman did not use them. He did not prepare written findings and he did not convene the Board of Review. Tr. 1944. He simply informed Freedom at the August 19, 1985 meeting that he was proposing a suspension of progress payments because Freedom's accounting system had been declared inadequate. R4, tab FT163. On August 23, 1985, Liebman issued a letter formalizing this proposed suspension. R4, tab 62.

245. At the same time, Liebman continued to interfere directly with Freedom's financing. On August 15, 1985, DLA's Financial Analyst declared that Freedom had obtained adequate financing from Bankers to perform the Contract. R4, tab FT158. Nevertheless, Liebman sought to interfere with that financing by advising Freedom's lender, Bankers, not to

advance any more funds to Freedom . R4, tab FT157.

246. It is now clear that Liebman had an ulterior motive in suspending progress payments again. Liebman was under pressure from DPSC for his unsupported position that he could not pay progress payments on capital expenses. He no longer could deny that DPSC had negotiated to pay these costs as direct expenses through progress payments. The PCO also was advising Liebman to pay these costs. R4, tab FT163. At a meeting held on August 19, 1985 with only Government representatives present, the PCO acknowledged that Liebman was refusing to administer the Contract as negotiated:

> In negotiations with DPSC, Freedom was allowed to claim direct costs for all [capital equipment] but production equipment. However, DCASMA will not pay progress payments for any capital equipment as a direct cost.

Id.

247. Liebman had to develop a new agenda -- to pressure and force Freedom to reclassify the disputed costs in its accounting system from direct costs expensed and subject to progress payments to "capital" costs which are capitalized so that only a small fraction of the costs are subject to progress payments. If successful, such a tactic would relieve Liebman of any pressure for denying progress payments on these costs. Liebman undertook to do so using DCAA's reports as a justification.

Additional Financing Requirements.

248. Liebman promptly implemented this plan. On August 30, 1985, the PCO improperly issued a Cure Notice based on two circumstances for which Liebman, not Freedom, was responsible: (1) Liebman's August 23, 1985 proposed suspension of progress payments; and

(2) Freedom's failure to have its production equipment in-house. R4, tab 63.

249. On September 13, 1985, Freedom responded to the PCO's Cure Notice. R4, tab 67. Freedom reminded the Government that Freedom's delays were directly attributable to the Government's actions. Freedom also advised the PCO that Freedom's production equipment was in-house and being prepared for production. However, because of the Government-caused delays, Freedom had had to lay off its production staff, causing additional delays. Freedom proposed two, alternative new delivery schedules. *Id.*

250. On October 1, the Government decided that Freedom needed $3.5 million in outside financing, in addition to the monies Bankers already had advanced, to complete the Contract. R4, tab FT186.[31] The Government's calculation of the $3.5 million figure was meaningless from a financial standpoint and was flawed according to Freedom's financial expert who testified at the trial. Tr 992-995. The calculation was performed by Liebman's financial analyst using a method of analysis that he called, "Backwards Induction." R4, tab FT186a, d. This calculation failed to consider various factors that diminished substantially Freedom's need for outside financing. The effect was to change the original obligation undertaken by the Government by transferring the risk of financing from the Government to Freedom and its bank. Tr. 992-995.

251. The inappropriate calculation gave a false impression of Freedom's financing needs beyond what Freedom already had obtained. The additional financing "needs" projected in the calculation assumed that a DAR deviation for $500K for capital expenses was going to be denied.

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[31]The Government now was requiring a total of $5.5 million in outside financing from Bankers. R4, tab 75, p. 5. Bankers originally had made available to Freedom a $5 million line of credit. $2 million, leaving $3 million in financing available. By requiring $3.5 million in outside financing the Government was increasing Freedom's outside financing requirements by an additional $500,000. *Id.*

R4, tab 75, p.5.

252. The Government not only refused to pay progress payments on approximately $500,000 in costs, as contractually agreed, but the Government now insisted that Freedom obtain outside financing to pay for these costs. If Freedom refused, the Government would default Freedom: "Freedom's ability to obtain this financing would be the basis for a satisfactory appraisal of their financial capability and, already receiving a favorable production evaluation, the basis for a favorable decision by the PCO to extend the contract." *Id.*

253. The Government also constrained Freedom's use of the additional financing it was demanding by dictating how this money would be applied: "Of this money becoming available to Freedom, Freedom would also be required to pay all 'over 30 day' liabilities." *Id.* The Government had no authority to direct how Freedom should manage its business.

254. The Government refused to acknowledge that Freedom had made progress under the Contract until Freedom paid the "over 30 day" liabilities, two unrelated activities. Rather, the Government stated, "This would constitute the start of progress." *Id.*

255. Stokes's calculation did identify two additional facts regarding the Government's wrongful withholding of progress payments from Freedom: (1) that, to date, the Government had withheld $3.1 million in progress payments from Freedom; and (2) that, even according to Liebman, ***at least*** $2 million in progress payments was due and owing but was being withheld while the Government decided what additional conditions to impose on Freedom. R4, tab FT186. The calculation was based on a "worst case scenario," under which Stokes assumed that Freedom would receive *no payment at all* on Progress Payment No. 8, which was submitted on October 11, 1985 for costs incurred in September 1985. Tr. 994-995; R4, tab F100, tab FT422(PPChart).

Concerned about the propriety of Liebman's withholding of payments to Freedom, the Government's legal counsel began to discuss efforts to obtain a release of claims from Freedom. R4, tab 186, Bates 01410.

256. After a Government meeting on October 2, 1985, a meeting was held on October 3, 1985 between Government and Freedom representatives at Freedom's plant to discuss a schedule extension and financial issues. R4, tab 75, pp. 5-8. The parties agreed to modify the existing progress payment schedule to allow for a $1 million dollar payment for each of the next four 50,000 case increments. *Id.*

257. At the meeting, the Government sought an additional concession from Freedom for these extensions – a release of all claims.

> The Government vigorously pursued this request but the Freedom personnel vehemently refused to agree to this condition. Freedom claimed that due to expenses of standing still and additional expenses incurred, all due to the Governments [sic] refusal to pay timely progress payments, contract profit was down to $900K from the negotiated $2.2M. Freedom made it known that it had not ruled out the possibility of a claim to recoup damages caused by breach of contract.

R4, tab 75, p.7.

258. When Freedom refused to waive any claims, the Government demanded $100,000 in consideration for the extension to the delivery schedule, the need for which the Government had caused. *Id.* Freedom was forced to agree to the payment or face default. *Id.*

259. During this meeting DPSC again confirmed that it had agreed during contract negotiations that Freedom could expense the $522,218 in "capital" type costs for which Liebman refused to pay progress payments. *Id.* Nevertheless, other Government representatives led by Liebman reiterated that they would only pay these costs upon verification of Freedom's receipt and prescribed use of the additional financing and a modification of the Contract, which only would occur upon "approval of a DD DAR deviation request." R4, tab 75, tab F100.

260. Liebman's scheme worked. Liebman successfully convinced Freedom to reclassify the disputed costs as "capital" costs on Freedom's books. R4, tab FT194, Bates 01451 ("Freedom has established accounts segregating costs which it concedes are of a capital nature"); Tr. 559-61. Freedom also met the Government's new financing requirements and obtained the $5.5 million line of credit that the Government demanded. R4, tab F100, tab F101. According to the Chief of the Financial Services Division, this financing "has placed Freedom N.Y. in the position of being a viable and financially satisfactory business entity which should be able to financially complete the contract . . . . " R4, tab F101.

261. The Chief of Financial Services Division reiterated on October 15, 1985 that "progress payments are a must for" Freedom to be able to complete the Contract. *Id.* Nevertheless, when Liebman resumed making partial payments to Freedom on its progress payment requests, beginning on October 11, 1985, he continued to make substantial and unwarranted deductions from each request. Tr. 338. As of October 11, 1985, Freedom had a balance of $1,487,274.00 in progress payments owed by the Government. R4, tab FT422(PPChart). With each subsequent progress payment request between October 11, 1985 (PP#8) and May 9, 1986 (PP#16), Liebman refused to pay substantial portions of these requests

so that the Government's deficit on making progress payments increased from $1,487,274.00 on October 11, 1985 to $5,368,427.00 on June 18, 1986. R4, tab FT422(PPChart).

262. This shortfall resulted, in part, from Liebman's application of a percentage of completion formula to Freedom's progress payments.

263. An ACO is prohibited from applying the "percentage of completion" method to progress payments for contracts that are based on incurred costs, such as Freedom's MRE 5 Contract. DLAM 32.590-4(b). The percentage of completion method is to be applied only to construction and shipbuilding contracts. DAR Appendix E-501; E-503.

264. Nevertheless, with respect to Freedom's Progress Payment Requests 5, 6, and 7, Liebman applied a percentage of completion calculation that reduced the amount of progress payments otherwise due Freedom. *See* R4, tab F90 (August 13, 1985 Liebman request for "percentage of physical completion" analysis, stating that "no payments shall be made at least until completion of this review").

265. From that time forward, Liebman regularly ordered that Freedom's progress payments be subject to a performance of a percentage of physical completion analysis. *See, e.g.*, R4, tab F080b (Industrial Specialist report dated November 5, 1985 reviewing Progress Payment #8 and stating that the "subject contract is 23.41 percent physically complete"). Liebman then applied the percentage of completion method to Freedom's progress payment requests to limit the amounts paid to Freedom.

266. These actions constituted violations of the progress payment clause and were instituted by Liebman in bad faith in order to reduce the amount of money to be paid to Freedom.

267. Freedom protested the application of a percentage of completion limitation on its progress payments. R4, tab FT193. These protests were ignored.

The Government Maneuvered Against Freedom In An Attempt To Obtain A Release Of Claims

268. Freedom began production in November 1985. Freedom encountered initial production problems that the Health Services Command personnel considered to be normal for a new contractor in the initial production stage. R4, FT194, Bates 01451; Tr. 1080-1084.

269. Accordingly, Freedom was unable to meet a revised delivery schedule (Modification P00018), which required the delivery of 50,000 cases on November 30, 1985. R4, tab 85.

270. On December 2, 1985, PCO Bankoff terminated 49,758 MRE cases for default. R4, tab 90. The Government also concluded that Freedom would not be able to deliver the next increment of 65,000 cases scheduled for delivery by December 31, 1985. R4, tab F111.

271. Upon being notified of this partial termination, Thomas immediately complained to DPSC. Thomas informed DPSC again that Freedom intended to file a multi-million dollar claim against the Government. Freedom's attorney wrote to Bankoff protesting the partial termination and explaining why the delays were attributable to the Government, not to Freedom. R4, tab FT212.

272. Freedom's complaints triggered an immediate response by the Government.

273. The Government needed delivery of the 114,758 cases (November and December 1985 deliveries), or it would be in danger of failing to meet the Prepositional War Reserve Level it was required to maintain. R4, tab 90. In order to reprocure these cases from another MRE

assembler, the Government required Freedom to release the GFM that already had been delivered to Freedom. Tr. 580-582.

274. The Government also wanted Freedom to release its impending claim against it for increased costs and delays caused by the Government. R4, tab FT218.

275. On December 6, 1985, the attorneys for DLA, DCASR-NY, and DLA met. *Id.* They anticipated the default of the 65,000 units scheduled for the end of the month and decided to use the possibility of reinstatement of the full quantity of 114,758 cases as a "carrot" to seek the following concessions from Freedom: (1) a full release of all potential claims; (2) cooperation regarding the release of 90,000 cases of GFM that the Government needed to provide to other MRE producers for the reprocurement of the 114,758 cases; and (3) the termination of the balance of MRE units if certain production milestones were not met. *Id.* In exchange, the Government would be willing to reinstate 114,758 cases to Freedom, "at the Government's sole discretion" if Freedom had demonstrated itself to be a viable producer. *Id.*

276. The Government met with Freedom on December 9, 1985 to negotiate these points. R4, tab FT220. The Government offered an extended delivery schedule, if Freedom released all its claims against the Government. *Id.* Freedom flatly refused since all of its production delays were attributable to the Government's failure to pay Freedom's progress payments and the Government's interference with Freedom's ability to obtain its production equipment. *Id.*

277. Freedom agreed to cooperate in the reprocurement of the 114,758 cases to another contractor on the condition that those cases would be reinstated to Freedom's contract after remaining units had been delivered by Freedom. *Id.*

278. The parties agreed to modify the delivery schedule for deliveries in January through July 1986, plus a reinstatement of the 114,758 partially terminated cases at the back end of the Contract. *Id.* R4, tab 100, ¶8. Reinstatement was conditioned only on Freedom's timely delivery of cases in accordance with the revised delivery schedule. R4, tab FT220, Bates 01540, 01542.

279. Within a day after reaching this agreement, Freedom assisted the Government in shipping Freedom's GFM from the Freedom plant. Tr. 580-582.

280. On December 11, 1985, the Government in bad faith issued Freedom a Cure Notice, the basis of which is an allegation that Freedom had declared during the December 9 meeting that it anticipated a shortfall of $1.4 million to $2 million in working capital. That alleged "announcement" did not prevent the Government on December 9 from reaching an agreement to extend the delivery schedule and to reinstate the 114,758 cases on the back end of the contract. That alleged "announcement" did not prevent the Government from taking Freedom's GFM within a day after its meeting with Freedom. Nevertheless, after the Government took possession of Freedom's GFM, the Government informed Freedom unilaterally that "all discussions from our 9 December 1985 meeting will be held in abeyance." R4, tab F113.

281. On January 2, 1986, Bankoff formally declared that he was terminating an additional 65,000 cases of MREs from the Contract, for a total of 114,759 cases, and that these cases would be reprocured to another contractor R4, tab 100. Bankoff confirmed, however, that the Government had agreed to reinstate 114,758 cases to Freedom for delivery at the back end of the Contract. *Id.* at ¶8.

281.a. On January 7, 1986, Bankoff interfered with and countermanded Freedom's ship-

in-place order to its CFM subcontractor, Sterling Backery. Bankoff claimed he had the right to approve the ship-in-place, R4, tab FT436. Neither the contract, nor any other evidence in the record of this case, supports the proposition that Bankoff had such authority. DPSC, on February 26, 1986, admitted to DLA that it had in fact commenderred Freedom's C.F.M. R4, tab FT255, ¶ 4.

282. Despite Freedom's increase in productivity during this time[32] and Liebman's "agreement" to pay some $353,000 in progress payments (Progress Payment No. 10), the issuance of the Cure Notice gave Liebman a new opportunity to refuse to pay any progress payments until the Cure Notice was removed. R4, tab FT239 ("Because of the cure notice, no progress payment monies were released to Freedom since 9 December 1985 although Freedom continued to increase production"). *Id.*

283. Thus, Liebman did not pay Freedom the $353,000 payment for "manufacturing salaries and other expenses verbally approved by DCAA" to which Liebman had agreed (*i.e.*, Progress Payment No. 10), or any portion of the $1,159,473 requested in Progress Payment No. 11, until January 30, 1986. R4, tab FT422(PP#10, PP#11, and PPChart).

284. On January 21, 1986, Bankoff instructed Liebman not to release any progress payments to Freedom until Freedom signed Modification P00020 ("Mod 20"). Tr. 1467-68; R4, tab FT219, Bates 01531. Mod 20 contained language stating that the 114,758 cases would be reinstated only at the "sole discretion of the Government." Because Liebman obeyed Bankoff's instruction not to pay any progress payments until Mod 20 was signed, Freedom had not received

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[32]According to Liebman, after one month of production, Freedom's rejection rate dropped from 99.37% in December 1985 to 2.9% in January 1986. R4, tab 194(1-31 January 1986 Contract Management Alert).

any progress payments since December 6, 1985. On January 29, 1986, with $3,603,497 in progress payments requested and overdue (R4, tab FT422(PPChart)), Freedom was forced to sign Mod 20. R4, tab 104.

285. The next day, January 30, 1986, Liebman released only $1,100,000 of the $3,603,497 that had been requested. R4, tab FT422 (PP Chart).

286. The Government met on January 16, 1986 to discuss Freedom's response to the December 11, 1985 Cure Notice. R4, tab FT239. The participants recognized that the issue of the L-4 progress payment ceiling was now crucial to Freedom. *Id.* By reducing the contract quantity by 114,758 cases, Bankoff affected the availability of progress payments under the Clause L-4 "ceiling," which permitted $3 million or 50% of total contract whichever was less subject to increases based on justifiable need." After the partial termination, the L-4 ceiling was reduced to $6.9 million. *Id.*

287. Freedom requested increases to the ceiling and provided the required justification. Freedom explained that, under the terms of L-4, the PCO must increase the level of progress payments upon the demonstration of need by the contractor as supported by cash flow statements. *Id.* Freedom submitted cash flows demonstrating this need and should have received an increase in progress payments up to 95%.

288. Bankoff acknowledged that, "The clause does not allow for the PCO or ACO denial of an increase other than for lack of need. This was discussed with DPSC Counsel, Chuck Wright, and with Bill Stokes and Marv Liebman." R4, tab FT239, Bates 01636, ¶9. Bankoff was even concerned that if the Government was sued concerning the L-4 ceiling, it would not stand up

in Court or before the Board. R4, tab 340, Bates 02367.[33]

289. Nevertheless, neither Liebman nor Bankoff ever raised the issue of the propriety of the L-4 with their superiors. They did not seek a DAR Deviation requesting approval of the use of the L-4 clause in this Contract. Rather, they quietly raised the L-4 ceiling to its $9 million "original" level -- and no further. R4, tab 104. Bankoff retained the "ceiling" at this level to maintain further control over Freedom. R4, tab FT340, Bates 02367.

290. The L-4 limitation was contrary to the DAR and, therefore, was illegal. *See* DAR 7-104.35(b). Bankoff violated the terms of the L-4 clause by arbitrarily refusing to increase the limit to the extent requested by Freedom, despite Freedom's demonstration of need and submission of cash flow statements in support of its request.

291. The Government obtained the necessary GFM for these cases from Freedom – with Freedom's permission and cooperation – based on the December 9, 1985 agreement the Government reached with Freedom.

292. The Government also needed CFM that had been purchased by Freedom to give to Rafco to produce the reprocured cases. R4, tab G32. The Government did not request, and Freedom did not give, its permission for the Government to take Freedom's CFM. Instead, the Government simply took this CFM without asking. *Id.*; R4, tab FT436.

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[33]Significantly, this is not what Bankoff told Mr. Chiesa, DLA Chief of Contracts, the following month. During a visit to DLA Headquarters on February 24, 1986, "Mr. Chiesa requested an answer as to the origin of a 50% (of contract value) ceiling on progress payments, that is unique to DPSC MRE contracts. Mr. Chiesa was assured that this ceiling was applied to all MRE contractors." R4, tab G32. This was not true. Sopacko did not receive progress payments and, therefore, had no limit placed on them. Moreover, no ceiling was placed on Rafco's progress payments during their first MRE contract, MRE1, during which Rafco's start-up costs were paid. Moreover, Bankoff avoided answering the question that Chiesa asked – what was the "origin of [the L-4] ceiling"? That question remains unanswered even until today.

293. Freedom needed the CFM to meet current production requirements. By diverting this CFM, the Government interfered with Freedom's ability to produce its own MRE cases under the Contract, resulting in schedule delays that could not be recovered. *See* R4, tab FT436; R4, tab 194 (January 1986 Contract Management Alert – short on brownies).

Freedom's March 21, 1986 Claim

294. On March 21, 1986, Freedom provided a draft claim for approximately $3.4 million to DLAM's Ray Chiesa. R4, tab F1.

295. On March 26, 1986, Freedom representatives met with Mr. Liebman, Mr. Bankoff, and other Government representatives to discuss Freedom's $3.4 million draft claim. At that meeting, the Government informed Freedom that it was willing to: (1) reinstate to the contract the previously terminated for default quantity of 114,758 cases and revise the contract price accordingly; (2) extend the delivery schedule on a "no cost" basis to October 1986; (3) return the $200,000 in monetary consideration taken for June 1985 and November 1985 delivery schedule extensions; and (4) pay Freedom approximately $500,000 in capital type costs that had been allowed by the PCO in the negotiation of the MRE-5 contract (but not paid by Mr. Liebman). R4, tab M22.

295.a. The formal claim was submitted to Frank Bankoff on April 24, 1986. R4, tab FT266.

296. Freedom and the Government were not able to settle the claim because Freedom (1) wanted assurance of participation in the MRE-7 procurement and (2) refused to waive the $3.4 million claim. The meeting concluded with DPSC advising Freedom that it was going to refer the entire claim to DLA Headquarters for resolution. *Id.*

Failure To Make Payments For MREs Delivered And Accepted

297. The Contract contained the standard Payments clause that appeared on the Standard Form 32, General Provisions (R4, tab 2), which authorized payment to the contractor for supplies and services delivered and accepted. Between March 13, 1986 and April 3, 1987, Freedom invoiced a total of $1,907,979 on 33 DD Form 250 invoices ("DD250"s) which were approved by the Government. R4, tab FT422(PPChart). These DD250s represented shipments of completed and accepted MRE cases under the Contract.

298. Under the terms of the Contract, Freedom was entitled to payment within 5 to 10 days after submission of a proper invoice (R4, tab F2), and for any such invoice remaining unpaid after 30 days, Freedom was entitled to interest on the amount due in accordance with the Prompt Payment Act.

299. The Government was entitled to liquidate outstanding progress payments against the total amount of the invoice, thereby entitling Freedom to a payment of the total value of the invoice less the amount representing the agreed liquidation rate (*i.e.*, 82.6%). Freedom did not receive any net payments against these 33 invoices which were submitted between March 13, 1986 and April 3, 1987. Liebman had no legitimate reason to withhold payment as the Government never disputed the amounts due under any of the invoices or acceptability of the shipments. Freedom is automatically entitled to interest on the amounts due in accordance with the Prompt Payment Act.

300. Freedom wrote to the Government and demanded payment for the outstanding invoices. R4, tab F126, tab FT276. These demands were ignored.

301. The Government presented internal Government documentation at the hearing allegedly showing that 28 of the 33 invoices had been paid by progress payment liquidation. Four payments were at a 95% liquidation rate and 24 were at a 100% liquidation rate. Tr. 1116-17, 1122-26. Freedom never received notice of these "payments." Freedom did not receive notice of these "payments" during the active life of the contract. Freedom first learned of the "payments" when it began preparation for its earlier litigation to overturn the default termination.

302. The Government now has promised to pay Freedom the principal amount of five of those thirty-three invoices (i.e., FNY 0172, FNY 0244, FNY 0297, FNY 0298, FNY 0329; see Tr. 1129-30) as part of an agreed settlement of Freedom's Termination for Convenience Proposal. *See* Exhibit 1 hereto.

303. When Freedom receives payment for these five invoices as part of the Termination of Convenience settlement reached by the parties, its claim for these payments will be withdrawn from before the Board. In any case, Freedom continues to dispute the alleged payment by the Government of the other 28 invoices and claims entitlement herein. In addition, Freedom has specifically reserved its rights, as part of the Termination for Convenience settlement, to claim before the Board all other impact damages caused by the late payment of invoices, both DD 250 and progress payments.

100% Progress Payment Liquidation

304. On 29 October 1986, Liebman took a drastic and catastrophic action towards Freedom when he decided to liquidate progress payments at the rate of 100%. R4, tab F173.

Liebman imposed this liquidation rate to put the "finishing touches" on Freedom. The liquidation of progress payments at the rate of 100% meant that Freedom would receive no net payment at all on any of the invoices submitted for delivered MREs. The 100% liquidation was a totally unwarranted act which Liebman was not able to justify.

305. At no time did Freedom stop working or continue to make progress on the Contract. Despite the considerable cost overrun which Freedom was experiencing because of the Government's continuing acts and omissions, Henry Thomas never gave up and managed to deliver to the Government 512,462 cases (6,916 cases toward MRE VI) out of a total of 620,304 MRE cases in spite of seemingly insurmountable obstacles. R4, tab F172, tab F183, tab 193 (Plant Visit Reports showing progress), tab 194, p.50 (tally of cases shipped).

306. Liebman was justifying his action by alleging the necessity of protecting the Government's financial interest against a contractor who was not making progress. In fact, the real impediment to Freedom's performance and inability to make further progress was the Government itself on accounts of its failure to provide the necessary GFM materials to Freedom and Liebman's refusal to pay monies rightfully due Freedom.

307. Liebman's unwarranted 100% liquidation signaled a death knell for Freedom in that it starved Freedom of much needed resources for continuing the project and which conveyed the worst message to Freedom's financial backer, Bankers, and to Freedom's subcontractors.

The Government's Failure To Provide Freedom With GFM

308. Revised delivery schedules were negotiated by Freedom and the Government in Modifications P00025 and P00028. R4, tab 133, tab 144. However, the Government breached its obligation under these modifications when, *inter alia*, it failed to provide the required GFM

that Freedom was relying upon in order to meet those schedules and to complete the balance of the Contract.

309. In one specific instance of late GFM, fruit jellies caused a production delay in July 1986. Freedom did, in fact, release the Government from any monetary claim for that particular late delivery of fruit jellies, as part of a settlement embodied within Modification P00028. However, the Government continued to fail in its obligation to provide necessary GFM to Freedom during the August 1986 through March 1987 time frame. *See* Findings 312-316.

310. The parties executed Modification P00025 on May 29, 1986 ("Mod 25"). R4, tab F133. This Modification purported to reinstate 114,758 MRE cases that had previously been improperly terminated for default. *Id.* Under Mod 25, the reinstated cases were to be produced in the MRE-6 rather than the MRE-5 configuration. *Id.* The Government, with the full intention of rendering Freedom's performance impossible, failed to procure the required MRE-6 configuration GFM essential to Freedom's performance. Tr. 1278-79, 1299. Neither did they return to Freedom the MRE-5 GFM that they had previously confiscated from Freedom's plant.

311. The details of the Government acts regarding GFM follow.

312. The evidence shows that despite performance improvements, Freedom was able to ship only 46,260 cases towards the 80,000 cases due by September 1986 per Mod 25. The main causes of the shortfall for the August production slippages and down time were stock outages of GFM fruit mix and potato patties. R4, tab 144, tab 145.

313. By letter to the PCO dated 17 September 1986 (R4, tab 153; *see* R4, tab M33, tab 194), Freedom told the Government that the lack of GFM fruit and potato patties was causing delivery slippages and Freedom proposed a revised delivery schedule. During the last week of

September 1986 accessory production had to be shut down for approximately one week, until on or about October 3, because of a stock outage of a particular GFM item, cream. R4, tab 164.

314. By October 22, 1986, Freedom had received all of the contractor furnished material (CFM) needed to begin producing cases in the MRE-6 configuration, but still had not received GFM beef slices, diced turkey, ground beef or ham slices. R4, tab F178. In an October 22, 1986 letter, Freedom advised the PCO that it was shutting down assembly production of MRE-6 cases, effective immediately, due to "lack of GFM." R4, tab F170.

315. Due to a lack of GFM entrees for MRE-6 cases, Freedom ceased final case assembly on October 22, 1986 and laid off 146 production workers out of approximately 400 employees. R4, tab F170, tab M44. As admitted by the PCO in testimony, except for crackers, DPSC never purchased a sufficient amount of MRE-6 configured components to permit assembly of the entire reinstated quantity of 114,758 cases. Tr. 718-721. Despite the reduced production force, Freedom completed and shipped by November 28, 1986 a total of 512,462 cases including 6,916 MRE-6 cases. R4, tab 194, p.50.

316. Notwithstanding its discontinuance of production in November 1986, Freedom still wished to complete the contract and was expecting to receive an award for the MRE-7 procurement. It had submitted the lowest acceptable price and received a positive pre-award survey recommending award. R4, tab F159, tab F182, FT308. Freedom used this period of down time at its plant to make modifications to its final assembly area and requested an extension for delivering the contract balance of 107,842 cases of the MRE-6 configuration through January and February 1987, conditioned upon receiving the necessary GFM. R4, tab 165, tab FT 308, tab FT309.

317. Freedom is entitled to an equitable adjustment as a result of the failure of the Government to provide the necessary GFM. The repeated failure of the Government to provide GFM resulted in increased costs as Freedom attempted to work rescheduling and re-sequencing and, ultimately, Freedom suffered complete production shutdowns.

318. Mr. Martin J. Bernstein, Appellant's expert witness in the area of industrial and manufacturing engineering testified that there were twenty-one (21) different product assembly lines and that 160 items had to be packaged. Tr. 894. He said that the operation was a flow line assembly and Freedom could not assemble any meal unless it had GFM accessory packs. Tr. 893. Lack of GFM, he said, would cause major plant disruption. Tr. 894.

319. Mr. Bernstein testified that substitutions by the Government, although allowed by the terms of the Contract, could also have a major impact or disruptive affect. Tr. 895. He said there were no substitutes for such materials as crackers, and that if a contractor did not have these materials, it was a "90% show stopper." Tr. 908, 909.

320. Mr. Bernstein testified that lack of Government furnished material could shut down Freedom's entire operation. Tr. 916.

321. Another Freedom witness, Mr. Philip Lewis, testified that based on his education and industrial experience, he had been hired to train Freedom personnel on the production assembly line. Lewis, who was with Thomas and Freedom from the beginning testified that he observed the effect on the operation of the missing GFM. Tr. 1085.

322. Lewis said that the Government never provided any notice that there was going to be a change in the schedule of delivery of GFM. *Id.* He said that Freedom's workforce was geared up and ready only to find out that GFM was not forthcoming:

> Without the necessary GFM, it was impossible to perform any work on the product that was to be delivered. . . . [T]he company was really strangled; the resources that it needed to continue were taken away from it and so you were left with a situation that dictated only one circumstance and that was closure of the company.

Tr. 1086.

323. Lewis testified that a single day's delay in receipt of GFM did not mean a one day production delay. He said that anything that interferes with a production process can cause a delay that is a magnification of the actual time of the event. It is a ripple effect, he said, and that there is a human ingredient involved. Tr.1088.

> When you begin to upset a schedule of assembly, of storage of inventory, of distribution, to a line, and you add to it that things that happen in a normal course of events - absence of a key person because of illness - your very likely to develop a longer delay than the specific period that the GFM was not available.

Tr. 1088.

Government-Caused Delays Increased Freedom's Costs

324. Government-caused delays forced Freedom to continue to incur the costs of maintaining its facility and production capability in place while awaiting resolution of the numerous and overlapping purtibations. The Government's failure to provide the required and necessary financing and GFM resulted in several stoppages and slowdowns that could not be predicated or managed as to the likelihood and frequency of occurrence nor as to the time of resolution. Tr. 1082, 1085-1088.

325. Freedom took action to mitigate the damage resulting from the Government caused stoppages and slow downs. Freedom would lay-off production workers and then hire them back when funds or GFM became available. The effect, however, was constant disruption.

Tr. 1083.

326. Freedom planned and budgeted its direct labor costs on an eight month production run. This run was to start with a one time phase-in training period. Tr. 1085. The constant lay-offs and rehiring totaling disrupted this plan. Freedom was forced to run an on-going phase-in training program because it could never bring back the majority of people it was forced to furlough. Tr. 1083, 1088.

327. Lewis, who was in charge of training operations at Freedom, testified about the impact on a workforce that faced lay-offs and subsequent rehiring. Referring to a loss of people because Freedom was forced to substitute slower equipment than planned because of a lack of Government financing, he said:

> And the people that the company lost were the key people. Those people who ought to be foreman and line leaders. And we were never able to get them back. So that changed - - it caused a slow down, and it had a resultant adverse impact on the morale of everyone who worked there, not only the people on the floor, but all of the executives as well.

Tr. 1083, 1088.

328. In summary, and as previously explained, extensive delay and disruption to the program was caused by Government acts and omissions as detailed in Findings herein for which Freedom is entitled to the increased costs resulting therefrom:

- Improper denials or suspension of progress payments related to (1) alleged inadequate financial condition, (2) alleged lack of progress, (3) alleged improper accounting treatment of costs, (4) alleged unallowability of costs, (5) alleged inadequate accounting system, and (6) improper offset of costs. Findings 87-94;

95-99; 111-125; 157-159

- Interference in Freedom's performance by (1) directly discouraging outside sources of capital, (2) directly discouraging critical suppliers, and (3) meddling in Freedom's internal management decisions. Findings 128-148; 268-293; 324-327.
- Imposition of an unnecessary novation agreement effective April 1985, resulting in a 5-month delay in completion of the pre-production period. Findings 166-175. Pre-production was supposed to be completed by May 1985 and instead was not completed until October - November 1985. See Quantum Section.
- The failure to pay for allowable incurred costs, *i.e.* $400,000 offset for the sale of the lease option, and the DAR deviation issue (July 1985 to June 1986), resulting in a delay in the installation of the automated lot tracking system. Findings 236-238.
- The failure to make payments, *i.e.*, DD250s (Findings 297-303) the imposition of an improper liquidation rate of 100% as of October 29, 1986 (Findings 304-307), and the suspension of progress payment in December of 1986, which caused a significant delay.
- The Government's failure to provide GFM, which resulted in production shutdowns, causing a 4-month delay from September through November 1986. Findings 308-315; 317-323.

- Failure to receive CFM because of the Government's breach of Mod 20 (the unauthorized commandeering of material that had been set aside at vendors), which resulted in further delay. Findings 292-293.
- Improper rejection of MRE units and change in inspection criteria, as discussed below, which resulted in delay. Findings 333-339.

The Government's Failure To Cooperate In The Administration Of The Contract (Maladministration)

329. The Government breached its duty to cooperate and not to interfere with the performance of Freedom's MRE-5 contract. *See* Finding 328.

330. As set forth above, the Government: (1) improperly administered progress payments throughout the MRE-5 contract, (2) disrupted and interfered with Freedom's relationship with its financing institutions, vendors, and suppliers, (3) failed to provide GFM to enable Freedom to complete the MRE-5 contract, (4) failed to cooperate with Freedom in connection with MRE-6 and MRE-7 procurements, and (5) otherwise repeatedly breached the MRE-5 contract.

331. Although Freedom protested to the Government concerning its wrongful conduct, the Government never corrected the problems.

332. Even in the face of Liebman's failure to cooperate, Freedom did not stop performance or default in its obligations as could have been reasonably expected. Rather, Freedom continued to make progress even without the Government's required financial participation, although at a slower rate and with mounting cost overruns. Findings 149-156.

Government Changes In Inspection Method and Additional Testing Requirements

Changes in Inspection Method

333. Inspection requirements for MREs in process were set forth in the Contractor Inspection System (CIS) and Plan for Inspection Job ("Plan," R4, tab FT106).

334. The CIS and Plan designated a specific point in the process where Government inspection was to occur. Tr. 2084. That point was a line on a moving belt where the cases came across after they were assembled. *Id.* Thus, the Government inspection was a "moving-lot inspection." As intended by the CIS, and Plan, samples from the moving-lot were to be pulled by both Freedom and the Government inspector from the line and inspected. Another method of inspection was called out but only for lots previously rejected during moving line inspection that had been reworked. This was referred to as stationary lot inspection and it was performed on completely assembled and palletized cases. Tr. 2084-85.

335. Mr. Leon Cabes who was employed by Freedom during the course of the MRE-5 contract testified concerning the Government's inspection. He stated that at the beginning of production, the Government was performing moving lot inspections as agreed upon. Freedom had its equipment on the line and the testing was done there. Tr. 2086. The Government inspector (or "AVI," as he was called) was at that spot (as required), pulling from the same point that Freedom was under the CIS and Plan that had been generated. Tr. 2087.

336. After Lot 1 was inspected and passed, using moving lot inspection, the AVI stopped performing moving lot inspection. The AVI's position was that it should be using stationary inspection. *Id.*

336.a. The AVI then refused, until November 15, 1985, even to perform stationary lot inspection. The AVI improperly claimed that Freedom's capping and strapping material had failed DPSC's strength tests. Liebman later admitted that there was nothing wrong with the strapping. R4, tab FT437.

336.b. Between November 15, 1985 and December 19, 1985, the AVI did infrequent stationary lot inspections. Stationary lot inspections are done after the product leaves the production floor. Stationary lot inspections will not quickly identify a problem with production equipment. Tr. 2085-90; R4, tab FT243, Bates 01649.

336.c. Moving lot inspection is done while the product is on the production line. Defects caused by production equipment are quickly detected and corrected. *Id.*

336.d. Because of the long delay in returning to moving lot inspection, numerous lots were produced with tears in the pouches caused by metal burs on particular production equipment. Between Lot 2 and Lot 23 Freedom experienced continuous rejections caused by the undetected bur problem. Had the Government met its obligation to perform moving lot inspection, the defective pouches would have been quickly detected, the equipment corrected and substantial rework would have been avoided. *Id.*

337. Moving lot inspection was reintroduced on lot 24 in December 1985. Lot 24 and virtually every lot thereafter, passed inspection. Tr. 2095. Liebman admitted in writing that Freedom Industries rejection rate dropped from 99% in December, 1985 to 2% in January, 1986. R4, tab194(1-3) January 1986, Contract Management Alert).

338. Cabes was able to resolve the problem using Mr. Dave Corry. Mr. Corry, a Freedom employee, had previously been an AVI inspector who had experience inspecting MREs

at MRE assembler Sopakco. Mr. Corry reviewed the defects and the point of inspection. He convinced the AVIs to return to the moving line inspection method that had been agreed upon initially. Tr. 2090. The rejections abruptly stopped. R4, tab PT243l, Bates 01649.

339. Cabes said that the effect of the Government's change in inspection method resulted in a three (3) month delay for the period October, November and December 1986. Tr. 2090-2091. The problem impacted 31,817 cases that had to be reworked or stripped down and put back into production. Tr. 2097; R4, tab FT243, Bates 01649.

Additional Testing

340. The Government imposed additional testing requirements on Freedom in March 1986. Tr. 2098. The Government had discovered micro holes in pouches produced by Star Food Processing. Freedom had Star Food's product in its warehouse as contractor furnished material Tr. 2098. The items in questions were the individual thermal stabilized retort products, apple sauce, beans and tomatoes and meatballs. As a result, the items that were produced by Star Food were put on a medical hold in the warehouse by the Government and Freedom was not able to use any of that product. Tr. 2099.

341. Cabes testified that substituted items in the meal bags were allowed by the Government. However, the substituted meal items were not always the same size as the ones for which they were substituted, which had a negative impact on the operation. Tr. 2103. It affected the efficiency and speed of Freedom's assembly of cases. It slowed down the labor, and more people were needed to work with the substitutes. It caused a bulging of the case, and sealing problems developed. Tr. 2014. It also depleted the supply after the substitutions were made which affected efficiency of operation downstream. *Id.*

342. The Government also required additional testing of the retort pouches before insertion in the meal bags. Freedom was required to use a flourescent dye called Zyglo which would be introduced inside the pouch to detect the micro holes. Tr. 2105. Cabes pointed out that this was a technique that was not previously used in the food assembly industry. Freedom was required to take approximately 200 samples of pouches from Star Foods and test them with Zyglo. Tr. 2106. In other words, Freedom had to perform a visual inspection of 200 samples to look for holes. Tr. 2106.

343. Cabes said that based on his knowledge and experience, the additional testing using Zyglo was "an absurdity." Tr. 2107. These holes, he said, were demonstrated to be smaller than a hole that would allow bacteria to get through. Thus, even if such holes existed, they would be "micro" holes -- they would have no effect on a contamination level of bacteria gaining entrance and would be invisible to visual inspection. *Id.*

344. Cabes pointed out that the extra testing slowed down the process and went on for about 6 to 8 months. Tr. 2107. The tasks were not included in Freedom's contract originally. It required additional people to perform the sampling and testing and additional time to produce cases as a result of these additional requirements. PCO Bankoff apparently recognized that imposing these testing requirements on Freedom constituted a constructive change of the Contract. R4, tab 435, Bates 04227.

Modifications P00028 and P00029

345. On 7 August 1986, Freedom and DPSC executed Modification P0028 ("Mod 28"). R4, tab 144. DPSC amended the delivery schedule as follows:

QUANTITY	DELIVERY DATE
80,000	12 Aug 1986
80,000	10 Sept 1986
15,304	10 Oct 1986
64,696	10 Oct 1986
50,062	12 Nov 1986

Id. DPSC also increased the current "ceiling" of 13 million on progress payments using a completed methodology rather than incurred costs as follows:

COMPLETION AND ACCEPTANCE	CEILING
333,000 cases	$13,000,000.00
410,000 cases	14,000,000.00
490,000 cases	15,000,000.00
570,000 cases	15,800,000.00

Id. In return for the amended delivery schedule, Freedom acknowledged "that it has no claim whatsoever for any consideration or damages, monetary or otherwise, resulting from lack of Government-furnished material jellies during the period of 16-28 July 1986." *Id.* The modification ended with the following statement:

> This document contains the complete agreement of the parties. There are no collateral agreements, reservations or understandings other than expressly set forth herein. It is agreed that no subsequent modification of this agreement shall be binding unless reduced to writing and signed by both parties.

Id.

346. DCAA, upon analyzing Mod 28, recommended that Liebman pay $699,904 of Freedom's outstanding progress payment requests. R4, tab 158.

347. On 22 September 1986, Freedom informed Bankoff that its finances were strained severely due to the manner in which it was receiving progress payments. R4, tab F157. Because the Government tied the release of progress payments to the completion of delivered cases (Mod 28), the Government prevented Freedom from obtaining funds which were necessary to acquire materials, which, in turn, were necessary to deliver the MREs . R4, tab F157.

348. [Intentionally left blank.]

349. On September 26, 1986, Thomas and Bankoff were negotiating the terms of Modification P00029 ("Mod 29"). During those negotiations, Bankoff informed Thomas that upon execution of Mod 29:

> the current progress payment ceiling for the subject contract, per modification P00028, will be $14,900,725.00 based on delivery of 482,058 cases. To date you have been paid $14,178,838.00. This leaves a balance of $721,887.00 available to you. This amount will be paid to you by DCASMA-N.Y. against progress payment request submitted by Freedom N.Y., Inc.

R4, tab F165. Liebman had approved payment of approximately $700,000 in progress payments. R4, tab F164. Thomas understood that if he executed Mod 29, the Government would release these progress payment funds. R4, tab F165. Freedom desperately needed this money and an MRE-7 award.

350. On October 3, 1986, Bankoff phoned Liebman and instructed him to hold up the payment of $700,000.00 due Freedom until Freedom executed Mod 29. R4, tab F164. Bankoff believed that Mod 29 contained terms favorable to the Government; namely, a release of claims.

Bankoff sought to obtain this release by withholding payment of progress payments that Freedom desperately needed until after Freedom was forced to sign Mod 29. Liebman complied. *Id.*

351. Thomas had no choice but to execute Mod 29 because it was the only way the Government would release the monies due under Mod 28. Freedom had to continue performing so Freedom would receive an MRE-7 award.

MRE-7

352. As part of DCASMA-NY's pre-award survey of Freedom for MRE-7, DCASMA-NY received a letter dated September 22, 1986 from Bankers. In it, Bankers informed DCASMA-NY that it would extend Freedom a $6,000,000.00 line of credit in connection with the MRE-7 contract. R4, tab M27, tab F163.

353. On September 25, 1986, DPSC amended the MRE-7 solicitation. *Id.*; R4, tab M35. DPSC informed Freedom that it planned to make four, instead of three awards under the MRE-7 solicitation but that the total quantity sought would remain roughly 4.3 million cases. Freedom, therefore, reasonably believed that the Government was going to fulfill its obligation to maintain Freedom in the IPP Program. Moreover, Freedom believed that MRE-7 would provide means to obtain needed financing for MRE-5 completion.

354. On September 25, 1986, DCASMA-NY completed a pre-award survey of Freedom in connection with the MRE-7 solicitation. As part of the financial analysis (R4, tab F182)(Stokes Analysis of 9/24/86), Stokes discussed Freedom's $6 million line of credit from

Bankers and concluded that Freedom had the necessary financing to complete the 1.5 million cases. *Id.* The pre-award survey was positive and recommended that DPSC award Freedom a contract for 867,792 cases of MREs. R4, tab F159, tab F182.

355. Freedom knew that it had passed its pre-award survey for the MRE-7 procurement. Freedom also understood that its price was lower than CINPAC's price.

356. On 18 November 1986, Bankoff ordered a pre-award resurvey of Freedom for MRE-7. R4, tab F192.

357. On 2 December 1986, DPSC amended the MRE-7 solicitation to reduce the number of anticipated awards from four back to three. *See* R4, tab M054.

358. On 16 December 1986, DCASR-NY completed the financial capability portion of the pre-award resurvey for MRE-7. R4, tab F189. Although Bankers had granted Freedom a $6 million line of credit and had agreed not to require repayment of Freedom's current overdue loans of $3 million, DCASR-NY concluded that Freedom lacked the financial capability to perform the MRE-7 contract and recommended "no-award." R4, tab F189 (Stokes Analysis of 12/16/86). R4, tab 165.

359. CINPAC, which had replaced Freedom for the award of MRE-6, received the MRE-7 award and continued to receive MRE awards that should have been made to Freedom. See R4, tab 379, tab FT 383.

The Implied-in-Fact Agreement Generally[34]

360. The Meal, Ready-to-Eat (MRE) ration was a mobilization essential item that was procured by negotiation pursuant to 10 U.S.C. § 2304(a)(16). Section "(a)(16)" was, in the early 1980s, an exception to the Armed Services Procurement Act (10 U.S.C. § 2303) general requirement for formal advertising. *Id.*

361. In accordance with Defense Acquisition Regulation (DAR) 3-216.2, MRE rations were selected supplies approved for production planning under the Industrial Preparedness Program (IPP). Procurement of MREs was limited only to "planned producers" with whom industrial preparedness agreements for these items had been entered into with DLA's DPSC. R4, tab FT004.

362. The goals of the IPP program were to establish, develop, and maintain industrial planned producers of mobilization essential items in order to meet the mobilization needs of the nation's armed forces in the event of war or a national emergency. R4, tab FT001. These goals were reflected in the Determinations and Findings (D&F) issued for each MRE procurement. *Op cit.*

363. "Mobilization essential item" are those items that are essential to support troops such as boots, uniforms, and food. Tr. 47. Some mobilization essential items, however, are so

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[34]The following proposed findings of fact, Findings 360-408, are directed to Freedom's claim that an implied-in-fact agreement existed between Freedom and the Government that Freedom would be maintained as an MRE contractor. These proposed findings supplement those set forth earlier in this section which relate to the IPP/MRE Program.

critical for combat that the military cannot go into battle without them. *Id.* The military designates these as "war stoppers." *Id.* Examples include ammunition and guns. *Id.* MREs are "war stoppers." *Id.*

364. Under the IPP program, DoD does planning during peace time for adequate quantities of "war stoppers" in the event of war or national emergency. Tr. 47, 48. The requirement is expressed as a number of units per month (for MREs, cases per month). *Id.*

365. The DoD-established requirement is sent for action to DPSC, the agency responsible and authorized to assure the necessary availability. This authorization includes procurement responsibility. Tr. 48

366. Because MREs are not commercially available (R4, tab FT004), DoD must develop and maintain MRE planned producers. Tr. 49. DoD's primary goal in establishing these planned producers is to assure that such planned producers are available and capable of escalating production from peace time to war or national emergency levels. R4, tab FT019, tab FT032.

367. To meet the military's war-time production levels, MRE contractors have to be able to "ramp up" drastically from their peace time levels. In 1981, for example, MRE contractors were required to increase their peace time production of 3.5 million cases per year to a mobilization requirement of 10 to 15 times their MSR to 4.5 million cases *per month*. Tr. 50. The increase had to be achieved by M+90, *i.e.*, within 90 days of mobilization. Tr. 50-51.

368. In order for MRE contractors to achieve that sharp increase in production, they had to be operating from a warm base, *i.e.*, actively producing. Tr. 51; R4, tab FT019, tab

FT032. It was essential for mobilization purposes that MRE contractors be kept in production during peace time. *Id*

369. MRE production, for the established MRE producers, essentially was their only business. *Id.* If the Government did not award annual contracts to these contractors, not only would they be unable to "ramp up" their production during an emergency, they likely would go out of business. *Id.*

370. Because of the necessity to keep MRE producers in production, DPSC anticipated awarding, and each MRE assembler anticipated receiving, a contract every year at the contractor's minimum sustaining rate (MSR).[35] Tr. 52. DPSC determined the MSR for each MRE producer to determine what portion of the year's award that each contractor required during peace time for its MSR. *Id.*

371. Once an MRE assembler was qualified and took on the burdens of an MRE IPP Planned Producer, the Government, of necessity, implicitly agreed that it would continue to award MSR/MRE contracts in order to maintain critical mobilization capacity. Tr. 50, 53. As the Honorable Frank Carlucci attested when he executed the MRE 2 D&F on April 3, 1981:

> Procurement is necessary to maintain [the MRE assemblers] as viable producers of MREs, thereby maintaining employee skills developed under the production test contracts. And in order to limit competition to planned producers with whom the Department of Defense has negotiated industrial preparedness agreements.

R4, tab FT004, ¶5.

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[35]MSR is the rate that a contractor can produce on a monthly basis without increasing the cost of the ration over what the Government normally would pay during peace time. Tr. 52.

372. DoD assured annual awards to the qualified IPP MRE contractors by limiting and restricting the negotiations only to planned producers. Tr. 53, 55; R4, tab F7(MRE-4 D&F: "Procurement will be limited to firms with current industrial preparedness planning agreements with the Department of Defense for MRE rations"). The only "competition" was among the assemblers themselves for the percentage of each procurement that the contractor would be awarded. That percentage was based on M+90 days production capability and price. *E.g.*, R4, tab F7.

373. The primary objective of the IPP Program was not to purchase the item during peace time at the greatest cost savings, but rather to develop and maintain adequate *sources* of supply for war time or times of national emergency. Tr. 83-84.

374. The agreement to become an MRE contractor, therefore, is based on an agreement between DPSC and the contractor. The contractor agrees to invest its time, effort, and money to become capable of: (1) producing MREs during peacetime; and, more importantly, (2) ramping up to the required mobilization rate of production at M+90. In consideration for that commitment, the Government agrees to award a contract to each qualified contractor each year, based on the contractor's MSR and production capability.

The Implied-in-Fact Agreement With Freedom

375. From Freedom's initial contact with the MRE program, the Department of Defense made clear to Freedom three points: (1) that MREs were critical to the national defense, (2) that the Department of Defense would maintain a mobilization base for these critical items,

and (3) that producers that were formally in that base, through the Industrial Preparedness Planned Producer Program, (hereinafter "planned producers") would be constantly maintained on a "hot base" basis.[36]

376. As of August 27, 1981, DoD informed Freedom that "(o)nly two companies have ever produced and delivered cases of MRE rations" and these were the only two planned producers, Sopakco and Rafco. R4, tab FT005, Bates 00063.

377. Freedom was directed by DoD (*id.*) to the April 3, 1981 Determination & Finding (D&F) covering CYs '81 and '82 (MRE 2). This D&F made Freedom aware that DoD's plan was to keep the planned producers constantly in "warm base" status as follows:

> 3. The U.S. Army developed the MRE to meet the growing need fort a lighter weight, less restrictive combat ration. There is no commercial equivalent to the MRE ration, and the production of rations in retort pouches for the MRE is based on state-of-the-art technology that is still evolving. The several different types of preservative packaging used for the components of the MRE demand extremely close supervision and quality control to preclude contamination or infestation of components.

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[36]The DoD Industrial Preparedness Manual in effect as of the award of Freedom's MRE 5 contract defined "Hot Base" as:

> A planned producer's manufacturing facility which is currently producing, or will be producing the planned item when M-Day occurs.

There is no definition of "Warm Base." DLA/DPSC most often applies the term "warm base" to a currently producing, *i.e.*, hot base facility. To be consistent, this Brief also will use the term "warm base."

> **4. Procurement by negotiation is necessary in order to maintain Southern Packaging and Storage Co., Inc of Mullins, South Carolina, and Right Away Foods Corp. of McAllen, Texas, as viable producers of MREs (thereby maintaining employee skills developed under the production test contracts) and in order to limit competition for MREs to planned producers with whom the Department of Defense has negotiated industrial preparedness agreements.**

R4, tab FT004 (emphasis added).

378. Freedom understood that there was a *quid pro quo* for becoming a "warm base" producer of MREs. Freedom informed the Defense Logisitics Agency (DLA) of its understanding in a letter of October 26, 1981 to DLA's Executive Director of Contracting, Raymond F. Chiesa. Freedom told Mr. Chiesa:

> Companies such as Southern Packaging and Storage Company and Right Away Foods, who hold Industrial Preparedness Agreements (a)(16), have negotiated prices **and are guaranteed business prior to the Request for Formal Proposals (RFP).**

R4, tab FT007 (emphasis added).

379. Freedom also knew that the Government was willing to invest heavily in the development of warm base MRE producers. An investment that would be returned **only** if the producer was consistently maintained in the MRE program. R4, tab FT010, Bates 00073-76. The GAO formally stated this in their 1982 report on RAFCOs MRE pricing when they identified Rafco's first MRE planned producer contract as "**the first in a series of contracts.**" *Id.* at Bates 00077.

380. Freedom knew it would have to make the investment required to become a planned producer in order for it to be kept as a warm base. It also knew that the investment would be very substantial. *Id.*, Bates 00081, last sentence.

381. By letter of September 28, 1981, Freedom Industries told the DPSC Industrial Preparedness Specialist that it was "ready, willing, and able," to become a planned producer and asked for the necessary procedures. R4, tab FT006. Copy of this letter was sent to Mr.Chiesa on October 26, 1981. R4, tab FT008. This letter was provided to contracting officer Michael Cunningham for action. R4, tab FT008..

382. Mr. Chiesa responded by letter of December 1, 1981. Although he responded point by point to Freedom's complaints, he never denied that planned producers for MREs were **guaranteed** business prior to the RFP. R4, tab FT009.

383. On or about March 3, 1982, Freedom was again made abruptly aware of DLA's commitments to its MRE planned producers. On that date the Under Secretary of Defense for Research and Engineering, Rrichard D. DeLauer, issued the D&F covering the CY 1983 MRE buy (MRE 3). It reiterated the absolute commitment to keep Sopakco and Rafco as "viable," *i.e.*, warm base, MRE producers. R4, tab FT011.

384. Freedom complained of its exclusion to Secretary DeLauer by letter of March 10, 1982. Freedom highlighted its attempt to become a planned producer and its investment on account thereof. R4, tab FT012.

385. Awards were made to Sopakco and Rafco on March 18, 1982. Freedom was approved as a planned producer on March 30, 1982. R4, tab FT014.

386. Secretary DeLauer responded on May 17, 1982. He explained the awards to SOPAKCO and Rafco, *inter alia*, as necessary "to prevent a break in production." *Id.*

387. On December 16, 1982 Secretary DeLauer issued the D&F for MRE 4. This covered the CY 1984 MRE requirement (MRE 4). For the first time, the D&F cited Freedom as a planned producer. R4, tab FT019

388. Freedom was aware of and was relying on D&Fs for prior MRE buys in its understanding of the MRE program. All previous D&Fs required award to all planned producers. The MRE 4 D&F allowed the possibility that only two of the three planned producers would receive an award. R4, tab FT019.

389. Freedom tried to clarify the situation. On March 29, 1983, Freedom put the question directly to the DPSC PCO, Mr. Michael Cunningham. Freedom highlighted the investment it was making to become "a ration production facility for use by the Department of Defense in peace and wartime." R4, tab FT021, Bates 00181. Freedom also asked Cunningham to affirm that such was the intent:

> 1. Should we base our proposal on developing a facility and capability for emergency production of 1,500,000 cases per month, which we believe can be done, of the total need of 5,100,000 cases? or
>
> 2. Should we only develop a capability for providing the requirements of the current offering?
>
> We believe the latter scenario (2) does not provide the capability to meet emergency situations. Further if we develop the capability to meet emergency needs our overhead base becomes quite substantial and would thus probably make our proposal non-competitive on pricing. We would have the problem of sustaining multi-year costs (e.g., rent, improvements, equipment) when the requirements are for one year. If the minimum sustaining rate is in reality a multi-year contract, we could conceivably ameliorate the problem by charging the substantial start-up, equipment

> acquisition, and facility renovation cost off on a multi-year basis. As a start-up we cannot be expected to be price competitive with existing producers.

R4, tab FT021.

390. The record does not indicate that Cunningham responded to this inquiry. Instead, on July 8, 1983, DLA awarded contracts to Sopakco and Rafco, but excluded Freedom. R4, tab FT024(A), Bates 00237.

391. Freedom believed that the Government had breached its obligation to create and maintain Freedom as a warm base MRE producer. On September 1, 1983, Freedom sued. R4, tab FT024.

392. The language of the suit is couched in terms necessary to support an injunction against an award of a Federal Government contract, *i.e.*, Government violation of procurement procedures. It is clear, however, that it was intended to enforce the agreement Freedom believed was in place. The complaint, in pertinent part, stated:

> 13. Defendant illegally, arbitrarily and capriciously awarded contracts under Solicitation DLA13H-83-R-7871 by (1) **failing to adhere to the requirement to provide a reasonable and adequate mobilization base capability,** the achievement of which is required in order to use the 10 U.S.C. 2304(a)(16) negotiation authority and (2) by failing to properly approve and review the representations made on the submitted form 1519s **to insure a realistic and feasible mobilization base capability**
>
> 14. On July 13, 1983 Plaintiff filed a protest against the award to Rafco and Southern Packaging with the General Accounting Office, Docket No. B-212371.
>
> 15. Plaintiff was denied an award **it should have received as a qualified industrial preparedness planned producer of MREs** because Defendants have not followed the applicable procurement laws and regulations. Such actions by

> Defendants will result in irreparable harm to Plaintiff because Plaintiff is likely to go out of business unless the relief sought by Plaintiff is granted and virtually certain to lose its present facility which is especially well suited to MRE production.

R4, tab FT024(A), Bates 00237, 00238 (emphasis added).

393. Faced with the suit, the Government accepted Freedom's position. In fact, it effectively admitted its obligation. By letter of December 9, 1983, DLA ordered DPSC to make MRE-5 awards to all three planned producers. R4, tab FT028, Bates 00331. In return, Freedom dropped its legal action. R4, tab FT034.

394. DLA's December 9th direction went even further. DLA virtually ordered a DPSC response to Freedom's March 29, 1983 inquiry. DLA's directive stated, in pertinent part, that:

> 5. The Procurement Plan should also address fully the issues of using multi-year contracting and the total systems approach.

Id. at Bates 00332.

394.a. The obligation was made absolutely clear by Under Secretary of Defense, James P. Wade in his D&F of February 7, 1984. Secretary Wade stated:

> Procurement by negotiation is necessary to maintain a mobilization base and provide the opportunity to expand the existing base that may decrease the current mobilization shortfall. Procurement will be limited to firms with current industrial preparedness planning agreements with the Department of Defense for MRE rations. As of 5 January 1984, these firms are Southern Packaging and Storage Company, Incorporated of Mullins, South Carolina, Right Away Foods Corporation of McAllen, Texas, and Freedom Industries of Mt. Vernon, New York.

395. DPSC issued Solicitation No. DLA13H-84-R-8257 for MRE-5 on February 15, 1984. R4, tab FT030.

396. The Government fully understood and agreed that there was an implied-in-fact understanding to keep the planned producers on a warm base. In a March 12, 1984 memo signed by DPSC's Chief, Contracting & Production Division, Directorate of Subsistence, and initialed by PCOs Barkewitz and Cunningham, Navy Captain Donald S. Parsons stated:

> 3. . . The present solicitation is being negotiated under 10 U.S.C. 2304(a)(16). This enables the Government to make multiple awards under the same solicitation. The (a)(16) also bases the award on the contractor's Industrial Preparedness Plan (IPP) submitted and approved for this item. This is necessary to insure industries' wartime cability **by keeping the industry geared up and producing each year. . .**
>
> 4. . . The defense critical nature of the MRE Ration requires special negotiation authority **to assure contractors essential to national defense are kept in production.** Without the warm base established by this procedure, the Government cannot meet the services' mobilization needs.

R4, tab FT032 (emphasis added).

397. Freedom submitted its initial proposal on MRE 5 on April 11, 1984. R4, tab FT036.

398. DPSC requested DLA award approval for Freedom on September 21, 1984. The request affirmed that the Government was meeting its obligation under the implied-in-fact understanding, *i.e.*, "to maintain them (Freedom) as an IPP contractor." R4, tab FT054; *Cf.*, FT056.

399. Further, DPSC was on notice that Freedom was taking on a new more expensive production facility in part for "insurance that Freedom would have facility for the future," and that Freedom was reducing its price "to gain entrance as a MRE supplier." R4, tab FT060(A), Bates 00812, tab FT060(B), Bates 00830.

400. DPSC was also aware that Freedom, in reliance on the understanding that it would be maintained as a warm base MRE producer, had divested itself of all other work to concentrate solely on MRE production. R4, tab FT060(C), Bates 00835.

401. On November 6, 1984, the parties negotiated a price of $17,197,928 for 620,304 MRE 5 cases. The price per case was $27.725. R4, tab FT062.

402. On November 7, 1984 DPSC issued a formal D&F verifying that Freedom had made the necessary investment and planning to be able to produce, in the event of an emergency, 600,000 cases of MREs per month 90 days after the declaration of mobilization. This compared to Freedom Industries requirement under its MRE 5 contract of 600,000 cases. R4, tab FT063.

403. On November 15, 1984, DPSC awarded Freedom Contract DLA13H-85-C-0591 on the terms as set forth in Finding 401 above. R4, tab FT068.

404. Freedom, believed it was now a warm-based planned producer for MREs just like Sopakco and Rafco. Freedom undertook costly investment and planning to get this status. Freedom did so in reliance on the implied-in-fact agreement that a warm based MRE planned producer, barring non-performance, would be maintained by the Government. The Government breached that obligation.

405. Freedom made a good faith attempt to perform its MRE 5 contract. It delivered in excess of 6 million meal bags and over 500,000 cases. R4, tab 182 - Mod 30 showing only 107,842 cases yet to be delivered. Freedom, however, was subjected to bad faith maladministration by Government contracting officials. Freedom's MRE-5 Contract was improperly terminated for default on June 22, 1987 even though PCO Bankoff knew Freedom was not in default. R4, tab FT363, M49.

405.a. In 1991, Freedom submitted a certified claim for $21 million. R4, tab F1. PCO Bankoff retaliated with a demand for repayment by Freedom of $1.6 million in unliquidated progress payments. R4, tab FT389. In light of Bankoff's knowledge of the real circumstances (see Finding 405 above), Bankoff's action was unconscionable and effected specifically to harm Freedom.

406. The default, after eleven (11) years of litigation, was overturned and converted to a convenience termination. *Freedom, NY, Inc.*, ASBCA No. 35671, 43965, 96-2 BCA ¶ 28,502.

406.a. In the year 2000, Freedom settled the Board ordered termination for convenience. The settlement established that Freedom did not owe the Government $1.6 million. Rather, the Government owed Freedom $799,947. See Exhibit 1.

407. The bad faith activities of certain Government contracting officials are set forth in detail above. These include, but are not limited to, these specific bad faith actions leading to the illegal termination for default. These activities poisoned the relationship between the Government and Freedom. The result was that the Government breached its implied-in-fact agreement with Freedom. Although Sopacko and Rafco remain MRE planned producers to this day, Freedom never received another MRE contract and was forced out of business.

408. Freedom was illegally replaced, as the implied-in-fact agreement third warm base planned producer, by CINPAC of Ohio. CINPAC was brought into the implied-in-fact agreement by PCO Bankoff in order to harm Freedom, even though the Department of Labor had determined that it could not qualify as a Walsh Healey producer. R4, tab FT278.

409. These Findings have established numerous actions and omission by authorized Government personnel. The record of this case is littered with numerous additional bad faith

Government acts that have not been specifically addressed above. These include, but are not limited to, acts of PCO Bankoff specifically intended to harm, and in fact eliminate, Freedom. To the extent these acts are known to the Board as the result of the proceedings herein, Freedom respectfully requests that the Board take notice.

III. ARGUMENT

A. FREEDOM IS ENTITLED TO AN EQUITABLE ADJUSTMENT TO RECOVER INCREASED COSTS CAUSED BY GOVERNMENT ACTS AND OMISSIONS THAT RESULTED IN CONSTRUCTIVE CHANGES TO THE CONTRACT.

When a contractor performs work beyond contract requirements, and such work resulted from acts or omissions of the Government, a constructive change has occurred and the contractor is entitled to an equitable adjustment in contract price on account of the change. J. Cibinic, Jr. and R. Nash, Jr., *Administration of Government Contracts*, 304-305 (2d Ed. 1985). *See, e.g., Appeal of Kos-Kam, Inc.*, ASBCA Nos. 34682, 35440, 92-1 BCA ¶ 24,546 (1991)(improper rejection of work, or non-acceptance of work or services performed in conformance with contract requirements, and overinspection have been considered constructive changes). During Freedom's performance of the MRE-5 Contract, the Government caused numerous constructive changes to the Contract. Freedom is entitled to compensation for these changes.

1. Freedom Is Entitled To An Equitable Adjustment On Account Of The Government's Breach Of Its Duty To Cooperate And/Or Not To Interfere With Contract Performance.

The Government owes contractors a duty to cooperate in the performance of their contracts. *S.A. Healy Co. v. United States*, 216, Ct. Cl. 172, 576 F.2d 299, 306-07 (1978)(and cases cited there). The Government also owes contractors a related duty not to interfere with or

delay the contractor's performance. *Nichols Dynamics Inc.*, ASBCA Nos. 17949, 18203, 75-2 BCA ¶ 11,556 (1975)(duty not to interfere); *George A. Fuller Co. v. United States*, 108 Ct. Cl. 70, 69 F.Supp. 409 (1947) (duty not to delay performance). When the Government fails to cooperate with the contractor, and/or hinders, interferes with, or delays its performance of work, the Government constructively changes the contract. *Id. See* John Cibinic, Jr. & Ralph C. Nash, Jr., *Administration of Government Contracts*, 352-56 (2d.Ed. 1985), *S.A. Healy Co., supra*, 576 F.2d at 306-08 (duty to cooperate); *George A. Fuller Co.*, 69 F.Supp. at 411-12(duty not to delay performance). To determine whether a breach of either twin duty has occurred, the Board will evaluate whether the Government's actions were reasonable. *Bruce-Andersen Co., Inc.*, ASBCA No. 29411, 88-3 BCA ¶ 21,135 (1988).

The Government failed to cooperate with Freedom in the performance of the MRE-5 Contract. Instead of cooperating, the Government consistently hindered, interfered with, and delayed Freedom's performance. These actions and omissions constitute constructive changes that substantially increased Freedom's cost of performance. These changes are set forth below.

a. Liebman Improperly Denied Progress Payment No. 1.

The Government is obligated to act reasonably in paying progress payment requests. *Virginia Electronics Co., Inc.*, ASBCA No. 18778, 77-1 BCA ¶ 12,393 (1977). The Government must consider such factors as the contractor's financial condition and whether the contractor needs the progress payment to pay its suppliers. *Id.* The Government's failure to pay progress payments in accordance with the payments clause of a contract is considered such a material breach of the contract so as to excuse further performance by the contractor. *H.E. & C.F. Blinne Contracting Co., Inc.*, ENGBCA No. 4174, 83-1 BCA ¶ 16,388 (1983). Particularly where the

progress payment is the contractor's first, the Government will be held responsible for the increased costs of performance that flow from the Government's breach. *R.H.J. Corp.*, ASBCA No. 12404, 69-1 BCA ¶ 7587 (1969); *Aerojet-General Corp.*, ASBCA No. 13548, 70-1 BCA ¶ 8245 (1970)(wrongful refusal to make progress payments imposes a contract change entitling the contractor to the increased costs that resulted from the withholding of progress payments); *Ingalls Shipbuilding Div., Litton Systems, Inc.*, ASBCA 17717, 76-1 BCA ¶ 11,851 (1976)(compensation granted for two-week delay resulting from improper rejection of progress payment request). *See Pilcher, Livingston & Wallace, Inc.*, ASBCA No. 13391, 70-1 BCA ¶ 8331 (1970)(and cases cited there)(failure to make progress payments is breach of contract that will overturn default termination). To cause a constructive change to the contract, the contracting officer did not have to intend to violate the payments clause. The contractor is entitled to relief if the decision not to pay was legally erroneous, regardless of intent. *George T. Johnson and Harvey Case d/b/a J.C. Company, a Co-Patnership v. United States,* 223 Ct. Cl. 210, 618 F.2d 751, 755-56 (1980).

The MRE-5 Contract incorporated the standard progress payment clause for small businesses, DAR 7-104.35(b), Progress Payment Clause for Small Business Concerns, DAC #76-38 (September 1, 1982). That clause required the Government to reimburse Freedom 95% of its incurred allowable costs. Findings 34, 39, 56. The applicable agency guidelines required that payments be paid promptly, normally within 5 to 10 days. R4, Tab F2. Liebman knew that Freedom Industries was a small, disadvantaged business. He knew that the MRE-5 Contract was Freedom Industries' only contract and, therefore, its sole source of revenue. Liebman also knew

that Freedom Industries needed its progress payments in order to pay its "suppliers" -- in the case of Progress Payment No. 1, Freedom Industries' landlord. Findings 67-75.

It was unreasonable, if not arbitrary and capricious, for Liebman to fail to pay Progress Payment No. 1. Liebman repeatedly made unjustified excuses in order to delay making payment:

- Freedom Industries hand-delivered the request to Liebman with an executed copy of the Contract on November 16, 1984, the day after Contract award. Nevertheless, Liebman would not begin processing the request for payment until he received another copy of the Contract through "official channels." This delay lasted until November 29, 1984. Findings 86-89.

- Liebman ordered a pre-payment review of this request by DCAA, despite receiving a positive DCAA audit for Freedom Industries less than two weeks before. This audit, and the previous reviews of Freedom's price proposals, provided Liebman with all of the information he needed to pay the progress payment request without a pre-payment audit. *See* DAR 1-904, Determination of Responsibility and Non Responsibility, 1-905.4, Preaward Surveys; DLAM 32.592-3b, Postaward ACO Review; DLAM 52-590-5b, DCAA Prepayment Audit of Individual Requests (when contractor's accounting system and controls are determined to be adequate, "there shall normally be no prepayment audit of the first progress payment request"). Findings 90-96.

- When Freedom Industries was prepared to submit a second progress payment request, Liebman instructed Freedom Industries instead to combine the first and second requests and "resubmit" it as a first request, knowing that this would delay the payment of the original progress payment. Findings 97-99.

- Liebman rejected the resubmitted request at least twice for purported "errors" on

the form. The "errors" were trivial and did not justify a delay in payment while the form was being revised. Finding 108.

The Board has stated specifically that the Government's penchant for dotted "i"s and crossed "t"s does not justify a delay in progress payments to a contractor that needs them. In *Virginia Electronics, supra*, 77-1 BCA at ¶ 12,393, the contracting officer rejected the contractor's initial request for progress payments because the total contract price indicated on the request form was not correct. The Board held that the "rejection of the initial progress payment request was arbitrary and unreasonable":

> Certainly the bureaucratic passion for dotted "i's" and crossed "t's" should not be allowed to deprive a contractor of monies required to pay for supplies needed to perform the contract. The Government knew the tight financial condition of the contractor and audited each progress payment request because of that condition. It should have known that Appellant probably needed the progress payment to pay its suppliers and get on with performance. Therefore, it was obligated to act reasonably in paying progress payment requests. *See Pilcher, Livingston and Wallace, Inc.*, ASBCA No. 13391, 70-1 BCA ¶ 8331. Assurance of correct entries of total contract amounts on future requests surely did not require the drastic action taken by the Government.

Id.

Liebman's reasons for rejecting Freedom's first progress payment request were equally petty. R4, tab 12; Finding 108. Liebman's failure to pay this request was improper and constituted a compensable constructive change. The amount of the adjustment, reflecting additional costs caused by delay and production inefficiency, is set forth and explained below in

the sections on Damages and Quantum.

b. Liebman Improperly Ordered An Audit of Every Progress Payment.

Liebman abused his discretion by requiring a prepayment audit review of each and every progress payment request submitted by Freedom. The purpose of a pre-payment review is for the ACO to determine that the contractor has, *or is capable of developing*, "effective accounting, production, quality, and management systems." DLAM 32.592-3b, Postaward ACO Review. When a Pre-Award Survey is performed, the ACO may use that information to make this determination. DAR 1-905.4, Preaward Surveys; DLA 32.592-2b, Preaward Actions ("Preaward surveys are an ideal source of information about those areas of a contractor's operation which are of interest in administering progress payments").

Once this determination is made, Government regulations envision a minimum administrative effort by the Government in processing progress payments. DLAM 32.590-5, Administrative Concepts Embodied in DAR E-500 and FAR 32.5 ("As a financing technique, progress payments enjoy a favored position because it requires a minimum of administrative effort by the Government"). When a contractor's accounting system and controls are deemed to be adequate for progress payment purposes, "there shall normally be no prepayment audit of the first progress payment request." DLAM 32.590-5b, DCAA Prepayment Audit of Individual Requests.

> Prepayment reviews at any time are limited to the following circumstances:

> (1) The ACO has reason to doubt the certification signed by the contractor on the Progress Payment Request.
>
> (2) The ACO believes the contract will involve a loss. Whenever the ACO determines prepayment audits is necessary, he shall document the contract file with his rationale, which may apply to one or more successive requests for progress payments.

DLAM 32.590-5b, DCAA Prepayment Audit of Individual Requests. Even then, reviews ordinarily should not be performed more often than quarterly. DLAM 32.592-3b(2), Frequency of Review. Indeed, "it is not expected that this will occur on any but the most doubtful of contractors on a long term basis." *Id.*

Liebman ordered a prepayment audit of every, or almost every, progress payment request. In fact, Liebman placed Freedom Industries on "mandatory review" status. R4, Tab G92, p.8. No justification can be found from the record for these regular reviews. Liebman did not "document the contract file with his rationale," as required by the DLAM. Finding 95. Certainly, Liebman could not, in good faith, have had reason to doubt the contractor's certification or have believed that the Contract involved a loss from the very outset of the MRE-5 Contract. Yet, Liebman ordered prepayment reviews beginning with Freedom's very first progress payment request. *Id.* Mr. Fishbane, Freedom's financial and accounting expert, testified that even Progress Payment No. 1 should have been paid without a prepayment review since the DCAA had approved the Freedom Industries accounting system for progress payment purposes shortly before award. Tr. 2022.

These actions delayed the payment of progress payments to Freedom. Freedom's first progress payment (for $100,310), submitted on November 16, 1984, should have been paid before December 1, 1984. Instead, it was submitted for review not once, but twice, after

Liebman instructed Freedom Industries to resubmit it on December 7, 1984 with additional costs incurred to date (total request, $252,150). Findings 97, 98. As a result, this progress payment request was included in the suspension that Liebman initiated on January 4, 1985 (Findings 111-114), and it was not paid until May 6, 1985. Findings 188, 189. Later progress payment requests that were not suspended or otherwise held for particular reasons required an average of 3 - 5 weeks for payment. R4, Tab FT422(PPChart)(PP #1, 2, 3, 8, 9, 13, 14, 15, 16, 17, 18, 19, 20, 21). Liebman's ordering of regular prepayment reviews was improper and constituted a constructive change of the MRE-5 Contract. The impact of these delays are set forth below in the Damages and Quantum sections, below.

c. Liebman Improperly Suspended Progress Payments.

The progress payment clause provides that progress payments may be suspended when a contractor "has so failed to make progress, or is in such unsatisfactory financial condition, as to endanger performance of this contract." DAR 7-104.35(b), Progress Payment Clause for Small Business Concerns, DAC #76-38 (September 1, 1982). When an ACO contemplates suspending progress payments, his actions must be "fair and reasonable under the circumstances of [the] particular cases, and supported by substantial evidence." ASPR E-524, DAC #76-18 (March 12, 1979).

Liebman's proposed suspension of progress payments on January 4, 1985 (Finding 114), and his formal suspension of progress payments on February 6, 1985 (Finding 157), violated these requirements. Liebman claimed that Freedom Industries was in such unsatisfactory condition as to endanger performance of the MRE-5 Contract. Liebman based this conclusion on his purported belief that the Contract award was based on a $7.2 million commitment of outside

financing from Dollar, and that Dollar had withdrawn, or made conditional, that financing without the knowledge of the Government. The record reveals that these conclusions are unsupported by any (much less, "substantial") evidence, and the manner in which Liebman purportedly investigated this matter was unfair and unreasonable. Findings 157-175.

i. Liebman Ignored Preaward Determinations Regarding Freedom's Financial Responsibility and Interfered with Freedom's Sources of Working Capital Financing.

To award a contract to a contractor, the Government must first make a determination that the contractor is financially responsible. DAR 1-903, Minimum Standards for Responsible Prospective Contractors. To meet this requirement, a contractor must "(i) have adequate financial resources, **or the ability to obtain such resources as required during performance of the contract**." DAR 1-903.1, General Standards (emphasis added).

When the MRE-5 Contract was awarded to Freedom, the Government was aware that the Commitment Letter issued by Dollar on August 9, 1984, as revised on August 10, was no longer binding. They were aware that the Commitment Letter was conditioned on the award of a $21 million contract, and they were aware that the Contract, as awarded, was for approximately $17 million. Findings 41, 45, 65. The PCO discussed with Liebman at the time that the Commitment Letter was issued, three months before Contract award, that such circumstances would result in the absence of a binding commitment letter at the time of award. Finding 46.

Nevertheless, in awarding the MRE-5 Contract to Freedom, the PCO necessarily made a determination that Freedom Industries was a responsible contractor. The only conclusion that can be drawn from the record is that the PCO determined that Freedom Industries was responsible

because it had demonstrated that it had "the ability to obtain such resources as required during performance of the contract." The PCO reached this conclusion with the knowledge that Freedom Industries had a negative net worth of several million dollars and no source of income beside the MRE-5 Contract. In evaluating whether Freedom Industries was "in such unsatisfactory condition as to endanger performance of this contract," Liebman was obligated to be aware of these facts. Finding 119.

Liebman failed to do so. Liebman proposed suspending progress payments because Freedom Industries did not yet have a line of credit in place at the time of the proposed suspension, without regard for whether Freedom Industries had the "ability to obtain such resources . . . during performance of the contract." Finding 116. Liebman rejected Dollar's availability on the basis that its financing now had a condition (*i.e.*, establishing an arrangement to pay creditors), without regard for Freedom's ability to satisfy that condition and still obtain financing from Dollar. *Id.* Liebman incorrectly asserted that Dollar's Commitment Letter was binding unconditionally at the time of award, and that Freedom's absence of a current, binding commitment rendered Freedom Industries non-responsible. Finding 118.

Liebman's conclusion was erroneous, and it ignored the advice of legal counsel at the time, who reminded Liebman that there had been no change in Freedom's financial condition between the time of Contract award and the time of Liebman's proposed suspension. Finding 124. Liebman's conclusion to the contrary was factually unsupportable.

Liebman's conduct during his investigation of the proposed suspension blatantly breached his duty of cooperation. Liebman required Freedom Industries to produce financial information blindly, without the knowledge that Liebman was considering suspension and without information

about what arrangements would satisfy Liebman. Liebman did not tell Freedom Industries informally that he was considering suspension of progress payments. Liebman did not tell Freedom Industries that he required financing to be **in place** in order to meet Liebman's criteria for responsibility, and Liebman did not provide a deadline for putting such financing in place. Liebman did not even identify for Freedom Industries precisely how much financing he was demanding in order to avoid progress payment suspension. Findings 114, 122 and 123.

Liebman not only failed to acknowledge Freedom's many sources of financing, he wrongfully rejected and interfered with them. Liebman never investigated whether Freedom Industries could have satisfied Dollar and still have obtained financing from Dollar, although Freedom Industries was certain that it could have done so. Finding 121. Freedom Industries had arranged adequate financing with Broadway Bank. Yet, Liebman refused to confirm to Broadway Bank that the Contract called for progress payments to be made on Freedom's costs on a monthly basis, beginning at once. Liebman's failure to confirm these basic contract terms prevented Broadway Bank from financing Freedom. Findings 136-138.

Liebman rejected Freedom's private lenders because they were not financial institutions -- a position that Liebman conceded at trial is incorrect. Liebman rejected the investors' offers to provide their financial backing through a financial institution. Findings 139-147. Liebman breached his duty of cooperation and acted arbitrarily and capriciously in concluding that Freedom Industries was in such unsatisfactory condition as to endanger performance of the MRE-5 Contract.

ii. Liebman Ignored the Parties' Advance Agreement to Treat All Costs as Direct.

A practical vehicle that is often used by the contracting parties to eliminate disputes concerning the treatment of specific costs is to enter into an agreement in advance of contract award on the treatment, *i.e.*, allowability or allocability, to be accorded a cost or particular cost items. *See General Dynamics Corp., Electric Boat Division,* ASBCA No. 21737, 83-2 BCA ¶ 16,907 (1983). Regardless of how carefully the cost principles are defined - - and many are not - - they can hardly be expected to apply clearly to the many accounting systems in the varying contract situations that develop. Hence, it is desirable that contractors seek agreement in advance of award with the Government as to the treatment of special or unusual costs. *See General Dynamics Corp. v. United States,* 202 Ct. Cl. 347 (1993); *Rockwell International Corp.*, ASBCA No. 20304, 76-2 BCA ¶ 12,131 (1976). Such an agreement, if negotiated before the incurrence of the cost in question, will be incorporated in the present and future contracts to which it is applicable.

DAR 15-107, Advance Agreements on Particular Cost Items, encouraged such advance agreements:

> In order to avoid possible subsequent disallowance or dispute based on unreasonableness or nonallocability, it is desirable that contractors seek advance agreement with the Government as to the treatment to be accorded those special or unusual costs.

(Emphasis added.) The binding effect of advance agreements entered into at or before the time of contract award is well settled. *See Riverside General Construction Co., Inc.,* IBCA No. 1603-7-82, 86-2 BCA ¶ 18,759 (1986); *RHC Construction,* IBCA No. 2083, 88-3, BCA ¶ 20,991 (1988); *Custom Janitorial Service,* GSBCA No. 5647, 81-1, BCA ¶ 14,845 (1980).

The Government entered into an Advance Agreement with Appellant regarding the treatment of Appellant's costs under the MRE-5 Contract. The parties agreed that all of Appellant's costs (except for the estimated $1.5 million in production equipment) would be considered direct costs to the MRE-5 Contract. At trial, the Government stipulated to this fact. This agreement confirmed and reflected the information set forth in the spreadsheets submitted with Freedom's proposal which showed that Freedom Industries would receive progress payments even on its pre-production costs. Findings 54-64.

As a practical matter, the Advance Agreement simply confirmed the treatment of Freedom's costs as already provided under the DAR. Under the progress payment clause, Freedom Industries was entitled to receive progress payments at the rate of 95% of its "total costs incurred under th[e] contract." DAR 7-104.35(b)(a)(1). "Incurred costs" include the "costs of direct labor, direct material and direct services identified with and necessary for the performance of the contract and also all properly allocable and allowable overhead (indirect) costs recorded on the books of the contractor." DAR E-509.5(a)(emphasis added.). Where a contractor only has a single contract, all costs the contractor incurs -- including those costs ordinarily thought of as "indirect" costs -- are allocable to that contract. *See* DAR 15-109(d)("allocability" means assigning costs to "one or more cost objectives"); DAR 109(e)("cost objective" includes a contract).

In this case, Freedom Industries only had a single contract. Therefore, all costs Freedom Industries incurred on the MRE-5 Contract were "direct," pursuant to applicable DAR cost

principles.[37] Freedom's Advance Agreement with the Government simply confirmed that principle – all of Freedom's costs would be treated as direct for purposes of progress payments.

Liebman nevertheless violated that Advance Agreement. In the Proposed Suspension Letter and again in the Suspension Letter, Liebman made it strikingly clear that he would refuse to pay progress payments until Freedom Industries began to incur production-related costs. Liebman stated that:

> there does not appear to be any evidence of progress being made in the performance of the contract (e.g., issuance of purchase orders, receipt of materials, ordering and/or leasing of equipment, receipt of equipment, work in process) which would serve to provide 'security' to the Government for any monies that would be paid, in accordance with the provisions of the progress payment clause.

Finding 158.

It is unclear whether this objection was based on a belief that no progress payments could be made until "direct" costs first were incurred, or a belief that no "progress" could be made on the Contract until the incurrence of production-related costs. It matters little since both propositions are incorrect. The Government now agrees that Freedom's pre-production costs were direct and eligible for progress payments, and Liebman conceded at trial that Freedom Industries began making "progress" for progress payment purposes immediately after the Contract was awarded. Findings 95-110. By considering Freedom's purported lack of "progress" in connection with his suspension of progress payments, Liebman violated Freedom's advance agreement with the Government and the DAR cost principles on which that agreement

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[37]Mr. Fishbane, Freedom's expert witness on all financial aspects of the MRE-5 contract testified that since all costs were intended to be incurred against a single MRE-5 Contract, the contract itself was the particular cost objective. Tr. 954, 956.

was based. Findings 165.

iii. Liebman Wrongfully Required Freedom Industries To Obtain Additional Outside Financing As A Condition Of Lifting The Suspension.

Progress payments are a means of financing a Government contract:

> When the PCO decides to include progress payments in his procurement he is telling prospective bidders/offerors that the Government will finance their production efforts.

DLAM 32.592-2a, Preaward Actions. Progress payments are beneficial to both the Government and to the contractor. By lowering the contractor's costs for outside financing, the Government is able to obtain a better price from the contractor, and the contractor obtains liquidity during the critical initial stages of a contract:

> Progress payments is a method of interim contract financing on fixed price contracts . . . in which the Government shares with the contractor the financial burden of performing on long lead-time items. Progress payments are used in order to save the Government the additional expense which would be incurred if the Government had to reimburse contractors for the cost of commercial financing through higher bid prices. Progress payments are especially beneficial to small business which, in many instances, would otherwise be unable to compete for Government contracts because they could not sustain the high rate of interest for the period between contract award and the first delivery for which they could be paid under standard payment provisions.

DLAM 32.590-2, Nature of Progress Payments.

Ordinarily, progress payments are the second most favorable form of contract financing, surpassed only by private financing. DLAM 32.590-4a, Administrative Concept Embodied in the Progress Payment Clause. In "long lead time" cases (such as the MRE-5 Contract), however, progress payments surpass even private financing as the most favored form of contract financing.

DAR, Appendix E-503 ("The general preference for private financing is not applicable to this class of cases").

The parties had these principles very much in mind when they negotiated the MRE-5 Contract. On August 2, 1984, Freedom Industries submitted a proposal of $34.81 per case. Finding 38. At that time, the L-4 "ceiling" was effectively set at $9,000,000. Finding 39. The Government insisted that Freedom Industries lower its price. Freedom Industries responded that it only would be able to do so by lowering the cost of its financing by having the Government increase progress payments. Finding 49.

As a result of negotiations, the Government increased progress payments under L-4 to $13,000,000 (still subject to increase upon demonstration of need). As a result of that increase, Freedom Industries was able to lower its projected need for outside working capital financing to $1,798,936, at a projected cost in interest of only $171,664. Freedom's ability to perform the MRE-5 Contract at the negotiated price was directly dependent upon Freedom's receipt of progress payments as negotiated in order to limit Freedom's need for outside financing to the amount projected. Finding 59.

The Government agreed to these terms. They were set forth in spread sheets reflecting Freedom's negotiations with the Government, were agreed to by both parties, and were incorporated into the MRE-5 Contract pursuant to Box 18 of the Contract Award Document. Findings 55-64.

On February 15, 1985, the Government (not for the first time) violated that contractual agreement by requiring Freedom Industries to obtain $3.8 million in working capital financing. As Liebman stated in a letter of that date to Freedom Industries:

> The purpose of this letter is to confirm the conditions the Government requires to be met before progress payments can be considered for release. . . . $3.8 million in credit would have to be committed to Freedom Industries, Inc. from reliable, reputable and verifiable sources of credit. **I noted that the commitment letters would have to include timetables depicting the actual and anticipated transfer of funds to Freedom Industries.**

R4, tab F49 (emphasis added). *Cf.* Finding 174. Liebman was shifting the source of Freedom's working capital from the Government, in the form of progress payments, to Freedom, in the form of outside financing.

At the time, Freedom Industries already was financing more than $650,000 in costs, for which it was entitled to (but had not received) $631,548 in progress payments. By requiring a commitment of $3.8 million and a timetable for transferring these funds to Freedom Industries, Liebman compelled Freedom Industries to obtain more than twice the amount of outside financing than that to which the parties had agreed in negotiations. *Id.*; *cf.* Finding 176. He knowingly compelled Freedom Industries to draw on this financing by continuing to refuse to pay progress payments for another four months. Findings 177-188. The imposition of additional outside financing requirements as a condition to lifting the suspension of progress payments was a constructive change of the Contract for which Freedom Industries is entitled to relief.

d. Liebman Improperly Insisted That The MRE-5 Contract Be Novated To HT Foods.

A "novation agreement" is a legal process by which the Government recognizes a third party as a successor-in-interest to a contractor on an existing Government contract. ASPR 26-400, Novation and Change of Name Agreements. A novation agreement ordinarily is used only where a party to a Government contract is replaced by a successor-in-interest, usually by sale, by

merger, or by other business transaction, motivated by the business needs of the contractor. ASPR 26-402(a), Agreement To Recognize a Successor In Interest; Tr. 975-76. In this case, Freedom Industries had no business needs that compelled it to novate the MRE-5 Contract to HT Foods. It did so only because Liebman refused to lift the suspension of Freedom's progress payments unless it did so. Finding 173.

At the February 14, 1985 meeting at DLA, Freedom Industries had available to it from Bankers the $3.8 million in working capital financing that Liebman demanded. R4, tab FT094. Nevertheless, Liebman rejected Bankers' proposed commitment letter, purportedly because of its form. Findings 169, 176. The real reason, however, is that Liebman was searching for another excuse not to pay Freedom Industries progress payments. Rather than accept Appellant's latest (of many) proposed source of financing and release progress payments on that basis, Liebman insisted that Freedom Industries' existing creditors posed a threat to Freedom's performance of the Contract.

Liebman's "concern" about past creditors was contrived. DPSC had awarded the MRE-5 Contract to Freedom Industries with full knowledge of these creditors. Freedom Industries had entered into a Conditional Assignment agreement with its affiliate, HT Foods, to protect Freedom Industries from an attack on MRE-5-related assets for past debts. Freedom Industries' largest creditor, Dollar (which also was an investor and stockholder, *see* Finding 20), had no intention of taking any imminent action against Freedom Industries to collect on past debts. At the DLA meeting, Liebman simply created the impression of a threat from Freedom's past creditors where none actually existed. Then, Liebman refused to lift the suspension of progress payments until this imagined threat was eliminated.

Freedom Industries did not want or need to novate its MRE-5 Contract. Nevertheless, after listening to Liebman describe his concerns about Freedom's past creditors, Freedom Industries inferred that Liebman was seeking to novate the Contract. Freedom Industries suggested doing so, and Liebman agreed. Moreover, Liebman insisted that a novation of the Contract from Freedom Industries to HT Foods was a condition of lifting the suspension.

Liebman admitted at trial that once Freedom Industries had obtained the $3.8 million in outside financing that Liebman had required, there was no legitimate need for the novation. Finding 175. Liebman also admitted, however, that he never told this to Freedom Industries. *Id.* Once the concept of novation was proposed, Liebman never advised Freedom Industries that a novation was superfluous because Freedom Industries had secured the additional financing that Liebman had imposed on it. *Id.*; *cf.* Finding 173; Tr. 24.

Faced with Liebman's continued refusal to pay progress payments without a novation, Freedom Industries proceeded to novate the Contract to HT Foods. The process was expensive and time-consuming. Freedom Industries and HT Foods both retained attorneys to draft the necessary paperwork and meet the Government's novation requirements. Freedom Industries submitted a novation package in March 1985. R4, tab F64. The Government submitted the process for legal review. On March 12, 1985, Wayne Gold, Assistant Counsel, DCASR, noted that "this novation does not arise out of the normal situation." R4, tab FT429. The process hit further snags. On March 18, 1985, Gold identified problems with the novation process. R4, tab FT430. Paperwork was rejected, additional paperwork was required.

Ultimately, the novation was not approved until April 17, 1985. Finding 182. Freedom Industries had obtained from Bankers in February 1985 the financing that Liebman (improperly)

demanded, first for Freedom Industries (R4, tab FT094), and then for HT Foods. R4, tab 36. The novation process required by Liebman resulted in an additional two month delay in progress payments to the contractor. This delay constitutes a constructive change to the Contract for which Freedom is entitled to compensation.

e. DPSC Wrongfully Issued a Cure Notice to Freedom for Failing to Accept GFM; The Delays Were Caused by Liebman, and DPSC Should Have Extended The GFM Delivery Schedule Without Demanding Consideration.

This Board has recognized the devastating effect that a delay in progress payments has on a contractor's progress, particularly at the beginning of a contract. *R.H.J. Corp.*, ASBCA No. 12404, 69-1 BCA ¶ 7587 (1969). At the time of Contract award, the Government knew that Freedom Industries had no sources of income other than the MRE-5 Contract. The Government knew that it had contractually obligated itself to pay Freedom Industries progress payments for Freedom Industries' pre-production efforts, including costs for rent and salaries. Finding 75. The Government also knew that one of Freedom Industries' primary tasks during this pre-production period that progress payments were intended to support was the preparation of Freedom Industries' facility for production. Finding 61.

Liebman also knew Freedom Industries' projected schedule. Freedom Industries provided Liebman with a set of the final, negotiated spreadsheets on December 13, 1984 and stated that Freedom Industries intended to gauge its performance by those cash flows. R4, tab FT072. Liebman admitted at trial that he used those cash flows to track Freedom Industries' progress. Liebman knew that Freedom Industries intended to begin receiving GFM by April 1985 and that Freedom Industries' facility had to be completed by that time. Finding 63.

Yet, Liebman refused to pay Freedom Industries a penny in progress payments during that period. By April 1985, Freedom had incurred costs of over $1.7 million. Most significantly, Liebman's failure to pay prevented Freedom from arranging for the completion of the renovation of its facility by April 1985, as projected. Finding 180. *See* R4, tab F70.

Aware of this Government-caused delay, Freedom twice asked DPSC for an extension of the schedule for delivery of GFM to the facility, on March 28, 1985 and on April 2, 1985. R4, tab 46. DPSC refused, stating that Freedom "must obtain [its] HSC approval and accept GFM or be subject to default termination." *Id.* As Freedom had warned, Freedom's facility was not prepared to receive GFM when it began arriving at the facility in April 1985. Instead of extending Freedom's GFM delivery schedule, DPSC issued Freedom a Cure Notice on April 9, 1985 for failing to complete building repairs adequately to accept GFM. R4, tab 44. Finding 181.

The Cure Notice was improper because it failed to acknowledge that the delay in contract performance was caused by Liebman's refusal to pay progress payments. Nevertheless, Liebman seized on the Cure Notice as a reason to extend further his moratorium on progress payments.

For two months, Liebman had been promising that he would lift Freedom's progress payment suspension upon novation of the Contract to HT Foods (which had changed its name to Freedom NY, Inc.; hereinafter, "Freedom"). The novation finally was completed on April 17, 1985. On that same date, Freedom submitted its first progress payment request for the $1.76 million dollars that Freedom had incurred to date. Nevertheless, the following day, on April 18,

1985, Liebman stated in an internal memorandum that "payment of Progress Payment request No. 1 to be held in abeyance until Freedom responds to the Cure Notice and DPSC's intended course of action is known." R4, tab FT116; Finding 183.

Freedom responded to the Cure Notice on April 19, 1985. Finding 185; R4, tab F70. Even then, DPSC continued to refuse to grant Freedom an extension of its GFM delivery schedule until Freedom offered to pay $100,000 in consideration. R4, tab 46 (April 15, 1985 refusal); R4, tab 71. Finally, on April 24, 1985, DPSC agreed to extend the delivery schedule for $100,000, plus the cost of storage of the GFM. R4, tab 73; *cf.* Finding 186. Liebman's actions had begun to feed on themselves – his delay in making progress payments caused delays in production, which Liebman then used as an excuse for further delays in making progress payments.

"It is black letter law that every contract with the Government contains an implied obligation that neither party will do anything to prevent, hinder or delay performance." *Sterling Millwrights, Inc. v. United States*, 26 Cl. Ct. 49, 67 (1992). *See SIPCO Services & Marine Inc. v. United States,* 41 Fed.Cl. 196 (1998). The Government's duty of cooperation adheres in the idea that it will (1) provide reasonable cooperation with the contractor's efforts to perform, and (2) not hinder contractor performance, but rather "do whatever is necessary to enable the contractor to perform." *Lewis-Nicholson, Inc. v. United States*, 550 F.2d 26, 32, 213 Ct. Cl. 192, 204 (1997) (citing *Kehm Corp. v. United States*, 93 F.Supp. 620, 623, 119 Ct. Cl. 454, 469 (1950)). Where Government actions delay a contractor's performance and increased costs result, the contractor has a claim for damages. *Lathan Co., Inc. v. United States*, 20 Ct. Cl. 122, 129 (1990)(citing *Lewis-Nicholson,* 550 F.2d at 26).

The Government is responsible for the delay in repairing Freedom's facility which prevented it from being ready to accept GFM. Consequently, the Government also is responsible for the additional one-month delay in progress payments, which were being "held in abeyance" during the pendency of the Cure Notice, and the $100,000 in consideration that Freedom paid to obtain extensions to its delivery schedules.

f. Liebman Improperly Interfered With Freedom's Equipment Financing.

Freedom's ability to perform the Contract within its projected budget depended on the use of state-of-the art production equipment from Doboy, Koch, and International Paper. Findings 209, 210. The band sealers from Doboy sealed the MRE meal pouches. Finding 213. The Koch vacuum sealers formed pouches for the accessory bags and crackers and then sealed them. Findings 211-12. The International Paper case formers and sleevers formed the thick fiberboard MRE cases, sealed them after they were filled, and placed a protective fiberboard sleeve around them. This equipment was faster, less labor intensive, and more mechanically reliable than the available alternatives. Finding 214. Freedom's cost projections were based on its use of this equipment. Finding 209.

Freedom took the steps necessary to obtain this equipment in a timely fashion. Freedom ordered this equipment in January 1985, and it was scheduled to be delivered and ready for production in accordance with Freedom's projected cash flow statements. Finding 216. In February 1985, Freedom arranged for the equipment acquisition to be financed by Bankers,

through its agent, Performance. Performance assumed the purchase orders that had been submitted by Freedom and undertook to make payment arrangements for the equipment. Finding 217.

Liebman directly interfered with Freedom's acquisition of this production equipment. Although Performance agreed in February 1985 to finance Freedom's lease of the production equipment, Liebman continued to withhold progress payments through May 6, 1985. This delay in making progress payments created significant insecurity in the lender. Findings 188, 223.

Liebman also interfered more directly. Liebman contacted Bankers personally and informed Bankers that he would not be making a progress payment in June 1985, despite previous promises to do so. As a result, Performance and Bankers were prepared to withdraw their offer to provide equipment financing. Finding 219-220. Freedom convinced Performance to meet with Liebman to establish a list of routine costs that would be paid monthly as a means of restoring the lender's confidence in the Contract. Liebman met with Freedom and Performance on June 19, 1985 to discuss these issues. R4, tab F81. Liebman promised to provide the list of routine costs, but he never did so. Finding 221-228.

As a result, Performance and Bankers withdrew their support of Freedom's equipment acquisition efforts. They refused to make payments on the equipment that had been ordered, and they canceled the pending purchase orders for the equipment. The equipment manufacturers had a backlog of orders, and the direct consequence of these cancelations was that Freedom lost its opportunity to obtain this equipment in time to use it for MRE-5 production. Finding 229-31.

The impact on Freedom's production efforts was devastating. Freedom was forced to scramble for whatever production equipment it could obtain. Freedom replaced the Koch

equipment with less reliable band sealers. Freedom had to mix and match different pieces of equipment for its cracker subassembly operations. Instead of the Koch vacuum sealers for accessory pouches, Freedom was forced to use "lazy susan" circular tables that spun around so that workers could drop in their accessory pouch item before sealing. The case sealer and sleever that Freedom obtained from Marq was designed to form corrugated cardboard boxes, not the heavy duty fiberboard cases used for MREs. This equipment required substantially more labor than planned, the employees required additional training, the equipment was slower, and it broke down more frequently. Findings 230, 232. The increase in costs of production and in delay time was enormous. This impact is set forth in the Quantum section of Appellant's Brief.

g. Liebman Improperly Refused to Pay the Costs of "Capital Type" Expenditures as Progress Payments, Further Violating the Parties' Advance Agreement – DAR Deviation Request.

On April 17, 1985, when Freedom submitted its first progress payment request after the novation (which was the fifth submission of a progress payment for the contractor), Liebman still had an excuse to avoid making progress payments – DPSC's Cure Notice. R4, tab 44. When DPSC finally agreed to resolve the Cure Notice on April 24, 1985 (R4, tab 46), Liebman had run out of excuses to withhold progress payments in their entirety. Left with no alternative, Liebman now created a new excuse to make deductions from Freedom's progress payments.

The Advance Agreement that the Government reached with Freedom Industries included an agreement to pay $522,218 in costs for the following cost items:

Quality Control and Supplies	$ 54,000.00
Maintenance Equipment	$ 25,380.00
Building Repairs	$160,000.00
Building Management and Computer Systems	$177,838.00

Lockers	$ 25,000.00
Office Automation Equipment	$ 80.000.00
TOTAL	$522,218.00

Finding 190.

In other contracts, these cost items often are treated as "capital" items, *i.e.*, their cost often is required to be deducted over the useful life of the item (depreciated). In this case, however, the parties' Advance Agreement and the DAR Cost Principles caused these cost items to be classified as direct costs. They were not to be depreciated; their costs were to be expensed to the MRE-5 Contract. Finding 191.

Nevertheless, on May 6, 1985, beginning with Liebman's first payment of any monies to Freedom, Liebman began to deduct these costs from Freedom's progress payments. Between May 1985 and May 1986, Leibman wrongfully withheld a total of $399,111 in allowable costs from progress payments to Freedom. Finding 192, 193.[38] These deductions interfered with Freedom's ability to obtain the identified items, including Freedom's Building Management and Computer System. That system included networked computer hardware and software that would contain Freedom's automated lot tracking system and accounting systems. Liebman recognized that this item was crucial to Freedom's ability to perform. Finding 195.

Liebman claimed that he was prohibited from paying these costs by the progress payment clause, which excludes from progress payments "costs ordinarily capitalized and subject to depreciation or amortization except for the properly depreciated or amortized portion of such

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[38]Of the total amount of $522,218, payments of $123,107 had been made by the Government. However, Liebman stated that the payments had been made in error, not because Leibman considered the paid amount of $123,107.00 to be allowable or that it represented what would have been considered an allowable depreciation portion.

costs." DAR 7-104.35(b), (a)(2)(iii). Liebman admitted that the costs had been negotiated as direct costs to the contract, and he agreed that the entire amount of these costs must be paid during the performance of the MRE-5 Contract. Liebman claimed, however, that he was permitted to pay only the depreciated portion of those costs as progress payments and that the balance of these costs would be paid as part of deliveries. Finding 203.

Liebman was wrong. Once Freedom Industries had reached an Advance Agreement on the treatment of these costs as "direct" costs, they no longer were "costs ordinarily capitalized and subject to depreciation or amortization." They were direct costs, and Liebman had an obligation to pay progress payments for them. His failure to do so was a breach of the parties' Advance Agreement and a violation of Part 15 of the DAR Cost Principles.

Liebman was advised repeatedly to make the requested payments. In June 1985, the acting PCO advised Liebman that he should pay these costs as progress payments. Finding 196-197. In July 1985, Assistant Counsel to DCASR-NY, Michael Montefinise, advised Liebman that "to the extent that said equipment . . . falls under some other category which permits treatment as direct costs," progress payments may be paid on their full value. Findings 198-201.

Liebman ignored this advice. He did not pay progress payments on the full cost of these items. Indeed, Liebman violated his own purported interpretation of the Progress Payment Clause because he failed to pay **any** portion of these costs as progress payments, including the depreciable portion. Finding 207. Instead, on July 18, 1985, Liebman submitted a DAR Deviation Request, ostensibly seeking permission to pay progress payments on these costs. Finding 204. The request was never approved by DoD. Nevertheless, in May 1986, when the PCO issued a modification of the contract permitting these costs to be paid as an invoice,

Liebman paid these costs all at once. Findings 205-207.

The Government recognized the injustice being done to Freedom. In a meeting of Government representatives from DPSC, DCASMA, DCAA, and DCASR (including the PCO and the ACO), the Government recognized the dilemma in which it was placing Freedom by taking Liebman's position:

> Primary problem with this contract with progress payments is that capital equipment must be capitalized – only depreciated portion can be paid in progress payments. In negotiations with DPSC, Freedom was allowed to claim direct costs for all but production equipment. However, DCASMA will not pay progress payments for any capital equipment as a direct cost.

R4, tab FT163, Bates 01336, ¶4b.

Liebman's pursuit of a DAR Deviation Request in lieu of paying progress payments on the full amount of these costs was a violation of the parties' Advance Agreement, was arbitrary and capricious, and amounted to a constructive change of the Contract. Moreover, Liebman's wrongdoing caused disastrous results.

Liebman's refusal to confirm that progress payments would be paid for this equipment caused Freedom's vendor, AT&T, to repossess the computer equipment shortly after installation. Findings 178-179. Liebman's delay of approximately one year in paying these costs assured that Freedom was unable to obtain the system it had planned. Rather than an automated lot tracking system, Freedom was forced to track inventory and product by hand, exponentially increasing its labor costs and likelihood of error.

Freedom is entitled to damages for Liebman's wrongful failure to pay these costs. *See Aerojet-General Corporation*, ASBCA No. 13548, 70-1 BCA ¶ 8245 (1970)(contractor entitled to recover increased costs attributable to contracting officer's refusal to make progress payments based upon an erroneous conclusion regarding entitlement).

h. Liebman Improperly Suspended Progress Payments for a Second Time.

On July 5, 1985, Freedom submitted Progress Payment No. 4, requesting payment of $807,348. On July 25, 1985, Liebman called Freedom and requested that Freedom renumber the July 5 progress payment request as No. 5. R4, tab 62. Liebman held any payment on this request (R4, tab 422(PPChart)) and requested a DCAA audit. On August 13, 1985, DCAA issued an audit report of Progress Payment No. 5. R4, tab 60. DCAA, with its proven bias against the contractor, lambasted Freedom for various, unjustifiable reasons. DCAA also claimed in its report, for the first time, that Freedom's accounting system was inadequate to support progress payments. *Id.* Findings 233-242.

Liebman seized on this opportunity to freeze progress payments again. At a meeting held on August 19, 1985, as confirmed by a letter dated August 23, 1985, Liebman proposed suspending progress payments for a second time. Finding 243. Liebman's action was based entirely on DCAA's conclusion that Freedom's accounting system was inadequate. R4, tab 163, Bates 01335, ¶2; tab 62, p.1, ¶2. *Cf.* Finding 244.

One week later, the PCO assured that this proposed suspension would freeze progress payments to Freedom. On August 30, 1985, Bankoff issued a Cure Notice declaring Freedom to be unable or unwilling to comply with the requirements of the Contract. The reason for the Cure

Notice was that Liebman had proposed suspending progress payments, which the PCO recognized "are considered vital to your company's financial capacity to perform on this contract." R4, tab 63, ¶2. Once again, the Government refused to provide Freedom with progress payments and then penalized Freedom for not having them. Finding 248.

Liebman's conclusion regarding the inadequacy of Freedom's accounting system was maliciously unsupportable. As explained by Freedom's financial and accounting expert, Mr. Fishbane, Freedom's accounting system was perfectly acceptable. Tr. 983-85. In addition to noting that DCAA had repeatedly found Freedom's accounting system adequate until that point, Mr. Fishbane testified that he tested Freedom's system himself. *Id.* In order to satisfy himself, Mr. Fishbane went back into Freedom's records and was able to identify the data that supported each and every progress payment "to the penny." *Id.* He noted that there were proper controls in place and everything that he would consider necessary for an adequate accounting system. *Id.*

Liebman actually was using the proposed suspension as a ploy. Liebman was receiving tremendous pressure as a result of his improper refusal to pay Freedom for its "capital" costs. As the PCO recognized:

> Freedom has continuously claimed that his delay in making progress under the contract was due to the DCAA and ACO mishandling and nonpayment of progress payment requests. Much of this stems from the differing interpretations of what the contract allows as far as capital vs. expensed costs. Freedom claims that all costs, other than production equipment, were allowed to be expensed as direct for this contract, as negotiated with the DPSC on 06 November 1984, rather than amortized over the normal depreciable life as DCAA claims should be done. As Freedom's accounting system had shown all costs as direct, DCAA stated their accounting system was unreliable for the purpose of handling progress payments. This had caused the ACO to delay payments pending a positive pre-payment audit report. Freedom has claimed this delay caused

> damages to itself and constitutes a breach of contract.
>
> Some normally capitalized cost elements, other than production equipment, in the amount of $500K plus were allowed to be expensed as indirect [sic] costs in contract cost negotiations.

R4, tab 75, p.2, ¶5a.

To alleviate the pressure on him, Liebman used the suspension as leverage to require Freedom to reclassify the disputed costs on its books – from ordinary expenses to capital expenses. On September 26, 1985, Freedom reported that it had done so. *Id.*, p.4, ¶6. By causing Freedom to reclassify these costs, Liebman thereafter was able to justify not paying progress payments on these costs. From the moment that Freedom agreed to reclassify these costs as "capital," rather than "direct" costs as negotiated, the Government dropped all objections to the classification of these costs.

Liebman's second proposed suspension was improper and further delayed payments to Freedom. Freedom originally submitted Progress Payment Request No. 5, requesting $807,348, on July 5, 1985. That request was followed by Progress Payment Request No. 6 on August 8, 1985, seeking payment of an additional $640,761. Liebman made no payment on this combined request for $1,854,955 before the proposed suspension on August 23, 1985. On September 11, 1985, after the proposed suspension and subsequent Cure Notice, Freedom submitted Progress Payment Request No. 7 for $1,546,045, bringing Freedom's total outstanding unpaid costs to $3,401,000. The suspension provided Liebman with the opportunity to continue to hold payment on these costs. These actions constituted a constructive change of the Contract.

Moreover, Liebman constructively changed the Contract by compelling Freedom to reclassify the costs that had been negotiated as direct and record them on its books as "capital" costs. Liebman strongarmed Freedom into relinquishing its right to progress payments on these costs, in violation of the parties' Advance Agreement. Finding 260.

It is established law that the Government cannot require a change in a contractor's allocation of costs if the contractor priced the contract in reliance on its reasonable understanding that its method of allocation would be satisfactory to the Government. *Litton Systems, Inc.*, ASBCA No. 10395, 66-1 BCA ¶ 5599 (1966).

Appellant clearly priced its MRE-5 Contract based on allocation of the "capital" costs as direct to the Contract. Not only did it have a "reasonable understanding" that this allocation was acceptable to the Government, it had an agreement that it could so allocate. Finding 58. Freedom is entitled to receive additional delay costs on account of Liebman's improper direction.

i. The Government Improperly Imposed Additional Financial Obligations on Freedom as a Condition of Resolving the Cure Notice.

Despite Freedom's knuckling under to Liebman's insistence that Freedom's costs be reclassified, Liebman did not let up. On September 30, 1985, Liebman had DCASR's financial analyst perform a financial analysis of Freedom and concluded that Freedom's financial condition was unsatisfactory. R4, tab 72; tab 75, p.5, ¶7. Stokes used a technique of analysis that made no sense, which he called Backwards Induction. Findings 250-255. Even the PCO was critical of the basis for the analyst's conclusion, which was based on DCAA's highly criticized reports and ignored Bankers' agreement to provide $5 million in financing:

> Financial Services presented a 30 September 1985 IOM signed by Morris Luster declaring Freedom's financial condition as unsatisfactory. **However, this report relied heavily on the DCAA reports in question and on the lack of much needed progress payments, (as a result of the DCAA recommendations).** In addition, Bill Stokes mentioned that Freedom's independent financial resource, Banker's Leasing, had verbally guaranteed a line of credit of $5M ($2M of which had already been drawn and not repaid).

R4, tab 75, p.5, ¶7.

Nevertheless, based on this analysis, the Government imposed two new financial requirements on Freedom: (1) that Freedom would require an additional $500,000 above the $3 million balance currently available from Bankers ***in order to finance the "capital" equipment that Liebman had just forced Freedom to reclassify***; and (2) that Freedom would have to pay all of its creditors who were more than 30 days past due:

> It was determined that Freedom would need additional funds in the following amount:
>
> $1 Million deficit working capital
> $1.5 Million October 1985 working capital
> $1 Million Capital over & above progress payments (needed for Nov.)
> $3.5 Million
>
> This $3.5M figure increases Freedom's original line of credit of $5M to 5.5M. **This extra $500K takes into consideration a DAR deviation for $500K for capital expenses being denied.** This figure ensures Freedom's financial ability to perform. **Of this money becoming available to Freedom, Freedom would also be required to pay all "over 30 day" liabilities. This would constitute the start of progress.**

Id. (emphasis added).

These requirements violated the parties' Advance Agreement regarding the treatment of costs, disregarded the parties' contractual agreement regarding Freedom's need for outside

financing, improperly directed the use of Freedom's funds, and incorrectly failed to acknowledge that Freedom had made "progress" on the MRE-5 Contract immediately after Contract award. The Government's imposition of these financial requirements on Freedom constituted constructive changes of the Contract that caused Freedom to incur additional costs for which it is entitled to be compensated.

j. Liebman Continued to Make Improper Deductions from Progress Payments for Proper Costs Incurred and Improperly Held Payments at the Request of the PCO.

i. Liebman Improperly Deducted $400,000 from Progress Payment No. 5. 8

Liebman disallowed $400,000 of Freedom's Progress Payment Request No. 8 as an offset for occupancy costs previously paid to Freedom. Findings 236. The disallowance was improper. Findings 237. The sale of the lease option was an independent transaction and was properly treated as such on Freedom's books and records. *Id.* Liebman's deduction for costs previously paid to Freedom for rent was unjustified and was a breach of the Government's obligation to pay progress payments.

Furthermore, such an offset violated the Assignment of Claims Act, 31 U.S.C. § 203 and 41 U.S.C. § 15 (the "Act"). The payments made on Progress Payments 1, 2, and 3 were paid directly to Bankers, which was Freedom's assignee subject to the Act. R4, tab F232 (Progress Payments 1, 2, and 3)(checks made payable to Bankers). The Act prohibits recoupment of any payment to an assignee regardless of the claim that the Government may have against the assignor. Liebman's recoupment of the $400,000 was illegal. Finding 238.

ii. Liebman Wrongfully Withheld Progress Payment Nos. 10 And 11 At The Request Of The PCO Until Mod 20 Was Signed.

Freedom submitted Progress Payment Request No. 10 on November 29, 1985, requesting payment of $353,081. R4, tab FT422(PPChart). Liebman approved the request for payment. Findings 282-283. On December 11, 1985, however, Bankoff and Liebman contrived the circumstances for a Cure Notice, again alleging that Freedom had a shortfall in working capital. Findings 280. The Cure Notice once again resulted in the freezing of progress payments. Freedom submitted Progress Payment Request No. 11 on December 11, 1985, requesting $1,159,473. Liebman continued not to pay Freedom while discussions continued regarding the Cure Notice. Findings 282-283.

In January 1986, the Government wanted Freedom to enter into a Contract modification that contained language Freedom had rejected. Findings 275-276. On January 21, 1986, PCO Bankoff instructed Liebman not to release any progress payments until the modification was signed. *Id.* Liebman complied. *Id.* Freedom signed Mod 20 on January 29, 1986. On January 30, 1986, Liebman paid Progress Payments 10 and 11 virtually in full. Findings 282-285. Bankoff's instruction to Liebman and Liebman's compliance with it constituted a breach of the Government's contractual obligation to pay progress payments.

iii. Liebman Wrongfully Withheld Progress Payment No. 21 At The Request Of The PCO Until Mod 29 Was Signed.

Bankoff conspired with Liebman to deny progress payments a second time. In September 1986, Bankoff wanted Freedom to execute another Contract modification, Mod 29. On September 15, 1986, Freedom had submitted Progress Payment Request No. 21, requesting

$2,487,623. Although Liebman had approved approximately $700,000 of this request for payment, Bankoff again instructed Liebman to withhold payment until Freedom executed the Contract modification. Findings 349-50. Desperate for payment, Freedom signed Mod 29 on October 7, 1986. Finding 151. On October 9, 1986, Liebman paid Freedom $721,887. *Id.*

k. DPSC Wrongfully Diverted CFM From Freedom (January1986).

In January 1986, the Government needed Freedom-purchased and Freedom-owned contractor furnished material (CFM) to give to Rafco to produce the 114,758 reprocured MRE cases. Finding 292. The Government took this CFM without asking Freedom. *Id.*

Freedom needed that CFM to meet its then current production requirements. By diverting this CFM, the Government interfered with Freedom's ability to produce its own MRE cases under the contract resulting in schedule delays that could not be recovered. Finding 293. The diversion of CFM interfered with Freedom's performance of work under the contract and constituted a constructive change.

l. Liebman Imposed Liquidation Of Progress Payments At 100%.

On October 29, 1986, Liebman took a drastic and catastrophic action towards Freedom when he decided to liquidate progress payments at the rate of 100%, including the twenty-four (24) invoices that previously had been submitted for payment. Findings 304-07. Liebman imposed this liquidation rate to put the "finishing touches" on Freedom. The liquidation of progress payments at the rate of 100% meant that Freedom would receive no net payment at all on any of the invoices submitted for delivered MREs.

Despite Liebman's attempts to justify this death knell to Freedom, the 100% liquidation was an entirely unwarranted act. At no time did Freedom stop working or continue to make

progress. Despite the considerable cost overrun which Freedom was experiencing because of the Government's continuing acts and omissions, Freedom managed to deliver over 500,000 MRE cases to the Government. Findings 315.

Yet, on October 1986, Liebman "officially decreed" that progress payments were to be liquidated against shipments at the rate of 100%. Findings 304-07. There was bad faith inherent in this action. Liebman claimed that he was protecting the Government's financial interest against a contractor who was not making progress. In fact, the real impediment to Freedom's performance and inability to make further progress was the Government's failure to provide the necessary GFM materials to Freedom.

Liebman's unwarranted 100% liquidation eliminated Freedom's last chance of survival in that it starved Freedom of the resources it critically needed to continue work on the Contract, and it communicated to Freedom's lender that the Government had abandoned the contract. Liebman's improper modification of the contractual liquidation rate from its negotiated rate of 82.6% – first to 95% and then to 100% – caused Freedom to incur additional costs for which Freedom is entitled to be compensated.

2. Freedom Is Entitled To Its Increased Costs Caused By The Government's Changes To Specific Contract Requirements.

a. Liebman Failed to Make Payments for MREs Delivered and Accepted.

The Contract contained the standard Payments clause that appeared on the Standard Form 32, General Provisions (R4, tab 2, p. 96 of 98) which authorized payment for supplies and services delivered and accepted. Between March 13, 1986 and April 3, 1987, Freedom invoiced a total of $1,907,979 on 33 DD Form 250 invoices (DD250s) which were approved by the

Government. Finding 297. These DD250s represented shipments of completed and accepted MRE cases under the Contract.

Under the terms of the contract, Freedom was entitled to payment within 5 to 10 days after submission of a proper invoice and if any such invoice remained unpaid after 30 days, Freedom was also entitled to interest on the amount due in accordance with the Prompt Payment Act. Findings 298. The Government was entitled to liquidate outstanding progress payments against the total amount of the invoice, thereby entitling Freedom to a payment of the total value of the invoice less the amount representing the agreed liquidation rate (82.6%) Freedom did not receive any net payments against invoices which were submitted between March 13, 1986 and April 3, 1987. Liebman had no legitimate reason to withhold payment as there was no dispute regarding the amounts due under any of the invoices or acceptability of the shipments. Finding 299.

As part of the recent settlement of Freedom's Termination for Convenience proposal, the Government has agreed to pay Freedom the amount representing five (5) of the thirty-three (33) DD 250 invoices. Finding 302. Freedom's claim for the balance due for the other 28 invoices remains unpaid and is part of what is claimed herein. Finding 303.[39]

Freedom also has reserved its rights, as part of the Termination for Convenience settlement, to claim all interest and impact damages caused by the late payment of all 33 DD250 invoices and progress payments. *See* Quantum Section, below.

b. DPSC Failed To Provide GFM To Freedom.

[39]Freedom assumes that the TCO will perform his promise to pay Freedom for the five invoices identified herein. Freedom expressly reserves its claim for these invoices before the Board to the extent that the Government fails to perform the settlement agreement.

A contractor's entitlement to an equitable adjustment for increased costs caused by the Government's failure to deliver GFM is well established. *See Pan American World Airways, Inc.*, ASBCA No. 3627, 57-1 BCA ¶ 1240 (1957)(contractor compensated for labor inefficiencies caused by the Government's failure to provide property to be used in the execution of the contract). Likewise, when the Government fails to provide Government furnished materials in a timely manner so that the contractor can economically perform the contract, the Government breaches the contract. The contractor can recover increased costs where the Government fails to promptly make available Government furnished materials. *Litchfield Manufacturing Corp. v. United States*, 167 Ct. Cl. 604, 338 F.2d 94 (1964).

Freedom is entitled to damages for just such constructive changes by the Government. Revised delivery schedules were negotiated by Freedom and the Government in Mods 25 and 28. Finding 308. However, the Government breached its obligation under these modifications when, *inter alia*, it failed to provide the required GFM that Freedom needed in order to meet those revised schedules and to complete the balance of the Contract. The details of the Government acts regarding failure to provide GFM as required by the Contract are set forth in Findings 308-315 and 317-323.

Freedom is entitled to an equitable adjustment as a result of the failure of the Government to provide the necessary GFM. This repeated failure resulted in increased costs as Freedom attempted to work rescheduling and re-sequencing and, ultimately, Freedom suffered complete production shutdowns.

c. The Government Imposed Changed and Additional Testing Requirements on Freedom.

It is well settled that a Government change to an agreed-upon test or inspection method is a constructive change under the contract. *Emerson-Sack-Warner Corporation v. United States,* 189 Ct. Cl. 264, 416 F.2d 1335 (1969); *Chris Berg, Inc. v. United States,* 197 Ct. Cl. 503, 455 F.2d 1037 (1972).

i. The Government Changed The MRE Inspection Requirements At The Outset Of Production Resulting In The Improper Rejection Of MREs (November 1985).

Inspection requirements for MREs in process were set forth in the Contractor Inspection System (CIS) and Inspection Plan, deliverable items under the contract that were developed by Freedom and approved by the Government. Finding 333. The CIS and Plan designated a specific point in the process where Government inspection was to occur. That point was a line on a moving belt that the cases passed after they were assembled. *Id.*

Mr. Leon Cabes who was employed by Freedom during the course of the MRE-5 Contract testified that at the beginning of the Contract, the Government was performing moving lot inspections as agreed upon. Finding 335. Then, at one point and without notice, the AVI stopped performing moving lot testing and waited until the lots became stationary. Finding 336.

The effect of the Government's change in inspection methods caused unwarranted rejections of MRE cases and resulted in a costly three (3) month delay for the period October, November and December 1986. Finding 339.

ii. The Government Imposted Additional Zyglo Testing Requirements on Freedom (March 1986).

The Government imposed additional testing requirements on Freedom in March 1986. Finding 340. The Government demanded that an additional test be performed on of the meal bags. Freedom was required to use a flourescent dye called Zyglo which would be introduced inside the pouch to detect possible micro holes. Finding 342.

The extra testing slowed down the process and went on for about 6 to 8 months. Finding 344. These additional tests were not included in Freedom's Contract. It required additional people to perform the sampling and testing and additional time to produce cases as a result of these additional requirements. *Id.* These additional tests constituted a constructive change to the Contract for which Freedom is entitled to compensation.

B. ACTS AND OMISSIONS BY GOVERNMENT REPRESENTATIVES IN THE ADMINISTRATION OF THE CONTRACT WERE DONE IN BAD FAITH AND CONSTITUTE A BREACH OF CONTRACT BY THE GOVERNMENT.

The United States Government, unlike private parties, is assumed always to act in good faith. *Librach v. United States*, 147 Ct. Cl. 605 (1959). Accordingly, a showing of bad faith requires "well-nigh irrefragable proof." *Knotts v. United States*, 128 Ct. Cl. 489, 492, 121 F. Supp. 630, 631 (1954). Meeting the *Knotts* criteria, while extremely difficult, is not impossible.

The cases in which courts and boards have found "irrefragable proof" of bad faith center on evidence of specific intent to injure the plaintiff or appellant. Thus, in *Gadsden v. United States*, 111 Ct. Cl. 487, 78 F. Supp 126 (1948), the Court of Claims equated bad faith with actions which are "motivated alone by malice." *Id.*, 111 Ct. Cl. at 489-90, 78 F. Supp. at 127. The same court, in a civilian pay suit, found bad faith in a proven "conspiracy . . . to get rid of the

plaintiff." *Knotts, supra*, 128 Ct. Cl. at 500, 121 F. Supp. at 636. Government conduct which is "designedly oppressive" also supported a Court of Claims finding of bad faith. *Struck Construction Co. v. United States*, 96 Ct. Cl. 186, 222 (1942).

More recently, the ASBCA discussed bad faith in *Apex International Management Services Inc., by Trustee in Bankruptcy*, ASBCA Nos. 38087 et al., 94-2 BCA ¶ 26,842 (1994). The Board, citing *Gadsden, Knotts, and Struck*, identified four "standards," any single one of which might be used to determine the presence of bad faith. The standards include proving that the Government: (1) had specific intent to injure appellant; (2) was motivated alone by malice; (3) engaged in a conspiracy to get rid of the appellant; or (4) engaged in designedly oppressive conduct. *Apex, supra*, 94-2 BCA at ¶ 26,842.

This Brief describes in detail the actions of Government contracting officers Liebman and Bankoff, as well as officials of the New York office of DCAA, that constituted bad faith. Liebman in particular constantly engaged in acts and omissions that ignored the Contract requirements and gave rise to equitable adjustment entitlement. The record proves that Liebman was motivated by malice toward Henry Thomas, that Liebman conspired against Freedom, and that Liebman engaged in actions that were designedly oppressive.

1. **Liebman Was Motivated By Malice.** The record shows that Liebman hated Henry Thomas. The sheer intensity of his unrelenting campaign to deny Freedom working capital is proof of this motivation. *See* Section III.A above. Liebman used combinations of feints, excuses, bureaucracy, administrative processes, bullying, obsequiousness, feigned ignorance, and professed superiority to achieve a single objective – to keep as much Government

money away from Freedom as possible. Liebman's demeanor at trial only reinforced the inescapable inference that Liebman harbored deep-seated malice toward Henry Thomas.

The Board, however, need not resort to making inferences about Liebman's motivation. Liebman openly admitted his malice toward Thomas. In February 1987, Freedom was starved of working capital and was struggling to complete the MRE-5 Contract. Freedom was desperate to stay in the MRE IPP program and needed an award of the MRE 7 Contract for that purpose. R4, tab FT342. Liebman was continuing to work as hard as he could to get Freedom out of the program.

On February 22, 1987, DLA's Colonel Francis Holland interviewed Liebman. The subject was Freedom and MRE 5. More specifically, the issue was Henry Thomas. The Colonel asked Liebman, "Would you deal with Henry Thomas as a businessman if you had a choice?" The man who had spent the last two years of his career purposely throttling Freedom's cash flow stated:

> **Knowing what I know now I wouldn't deal with him because he repeatedly doesn't pay his bills in the ordinary course of business.** Thomas is a shrewd businessman, **wheeler-dealer.** He believes he can do anything he wants. He feels he can get away with the violation of normal business practices and government regulations. **He feels that through the use of political clout he can get whatever he wants. He can get leverage through minority status and political clout.** DCAA believes there may be some questionable accounting/business practices that could be criminal.

R4, tab FT338, Bates 02342(emphasis added). *See* Findings 76-84.

These statements reflect Liebman's true feelings about Thomas. Any possible doubt is erased by Liebman's reaction to these statements at trial. If Liebman were motivated by anything less than personal dislike, if Liebman simply were protecting the Government from a questionable

contractor, Liebman would have admitted those feelings at trial. He would have stated, without hesitation, that Thomas was . . . whatever Liebman imagined him to be. Instead, Liebman denied that he disliked Thomas. Liebman tried to convince this Board that he was complimenting Thomas when Liebman called him a "wheeler-dealer." Such absurd denial is the best evidence of Liebman's twisted, deep loathing of Thomas.

2. **Liebman Engaged In A Conspiracy To Get Rid Of Freedom.** As detailed above, Liebman knew his unyielding progress payment request denials, suspensions, and withholdings had put the Government in breach of the MRE-5 Contract. Findings 75-90. To succeed with his goal, in the face of such clearly egregious conduct, he needed a powerful ally.

Freedom's MRE-5 Contract contained clause DAR 7-104.35(b), entitled "Progress Payments for Small Business Concerns." This clause provides for progress payments based on incurred costs. Incurred costs are defined generally in DAR Appendix E, §509.5 and more specifically in DAR Part 15.

DCAA is the audit arm of DoD. Among other things, such as the determination of the adequacy of a contractor's accounting system (DAR E-506), DCAA acts as the contracting officer's adviser on matters of incurred cost allowability. When DCAA talks, DoD usually listens. Liebman enlisted DCAA's support in his campaign against Freedom. Liebman knew that DCAA had been opposed to Freedom's Contract. Findings 81, 96. For this reason, Liebman intentionally submitted every Freedom progress payment request to DCAA audit (Findings 95-99), knowing DCAA would provide justification for Liebman to withhold payment. Findings 80-85.

DCAA validated Liebman's confidence in it. Between November 1984 and December 1985, DCAA returned every single progress payment request unaudited or with a recommendation of no payment. Finding 80. Liebman was able to support his refusal to make payments by citing his reliance on DCAA's reports. Finding 84.

In May 1985, six months into Contract performance, Liebman finally made his first payment. By now he had forced Freedom into substantial debt. Findings 87-188. Liebman and DCAA, however, did not relax their campaign against Freedom.

Progress Payment Request No. 4 was submitted on July 5, 1985. DCAA used its audit of this request to suddenly question Freedom's accounting system, a system that had been approved by DCAA in the pre-award phase and in the monthly audits of Freedom's progress payment requests. Liebman used this excuse to reinstate a formal suspension of payments to Freedom. Findings 233-235, 238-244.

After refusing to honor the Government's financing commitment and interfering with Freedom's private financiers (Findings 128-148), Liebman still did not let up. Liebman sought to finish off Freedom with a new ally – PCO Bankoff.

Liebman's maladministration had poisoned Freedom's relationship with DLA. R4, tab FT338. Freedom's last chance to hang on was an award under the MRE 7 solicitation. Freedom submitted its proposal and, in October 1986, was given a positive pre-award survey. R4, tab F182. Liebman went to work with the PCO, Bankoff, to turn the positive pre-award around. The conspirators secretly increased the progress payment liquidation rate to 100% to deny cash flow (Findings 304-07), held up payment on invoices to extort claim releases (Findings 284, 350-351), and failed to provide GFM required to complete the MRE-5 Contract. Findings 308-15, 317-23.

Liebman and Bankoff were successful. By November 7, 1986, Freedom was forced to shut down production. In December 1986, the positive pre-award on MRE-7 was reversed. R4, tab FT317. On March 4, 1987 Bankoff determined that Freedom was nonresponsible. R4, tab FT342. It was all over.

3. Liebman Tactics Were Designedly Oppressive. From the award of the MRE-5 Contract in November 1984 until the final 100,000 cases were defaulted in June 1987, Liebman persistently, and in violation of the terms of the Contract, acted specifically to destroy Freedom.

In violation of the Contract, he denied essential progress payments for six months. From November 1985 through January 1986, he delayed making any progress payments. Beginning in January 1985, he suspended progress payments. In February 1985, he inappropriately required a novation of the Contract. In April and May 1985, he refused to pay progress payments despite completion of the novation process and wrongfully threatened default. Section III.A.1. a-e above.

Liebman interfered with Freedom's securing of financing from private financiers. He required Freedom to obtain substantially more outside financing than the Contract required. He interfered with Freedom's purchase of production equipment. He prevented Freedom from obtaining its automated lot tracking and networked computer system. He suspended progress payments for a second time between August and October 1985. He made substantial deductions from progress payments, including a $400,000 deduction (associated with the lease option) that was even illegal. He participated in extorting releases from Freedom. He liquidated progress payments at 100% in order to stop all cash flow during the Contract's final stages. And, finally, he failed to make any payment on invoices for MREs delivered and accepted between March 1986 and April 1987. Section III.A.1.f-k above.

Liebman planned to strangle the "wheeler-dealer" Thomas by cutting off his lifeblood, his working capital. He succeeded. These actions truly define what it means to be "designedly oppressive."

4. Liebman's Specific Intent Was To Injure Freedom. Even the most jaded observer would see from the record of this case that ACO Liebman intended to destroy Freedom. Liebman admitted his personal distaste for Thomas. He admitted his belief that Freedom was not entitled to receive the Contract that Liebman was responsible to administer. Liebman's actions were designed to deprive Thomas of the benefits that Liebman believed had been obtained by political pull. Liebman successfully achieved his goal, which constituted a material breach of the MRE-5 Contract. Freedom is entitled to recover damages for Liebman's heinous acts.

5. Summary

Every *Apex* bad faith criteria has been established. The Government's actions were in bad faith. They constitute a breach of Freedom's MRE contract. Accordingly, Freedom is entitled to common law breach damages as set forth below.

C. THE GOVERNMENT BREACHED AN IMPLIED IN FACT AGREEMENT WITH FREEDOM TO MAINTAIN FREEDOM AS A WARM BASE PLANNED PRODUCER IN THE MRE IPP PROGRAM.

1. The Parties Entered Into An Implied-In-Fact Agreement To Maintain Freedom As A Warm Base Planned Producer In The MRE IPP Program.

a. Introduction.

The purpose of the MRE IPP program and of individual procurements under the MRE IPP program was to establish, develop and maintain industrial planned producers of mobilization essential items, such as MREs, in order to meet the mobilization needs of the nation's armed

forces in the event of war or national emergency. Findings 362-364. To that end, the program specifically attempted to support the best interests of the Government by first establishing MRE producers and then maintaining them with annual Minimum Sustaining Rate (MSR) awards. Findings 366-370. The MRE-5 Contract with Freedom - and any MRE contract for that matter - was a means to that end. *American Radio Hardware Co., Inc.*, ASBCA No. 3069, 57-2 BCA ¶ 1438 (1957).

The award of contracts in support of the MRE industrial planned producer program was never based on formal advertising. The agency, DLA, negotiated these contracts pursuant to the authority granted by 10 USC §2304(a)(16) and DAR 3-216. This meant that the Government could negotiate exclusively with the contractors established as IPP planned producers. Finding 360.

In the case of an ordinary supply contract, the purpose of the contract is to supply conforming material which satisfies a known field-stock or depot requirement. An MRE contract awarded as part of the IPP program had a very different goal. Its primary purpose was not product supply, although it accomplished that goal, but the retention of planned producers' production capabilities and the continued participation of such producers in the program. Findings 362, 366, 369.

The minimum sustaining rate (MSR) was a key factor in MRE planned producer maintenance. The MSR was established as the lowest monthly production rate at which a producer's plant could economically produce the essential items **so as to retain its production/maintenance capabilities.** Finding 370. Periodic and systematic award of MSR contracts was deemed essential to achieving the overall goals of the program, namely, to establish

and maintain producers to be part of an industrial base which could be kept available for the purpose of ramping up production of mobilization essential items in time or war or national emergency. Findings 366-369.

Thus, the Government had to obligate itself to each planned producer to make periodic awards of MSR contracts in order to be assured that the producer would obtain/retain and maintain the necessary facilities, personnel and planning that would allow the required production response in times of emergency. Finding 371.

The understanding between the Government and qualified MRE planned producers to award periodic follow-on contracts was never put in writing. In reality, and undeniably, it was an implied-in-fact agreement absolutely necessitated by the Government's critical need to maintain each contractor as a warm base planned producer. Findings 360-374.

On March 30, 1982 the Government admitted Freedom to the MRE program as a planned producer. Finding 385. Freedom is identified as one of three planed producers designated for award of an MRE 5 minimum sustaining contract pursuant to the secretarial D&F supporting that procurement. This admission established the implied-in-fact agreement between Freedom and the Government. Finding 387.

After a court battle initiated by Freedom to enforce the implied-in-fact agreement (Findings 391, 392), the Government began implementation with an MSR contract to Freedom. Findings 393-404. The Contract, under MRE 5, was awarded on November 15, 1984. Finding 403.

Unfortunately, as described above, in the administration of Freedom's MRE-5 Contract, the actions and decisions of the ACO, Liebman, and other officials, driven by a deep-rooted

negative attitude against Freedom and its President, Henry Thomas (Findings 76-85) served both as a rejection of these goals and the unlawful elimination of Freedom from the program. As such, the Government breached its implied-in-fact agreement with Freedom. As a result, Freedom is entitled to common law breach damages. Findings 404-409.

b. <u>The Law</u>.

That the United States may be bound by an agreement implied-in-fact is well established. The Courts and Boards of Contract Appeals have often so held and have clearly established the necessary elements. In *Webster University v. United States,* 20 Cl. Ct. 429 (1990), the United States Claims Court provided the following guidance:

> In order to prove the formation (or lack) of a contract, the parties must address four basic elements: (1) mutuality of intent, *e.g., Saul Bass & Associates v. United States* [20 CCF ¶ 83,194], 205 Ct. Cl. 214, 226-227, 505 F.2d 1386, 1393 (1974); (2) offer and acceptance, *e.g., Russell Corp. v. United States,* 210 Ct. Cl. 596, 608-609, 537 F.2d 474, 481-482 (1976), *cert. denied,* 429 U.S. 1073, 97 S.Ct. 811, 50 L.Ed.2d 791 (1977); (3) consideration, *e.g., Brannan v. United States,* 7 Ct. Cl. 399, 405 (1985); and (4) actual authority to contract in the agent purporting to act on behalf of the Government, e.g., *H.F. Allen Orchards v. United States,* 794 F.2d 1571, 1575 (1984).
>
> These elements are the same for both expressed and implied-in-fact contracts. *See, e.g., Fincke v. United States,* 230 Ct. Cl. 233, 244, 675 F.2d 289, 295 (1982), citing *Baltimore and Ohio R.R. Co. v. United States,* 261 U.S. 592, 43 S.Ct. 425, 67 L.Ed. 816 (1923). Most importantly, the critical need to demonstrate mutuality of intent, and in turn the lack of ambiguity, an offer and acceptance is the same for both; it is only the nature of the evidence that differs. *Russell,* 210 Ct. Cl. at 609, 537 F.2d at 482. *An expressed contract must be manifested by words, either oral or written, which contain agreements and/or mutual assent, E.g., Bank & Trust Co, v. United States,* 11 Cl. Ct. 554, 556 (1987); *Gratkowski v. United States,* 6 Cl. Ct. 458, 461 (1984). An expressed contract speaks for itself and leaves no room for implications. *Algonac*

> *Manufacturing Co. v. United States* [15 CCF ¶ 83,789], 192 Ct. Cl. 649, 674, 428 F.2d 1241, 1255 (1970)(citation omitted). ***An implied-in-fact contract, on the other hand "is one inferred from the circumstances or acts of the parties."*** *Algonac*, 192 Ct. Cl. at 674, 28 F.2d at 1255 (citation omitted).

Webster University, supra, 20 Cl. Ct. at 432-33 (emphasis added).

The MRE procurement history, detailed in Findings 1-8; 360-409, is replete with evidence of each and every element required to establish an implied-in-fact contract in favor of Freedom:

i. **Mutuality Of Intent.** The Claims Court has said with respect to implied-in-fact contracts, that "(m)utuality is inferred from conduct of the parties showing, in light of the surrounding circumstances, their tacit understanding." *Kollsman, a Division of Sequa Corporation v. United States,* 25 Cl. Ct. 500, 514 (1992).

The circumstances of this case absolutely demonstrate the parties' intent, indeed, **the absolute necessity,** that periodic follow-on contracts would be negotiated by the Government with its MRE contractors for a portion of each year's procurement at the contractor's MSR, so long as the contractor's price was reasonable and the contractor remained capable of producing sufficient MRE units. Findings 369-372.

- **The Government**

Department of Defense Directive 4005.1 (July 28, 21972) entitled "DoD Industrial Preparedness Production Planning" (Finding 375; R4, tab FT001) was the foundation document for implementing any IPP program for the Defense Department. The Directive, under its heading "Purpose and Authority," established responsibilities governing industrial preparedness planning for production of essential military items in a national emergency. To accomplish this, it indicated that the Department of Defense would provide a sustained state of industrial preparedness for the

production of essential military items to meet the needs of the approved U.S. and Allied Forces in a national emergency.

MREs are unique "war stoppers." Findings 363-364. There is no commercial equivalent. Finding 366. Further, the MRE planned producers, including Freedom, had no other business. Without annual MSR contracts **the Government knew** that these essential producers, and the Government's mobilization capability, would be lost. Findings 367-370.

Entry into the MRE program required a large investment. It was an investment the large food processing companies were unwilling to make. Findings 379, 380. To induce the investment and maintain the essential mobilization capability, the Government provided an incentive: **an unstated agreement to maintain a planned producer through yearly warm base contract awards.** Finding 374.

- **Freedom**

Prior to its involvement in the MRE IPP program, Henry Thomas, as President of Freedom, had successfully operated a food processing business out of two USDA inspected and approved facilities. Finding 13. Freedom became aware of the MRE program in 1980. Tr. 218-19.

The Government, from the very beginning of its contact with Freedom, advertised its intent. Freedom was made aware of the D&Fs supporting the annual MSR contracts to planned producers Sopakco and Rafco. Findings 372; 375-377. Freedom was also made aware of how the Government viewed its obligation to the planned producers. Findings 382-385. Freedom, as set forth below, understood and relied on the Government's intent. Findings 388-392.

Freedom understood the Government's intent and wanted to become part of the program.

Finding 381. Freedom went into debt and invested heavily in plant and equipment to meet the Government's requirements (1) that an MRE assembler be Walsh Healey qualified and (2) have sufficient facilities to meet mobilization demands. Freedom also, at the Government request, abandoned its school lunch business. Findings 18-31.

Freedom's intent to be bound by the implied-in-fact agreement became reality when it was designated an MRE planned producer on March 30, 1982. Finding 385. Freedom's entire future was now totally tied to the Government's good faith compliance with its implied-in-fact agreement. As Mr. Alan Koerber, one of the principal Government architects of the MRE program testified:

> [I]f we did not give them continuing contracts, we felt there was a better than average chance, probably a really good chance that they would go out of business. They had nothing else to support their production. So, if they didn't have a contract from us, they would close down the plant.

ii. Offer and Acceptance

The Claims Court in *Kollsman, supra,* addressed the second implied-in-fact contract element, offer and acceptance. The Court said:

> An offer must be unambiguous, and acceptance must be manifested unambiguously by conduct that indicates assent. . . [Citations omitted.] Inducement or encouragement to do work may constitute the conduct that indicates acceptance. [Citations omitted.] Government acceptance of services without disclaiming an intention to pay after demand for payment is made supports and implied-in-fact contract. [Citations omitted.]

25 Cl. Ct. at 514.

The foundation for the Government's "offer" to enter into an implied-in-fact agreement to maintain IPP producers in the program was set forth in DoD Directive 4005.1. R4, tab FT001. DoD was charged with the responsibility for providing a sustained state of industrial preparedness for the production of essential military items such as the MRE. In addition, based on the MRE's unique circumstance, both parties understood that the basis of the bargain with respect to MRE mobilization was investment in capacity in return for warm base maintenance. Findings 360-404.

The Government offered Freedom entry into the MRE planned production program, and therefore into its implied-in-fact agreement, in June 1981. R4, tab 014. Freedom indicated its intention to accept the offer by its letter of September 28, 1981. Finding 381. The agreement was consummated when Freedom was designated an MRE planned producer on March 30, 1982. Finding 385.

iii. Consideration

In consideration for the Government's obligation to establish and maintain Freedom as a planned producer under the IPP program, Freedom: (a) agreed to give up all prior businesses and, indeed, any business opportunities other than the MRE, so that it could provide the Government the concentration on the MRE program that the Government demanded (Finding 18; Tr. 22- 23); (b) relied on the promise of receiving periodic MSR awards based upon representations by the Government as to the MSR for each of the planned producers that were identified in the program. (Findings 376, 377, 381-387, 391, 392; Tr. 52); (c) purchased production equipment available from APF in order to provide the capacity demanded by the Government (R4, tab FT44); (d) made a substantial investment in other production facilities and start-up costs also to provide the capacity demanded (Findings 18-23); and (e) went substantially into debt, in the neighborhood of

$2 million, in order to achieve all the above. Finding 19. None of these efforts would be productive nor the expense recovered unless the Government complied with its implied-in-fact agreement. Tr. 70,71.

The Government as consideration received the added production capacity that it was required to have in order to meet mobilization demands.

iv. Authority

The last element needed to affect an implied-in-fact contract concerns the authority of the individual purporting to act on behalf of the Government. That individual must have actual authority. *Webster University, supra.*

Freedom's request to become an MRE planned producer was forwarded to a top level contracting officer at DPSC, Mr. Michael Cunningham. Finding 381. Mr. Cunningham was Chief, Operational Rations Section, General Products Branch, Contracting and Production Division. Mr. Cunningham informed Freedom that he would respond to the request. *Id.* Further, the designation as a planned producer was ratified by no one less than the Under Secretary of Defense for Research and Engineering, Richard D. DeLauer. That ratification occurred at least as early as December 16, 1982 when Secretary DeLauer executed the MRE 4 D&F. That D&F included Freedom as an MRE planned producer. Finding 387. The Government officials responsible for the planned production designation, and therefore the implied-in-fact agreement, had actual contracting authority.

The Court of Appeals for the Federal Circuit summarized the formation of an implied-in-fact contract with the United States as follows:

> A contract implied-in-fact is not created or evidenced by explicit

> agreement of the parties, but is inferred as a matter of reason or justice from the acts or conduct of the parties. However, all of the elements of an express contract must be shown by the facts or circumstances surrounding the transaction - - - mutuality of intent, offer and acceptance, authority to contract - - - so that it is reasonable, or even necessary, for the Court to assume that the parties intended to be bound.

Prudential Insurance Co. of America v. United States, 801 F.2d 1295, 1297, *cert. denied,* 470 U.S. 1086 (1987).

The implied-in-fact agreement that Freedom would continue to be maintained as an IPP producer is obvious and, as set forth, above supported by all the elements of an express contract.

2. DoD's Objective To Establish And Maintain Planned Producers Could Not Be Achieved In The Absence Of An Implied-In-Fact Agreement.

But for the implied-in-fact agreement, DoD's primary goal of establishing and maintaining planned producers for MREs in order to meet the mobilization needs of the nation's armed forces in the event of war or a national emergency could not be achieved. Findings 362; 368-372. Consideration of the MRE-5 Contract as simply a procurement to provide MRE units to meet the 1984-85 requirements would have not achieved that purpose. Such a stand-alone interpretation of the MRE-5 Contract would have rendered the overall goal as meaningless. *American Radio Hardware Co., Inc., supra.*

The Board was faced with a similar situation in *United Technologies Corp., Pratt & Whitney Group,* ASBCA Nos. 46880 et al., 97-1 BCA ¶ 28,818 (1997). In that case, the Navy sought to avoid its obligation to award follow-on contracts to Pratt & Whitney, its established dual source for the F404 based upon a narrow reading of a particular clause in the F404 dual sourcing contract. The clause in question, the "Investment Incentive clause," said that if

specified conditions were met, the Navy intends to award future second source F404 engine contracts to Pratt & Whitney. The Navy contended that this language did not establish a contract obligation to award future contracts to Pratt & Whitney.

Citing *Hol-Gar Manufacturing Corp. v. United States*, 169 Ct. Cl. 384, the Board stated that the intention of the parties to a contract must be gathered from the whole instrument. The Board indicated that the Navy's narrow focus of the plain meaning of the word "intends" leaves the other provisions of the Investment Incentive clause useless, inexplicable, meaningless and superfluous. The Board concluded that not awarding Pratt & Whitney the future dual sourcing contracts for the F404 constituted a breach by the Navy of the Investment Incentive clause for which the Navy was liable for the common law damages caused by such breach.

Indeed, the Board very recently recognized directly that planned producer status implies sustaining contract awards. Although the Board found in *Defense Systems Company, Inc.*, ASBCA No. 50918, 00-2 BCA ¶ 30,991 (2000) that the appellant did not have a contractual right to a sustaining contract, that conclusion was based on a finding that the contractor had **not** become a planned producer.

> As the 'Base Retention Requirements' clause made clear, the establishment of a mobilization base contractor was through execution of a PPS contract and 'at the Government's discretion.' Since no PPS contract was executed between DSC and the Government, we conclude that DSC had no contract right under the systems contract to be awarded the fin and nozzle replacement work.

Defense Systems Company, Inc., supra (emphasis added).

The parallel with the Freedom case is clear. If the Freedom contracting officer had unfettered discretion to remove Freedom from the program, or more specifically, to engage in

egregious conduct that caused Freedom's removal from the program, what was the incentive of Freedom to give up its existing business and make substantial investments that could only be recovered in future contracts? Likewise, if the contracting officer could ignore the existence of an implied-in-fact contract and arbitrarily remove Freedom, or any other planned producer, from the program, DoD's obligation to establish and maintain an MRE mobilization base was impossible to meet and therefor meaningless.

3. The Government Breached the Implied-in-Fact Agreement to Continue Freedom in the Program.

This Brief, as set forth above, details the egregious pattern of abuse of discretion and bad faith faced by Freedom during the performance of the MRE- 5 Contract. Those Government acts so poisoned the relationship between Freedom and DLA that DLA decided to eliminate Freedom from the MRE program. An additional planned producer, CINPAC, was illegally added to the program with the specific intent to replace Freedom. Freedom never received another MSR contract. The implied-in-fact agreement was breached.

D. DAMAGES.

1. Equitable Adjustment Entitlement – Freedom Is Entitled To An Equitable Adjustment Under The Changes Clause Of The MRE-5 Contract On Account Of The Compensable Acts And Omissions Of The Government.

The Government contract jurisprudence concept of the constructive change is now more than 50 years old. If the Government, in the person of an individual with actual authority, acts or fails to act in a manner that, within the scope of the contract, changes contract requirements, a "constructive change" results. Under such circumstances, the contractor is entitled to an

equitable adjustment in contract price (costs plus a profit thereon) and/or an extension in performance time. This is the case even though such "change" is never reduced to writing.

Section III.A above sets forth a panoply of acts and omissions, all the responsibility of individuals with actual authority, that amount to constructive changes of the MRE-5 Contract. Section III.E below addresses the quantum calculation of the equitable adjustment for each constructive change. Freedom respectfully requests that the Board find for the existence of such constructive changes and order the equitable adjustments claimed.

2. Common Law Breach Damages – The Government's Acts and Omissions, All as Set Forth Above, Constituted a Material Breach of Both the MRE-5 Contract and the Parties' Implied-in-Fact Agreement So That the Contractor is Entitled to Common Law Breach Damages, As Set Forth Below and Quantified in Section III.E.

The Contract Disputes Act of 1978, 41 U.S. C. § 607d, authorizes the Board to grant relief for breach of contract. It provides that an agency board "is authorized to grant any relief that would be available to a litigant asserting a contract claim in the United States Claims Court." *Darwin Construction Co., Inc. v. United States,* USCFC No. 86-1370, 33 CCF ¶ 75,063 (1987).

The Government is liable like any private party for all damages resulting from its contract breaches. *United States v. Winstar Corporation,* 116 S. Ct. at 2453 (1996) ("when the United States enters into contractual relations, its rights and duties are governed generally by the law applicable to contracts between private individuals") (quoting *Lynch v. United States,* 229 U.S. at 579*); United States v. Spearin,* 248 U.S. 132, 138 (1918); *United States v. Behan,* 110 U.S. 338, 346 (1884). The primary common law measure of damages seeks to award the injured party his "expectation interest" in the transaction, *i.e.*, place it in as good a position as it would have been in had the Government fully performed its obligations); *Miller v. Robertson,* 266 U.S. 243, 257

(1924); *Massachusetts Bay Transportation Authority v. United States,* 42 CCF ¶77, 290 (Fed. Cir. 1997); *San Carlos Irrigation and Drainage District v. United States,* 111 F.3d 1557, 1562-63 (Fed.Cir.1997); *Estate of Berg v United States,* 21 Ct. Cl. 466, 687 F.2d 377, 379 (1982); *Needles v. United States,* 101 Ct. Cl. 535, 619 (1944). Such damages should include all profits that should have been within the contemplation of the parties when the contract was made. *Olin Jones Sand Co. v. United States*, 225 Ct. Cl. 741, 642-44 (1980). They also include those incidental and consequential damages arising foreseeably from the breach. *Mass. Bay Trans, supra; PAAE International,* ASBCA No. 45314, 98-1 BCA ¶ 29,347 (1998)("Complete, as opposed to partial, relief for breach of contract includes, therefore, recovery for both types of loss"); *Allegheny Iron Co. v. Teaford,* 96 Va. 372, 31 S.E. 525, 527 (1898) (allowing loss of profits and consequential damages). *See also* UCC §2-710 ("Incidental damages to an aggrieved seller include any commercially reasonable charges, or commissions incurred . . .or otherwise resulting from the breach"); White & Summers, *Uniform Commercial Code* §6-5 (3rd Ed. 1988) ("Consequential damages may include sums for lost profits, loss of goodwill, losses resulting from interruption of . . . production processes, lost interest and much else")

Alternatively, the injured party may recover those damages sustained in detrimental reliance upon the contract. *Restatement (Second)* at § 349, comment a, and § 344(b); 3 Dobbs, *Remedies* §12.3(2) at 51-52; McCormick, *Damages,* § 142 at 584. Reliance damages are also appropriate whenever lost profits have not been sufficiently proven. *United States v. Behan,* 110 U.S. 338, 347 (1884) ("The claim for profits, if not sustained by proof, ought not to preclude a recovery of the claim for losses sustained by outlay and expenses"); *Coastland Corporation v. Third National Mortgage Co.,* 611 F.2d 969 (4th Cir. 1979)(applying Virginia law); *Burnstein v.*

United States, 232 F.2d 19, 22 (1956); accord *Restatement (Second)* §349, comment a, illus, 1-2; 5 Corbin, Contracts, § 1031 at 188-91: Calamari & Perillo, §4-9 at 603 -04 (3d ed. 1987).

Freedom has proven breaches of both contract and contractual duties. It is entitled to recover on the basis of the alternate theories. *United Technologies Corp., Pratt and Whitney Group,* ASBCA Nos. 46880, et al., 96-1 BCA ¶ 28,226 (1996)(citing *Acme Process Equipment Co. v. United States,* 171 Ct. Cl. 324, 356-60, 347 F.2d 509, 528-30 (1965)); *Restatement (Second),* §378, comment a (1981) ("Alternative counts seeking inconsistent remedies are generally permitted, . . . even at an advanced state of the action"); *Banner Mfg. Co. v. United States,* 125 Ct. Cl. 384, 112 F. Supp. 365, 367 (1953) (election of remedies rule "is recognized as a harsh and largely obsolete one which should not be extended"); *accord* 5 A. *Corbin,* supra, § 1104 (1964). Freedom is entitled to recover all non-overlapping damages that resulted from these breaches.

Freedom is entitled to its expectation interest damages on account of the Government's breach of the implied-in-fact agreement. These include lost profits on all contract awards to CINPAC, *i.e.*, MRE 7 through the present. Damages also include the adverse impact on Freedom's guarantor, Mr. Henry Thomas.

Expectation interests are also recoverable as the result of the breach of the MRE-5 Contract. These include the lost profits on the terminated 107,600 MRE cases.

Restitution damages by breach of the implied-in-fact agreement and/or the MRE-5 Contract include the loss of the value of Freedom as a business. Restitution damages resulting from the breach of the MRE-5 Contract include all uncompensated costs incurred by Freedom in the performance of that contract.

In any event, Freedom is entitled to be compensated for all foreseeable damages flowing from the Government's breaches. The Quantum Section of this brief sets forth the specific damages identified for each Government act or omission including lost profits.

a. Expectation Interest Damages.

Section 347 of the *Restatement (Second), supra,* provides, in pertinent part, that:

> The injured party has the right to damages based on his expectation interest as measured by the loss in value to him of the other party's performance caused by its failure or deficiency, plus any other loss, including incidental or consequential loss, caused by the breach, less any cost or other loss that he has avoided by not having to perform.

Accord 3 Dobbs, *Dobbs Law of Remedies,* §12.2 (1), at 22 (2d. Ed. 1993). These elements of expectation damages are recoverable when the breach damages satisfy the three proof elements of foreseeability, causation, and reasonable certainty. *See, e.g., Energy Capital Corp., as General Partners of Energy Capital Partners Limited Partnership v. United States,* 47 Fed. Ct. 382, No. 97-293C (August 22, 2000), *Neely v. United States,* 285 F.2d 438, 443 (Ct. Cl. 1961); *Goolsby v. United States*, 21 Cl. Ct. 88, 91 (1990). The standards for these three elements of proof are as follows:

Foreseeability: The question as to whether particular damages are foreseeable is one of fact. *International Gunnery Range Services, Inc.,* ASBCA No. 34152, 96-2 BCA ¶ 28,497 at 142,306; *Environmental Tectonics Corporation,* ASBCA No. 42540, 92-2 BCA ¶ 24,902; *Joseph Becks and Associates, Inc.,* ASBCA No. 31126, 86-3 BCA ¶ 19,299. *Neely,* 285 F.2d at 443.

There are two, independent ways to prove such foreseeability – actual foresight or objective foreseeability. First, it may be shown that the breaching party actually foresaw the consequences of a particular breach. Alternatively, it may be shown that the consequences of a breach were reasonably foreseeable "in the ordinary course of events," although there is no evidence that they were actually foreseen at the time of contracting, *see Roanoke Hospital Assn. v. Doyle and Russell, Inc.*, 215 Va. 796, 214 S.E.2d 155, 160 (1975) (foreseeability of the specific injury or its exact amount not required). The *Restatement* provides:

> Loss may be foreseeable as a probable result of a breach because it follows from the breach in the ordinary course of events, or as a result of special circumstances, beyond the ordinary course of events, *that the party in breach had reason to know.*

Restatement (Second), supra, §351(2)(b) (emphasis added); accord UCC §2-715(2)(a). *See also Restatement (Second), supra,* §351(2)(a), comment a (1981)("the test is an objective one based on what he had a reason to foresee"); 5 *Corbin,* §1014 (1964); 11 *Williston on Contracts,* §1344 3rd Ed. 1979).

Causation: Whether damages were, in fact, caused by a breach is also a question of fact. *Olin Jones Sand Co. v. United States,* 225 Ct. Cl. 741 (1980). Where an injury may have resulted from multiple causes, including a contract breach, the rule is that "the plaintiff must show that the defendant's breach was a 'substantial factor' in causing the injury" and that any other contributing factor was foreseeable. 5 *Corbin,* §999-1000 at 24 - 25 (1964 and 1998 Supp.) (citing numerous cases). Professor Corbin has noted that:

> In all cases involving problems of causation and responsibility for harm, a good many factors have united in producing the result; the plaintiff's total injury may have been the result of many factors in addition to the defendant's tort or breach of contract. Must the

> defendant pay damages equivalent to the total harm suffered? Generally the answer is Yes, even though there were contributing factors other than his own conduct.

Id. (footnotes and citations omitted); *see also Gardner Displays Co. v. United States*, 171 Ct. Cl. 497, 346 F.2d 585, 589 (1965) (breach exposed plaintiff to other contributing causes of compensable loss); *Continental Ill. Nat'l Bank and Trust Co. v. United States*, 115 F. Supp. 892, 896 (Ct. Cl. 1953) (Government liable for entire injury even if its breach was not "the sole cause").

Reasonable Certainty: Where a plaintiff establishes the fact of damages with reasonable certainty, the amount of damages is proven damages ". . .if the evidence adduced enables the court to make a fair and reasonable approximation of the damages." *Locke v. United States*, 151 Ct. Cl. 262, 283 F.2d 521, 524 (1960). While the calculation of damages "cannot be speculative," it "need not be proven with unerring precision." *Bio-Rad Labs, Inc. v. Nicolet Instrument Corp.*, 739 F.2d 604, 616 (Fed. Cir.), *cert. denied*, 469 U.S. 1038 (1984), *appeal after remand*, 807 F.2d 964, *cert. denied*, 482 U.S. 915 (1987). *See also T. Brown Constructors, Inc. v. Pena*, 42 CCF ¶ 77232 (Fed. Cir.)(1997); *Himfar v. United States*, 174 Ct. Cl. 209, 355 F.2d 606, 611 (Ct. Cl. 1966)("it is not necessary that plaintiff present proof of the amount of [anticipated profits] with an absolute certainty"). Furthermore, there is no requirement that a contractor maintain any specific records of its damages. *Neal & Company, Inc. v. United States*, 945 F.2d 385 (Fed. Cir. 1991) ("it would [be] grossly unfair to keep one set of records for work originally contemplated under the contract and another set of records for the additional work")

In accordance with these legal standards, Freedom's proven expectation damages are as follows:

i. Lost Profits on MRE-5

The Government breached Freedom's MRE-5 Contract. As a direct result, Freedom was prevented from completion and delivery of 107,842 MRE cases. Finding 405. As a measure of common law damages, Freedom is entitled to the lost profit on these cases. Freedom is entitled to the lost profit on these cases. The calculation of that profit as impacted by the termination settlement is set forth in Section III.C., below.

ii. Lost Profits Because of the Breach of the Implied-in-Fact Agreement

Foreseeability: Foreseeable damage flowing from a breach of contract may include lost profits. As a result, the Government has been held to have objectively foreseen, and therefore to be responsible for, the loss of anticipated profits. *See, e.g., Energy Capital Corp., supra; United States v. Purcell Envelope Co.,* 39 S. Ct. 300, 303 (1919) (awarding 4 years of lost estimated profits); *Urban Data Systems, Inc. v. United States,* 669 F.2d 1147 (Fed. Cir. 1983) (affirming award of lost profits from breach of implied-in-fact contract); *Northern Helex Co. v. United States,* 634 F.2d 557 (Ct. Cl. 1980) (awarding anticipated profits and incidental damages); *Peck Iron & Metal Co. v. United States,* 221 Ct. Cl. 37, 603 F.2d 171, 175-77 (1979) (awarding "anticipated profits" damages against the Navy); *North Star Aviation v. United States,* 458 F.2d 64, 66 (Ct. Cl. 1972) (awarding lost profits); *Gardner Displays Co. v. United States,* 171 Ct. Cl. 497, 346 F.2d 585 (1965); *Senor Tenedor, S.A. de C.V.,* ASBCA Nos. 48502 *et al,* 97-2 BCA ¶ 29,192 (awarding anticipatory profits); *International Gunnery Range Services, Inc., supra* (holding Government responsible for lost profits "reasonably supposed to be in the contemplation of the parties at the time of contract"); *Shawn K Cristensen, d.b.a Island Wide Contracting,*

ASBCA No. 95-188-R, 95-2 BCA ¶ 27,724 (awarding anticipatory profits); *Keith L. Williams,* ASBCA No. 46068, 94-3 BCA ¶ 27196; *E.L. Hamm & Associates, Inc.,* ASBCA No 43972, 94-2 BCA ¶ 26,724 (damages from Navy holdover after appellant's graduation from the 8(a) Program potentially foreseeable from time of contracting); *Hector Rivera Ruiz,* ASBCA No 1756, 88-3 BCA ¶ 20,829 (awarding lost profits for breach of implied duty); *S&S Equipment,* ASBCA No. 36681. 89-1 BCA ¶ 21,469 (awarding lost profits for breach of implied duty); *Summit Contractors,* ASBCA Nos. 81-252-1, 83-312-1, 86-1 BCA ¶ 18,632 (awarding lost profits); *Tamp Corporation,* ASBCA No 25692, 84-2 BCA ¶ 17,460 (awarding lost profits for termination that was an abuse of discretion); *Stoner-Caroga Corp., Inc. v. United States,* 3 Cl. Ct. 92 [31 CCF ¶71,370] (Ct. Cl. 1983); *Smith Surplus Metals,* ASBCA No. 25128, 81-1 BCA ¶ 15,123 (awarding net profits); *James J. Temple,* ASBCA No. 21447, 79-1 BCA ¶ 13,605.

Freedom has proven that its lost profits were reasonably foreseeable at the time of contracting. The implied-in-fact contract to continue Freedom in the MRE program was breached by the Government when Liebman and others embarked on an egregious pattern of abuse of discretion and bad faith acts specifically designed to remove Freedom from the program and thereby eliminate Freedom as a planned producer for future MRE contracts. The Government understood that if it prevented Freedom from completing MRE-5, it would lead to a termination and Freedom's inevitable elimination from the MRE program. Likewise, the Government must have expected that Freedom planned to earn profits on all its contracts. That was the reason it was in business. *See Energy Capital, supra.*

Causation: The record clearly shows that the Government's breaches were not only a substantial factor in causing Freedom's loss of profits, but were *the primary cause*. *Continental*

Ill. National Bank & Trust Co. v. United States, 115 F. Supp. 862, 896 (Ct. Cl.1953) (Government liable for entire injury even if its breach was not "the sole cause"); *Gardner Displays Co. v. United States,* 346 F. 2d 585, 589 (Ct. Cl. 1965) (breached exposed to plaintiff to other contributing causes of compensable loss); *Energy Capital, supra,* (court only required plaintiff to prove that the breach was a substantial factor in causing its losses).

The record is clear. But for the Government's breaches, Freedom would have:

- completed the MRE-5 contract; (Tr. 998)
- been awarded MRE-7; (Tr. 999); and
- would have continued as the third planned producer receiving awards for all MRE contracts from MRE 7 through the present. Findings 368-372.

Reasonable Certainty: The requirement for determining lost profits with reasonable certainty was considered in the recent case of *Energy Capital,* 47 Fed. Ct. 382, *supra.* The central issue in that case was whether lost profits of a new venture may be obtained from the Government in a breach of contract case. The Court after reviewing several previous decisions on this subject, stated that the precedents did not preclude, as a matter of law, the awarding of lost profits when the plaintiff was involved in a new venture, nor did it preclude awarding lost profits of a new venture when the defendant was the United States. The Court found in *Energy Capital* that it was a case where the plaintiff was entitled to an award of lost profits and awarded $8.787 million as the present value for the plaintiff's lost profits.

The Government's argument was that because Energy Capital was engaged in a new business, any measure of lost profits would be unreasonable and speculative. The Court rejected that argument. The Court clearly recognized that the most reliable way for a new venture to

show lost profits with "reasonable certainty" would be to introduce evidence of subsequent performance by a third party under the exact same contract or contracts. That is exactly what Freedom is able to do.

Energy Capital was able to show that its new venture of originating loans for energy-efficiency improvements in Government-assisted housing, would have succeeded had the Government not breached its contract by improperly terminating it.

The Court concluded that Energy Capital met its burden of showing lost profits with reasonable certainty. The Court's conclusion relied heavily on earlier cases where reasonable certainty was the issue, *e. g.*, *Neely v. United States*, 285 F. 2d 438, 443, 152 Ct. Cl. 137, 146 (1961) and *Neely v. United States*, 167 Ct Cl. 407 (1964), a case where lost profits were awarded. In both *the Energy Capital* and the *Neely* cases, evidence was presented that allowed the plaintiff to establish the amount of lost profit.

A finding that Freedom's lost profits were proven with reasonable certainty fits into the pattern of precedents concerning lost profits, starting with the *Neely* cases, *supra.* A Government lease in *Neely* permitted the plaintiff to mine coal from a 2,000 acre plot of land. *Neely I,* 285 F.2d at 439, 152 Ct. Cl. 139. The Plaintiff could, then, sell the ore to purchasers for a profit. The Court of Claims found that the plaintiff established the amount of lost profit by introducing evidence of how much profit the plaintiff's assignee earned after actually mining the ore. *Neely I,* 285 F.2d at 443, 152 Ct. Cl. at 147. Thus, the Court of Claims affirmed the award of lost profits because of the performance by another party for the same services.

When viewed from one perspective, the facts here compare with the facts in *Neely.* The plaintiff in *Neely* had the right to use a specific resource – the plot of land and the coal beneath it.

The quantity of coal was finite and easily established. The amount of coal was an outer boundary on the plaintiff's income. After all the coal was extracted, the plaintiff could not generate any more income from this contract.

Likewise, Freedom has the opportunity to use the performance of CINPAC in MRE-7 through the present as a basis for measurement. The amount of lost profits on those contracts is like the quantity of coal in *Neely*. When each MRE contract was completed, Freedom could not earn any more revenue from it. Therefore, this case is analogous to *Neely* in that the source of profit revenue is easily established.

The record provides ample basis for a reasonable approximation of Freedom's loss of anticipated profits on MRE-7 on up. It is undisputed that the parties agreed to a profit rate of 14.88% for MRE-5. Findings 54-75. Freedom's expert witness on financial matters, Jordan Fishbane, supported Freedom's position on anticipated profits. Tr 999.

There is nothing in the record or elsewhere to believe that that same profit rate (or better) would not have been achieved on all the CINPAC MRE contracts which, but for the breach, would have been awarded to Freedom.

iii. Additional Lost Profits on Account of the Agreement Breach

Freedom's obligation under the implied-in-fact agreement was to invest in the extra capacity necessary to give Freedom the maximum mobilization capability. In early 1986, in reliance on the implied-in-fact agreement, Freedom arranged to obtain control of 4 additional

Rotomat retort machines from Nadar Ali, owner of APF and MidAmerica Foods. R4, tab FT441. The machinery had been purchased by APF through a US EDA loan granted to Mr. Ali. Freedom Industries set out to purchase this $5.5 million EDA note. R4, tab FT 265.

Mr. Koerber testified that the production capacity roadblock was retort capacity. Further, Sopacko had 5 retorts and RAFCO only 3. Tr. 62-64.

Freedom had 350,000 square feet of production space at its Bronx plant. With the 2 Rotomats in house and the additional 4 Rotomats, Freedom Industries would have had the greatest M +90 mobilization capacity of any MRE planned producer. But for the Government's breach, Freedom would have been the number one planned producer. Freedom's profits would have increased accordingly.

iv. Guarantor Thomas is Entitled to Expectation Damages as a Result of the Breach of the Implied-in-Fact Agreement

Foreseeability: Liebman did not differentiate between Freedom and Henry Thomas. Liebman knew that Freedom was Henry Thomas and Henry Thomas was Freedom. In fact, when Colonel Holland interviewed Liebman the question was not whether to do business with Freedom but whether to do business with Henry Thomas. R4, tab FT338.

Liebman hated Mr. Thomas and wanted him out of the program. Findings 76-79. It was entirely foreseeable to Liebman, and therefore to the Government, that if he destroyed Freedom he would also destroy Mr. Thomas. Not only was it foreseeable, it was his intent.

Causation: Freedom needed funding to meet the Government's MRE Industrial Preparedness Program entry requirements. The Government promised years of MSR

maintenance once entry was effected. Mr. Thomas personally guaranteed Freedoms' financing in order to meet the Government's requirements and based on the Government's promise.

Thomas personally guaranteed a $1.4 million loan from Dollar Dry Dock Savings Bank as well as $3.5 million borrowed from Bankers Leasing. In addition, trade vendors extended credit for over $3.3 million based on Thomas's personal guarantee.

In addition to loan guarantees, New York State and the Internal Revenue Service have declared Thomas as the "responsible party" for all unpaid taxes.

The Government's twin breach of the MRE-5 Contract and the implied-in-fact agreement left Thomas with the full weight of the debt and the unpaid taxes. As a result of the breaches, not only was Freedom destroyed as a viable business entity, but Thomas was left with a damaged reputation, heavy debt, and no ability to repay the loans or obtain credit.

Reasonable certainty: For the last 14 years, Mr. Thomas has worked to reverse the results of the breach. Without pay he has successfully overturned the wrongful default of the MRE-5 Contract, reversed the Government's long held position that Freedom owed the Government $1.6 million and therefore nothing was owed on account of the Board determined convenience termination[40], and prosecuted this claim for breach damages.

Mr. Thomas is being carried on Freedom's books for 14 years at an unpaid salary of $125,000 per year, plus reasonable benefits. But for the breach of the implied-in-fact agreement,

[40] Freedom has settled the termination for a net payment to Freedom of $799,947.

Mr. Thomas would have earned this salary, with medical and other benefits, as a minimum. Freedom requests, as consequential expectation damages, $2,000,000 in compensation for Mr. Thomas' unpaid salary .

b. Reliance (Restitution) Damages.

In addition to its claim for expectancy damages, measured by lost profits on the MRE contracts, Freedom also claims reliance (*i.e.*, restitution) damages for the Government's breach of MRE-5 and the implied-in-fact agreement.

California Federal Bank v. United States, 43 Fed. Cl. 445 (1999) states the basic principles of reliance damages:

> Reliance damages seek to place the plaintiff 'in as good a position as he would have been in had the contract not been made.' *Restatement (Second) of Contracts* §344 (b) 1981. Reliance damages included expenditures made 'in preparing to performing, or in foregoing opportunities to make other contracts.' *Restatement (Second) of Contracts* §344 comment a (1981). This relief is awarded on 'the assumption that the value of the contract would at least have covered the outlay.'

Even if Freedom is unable to prove expectancy damages with reasonable certainty (and it believes that it has), any failure on its part to prove lost profits will not prevent it from recovering its losses for actual outlay and expenditures on the MRE-5 Contract that were the direct result of the Government's acts.

The reliance/restitution damages sought by Freedom in this case relate to the additional costs incurred on MRE-5 as a result of the Governments acts and omissions as well as costs incurred in anticipation of the continued performance of the implied-in-fact contract

i. Increased costs to perform MRE-5.

Barring recovery of damages, whether breach damages or equitable adjustment, Freedom cannot recover costs from the Government, incurred in the performance of its MRE-5 Contract in excess of the current contract price. This is because the Government's acts forced Freedom to incur costs in excess of the Contract price while termination for convenience settlements cannot exceed the contract price.

Freedom now claims, in the alternative, that excess costs recoverable under equitable adjustment theory also represent reliance breach damages. Freedom has presented evidence to support its claim that these expenses would not have been incurred but for the Government's acts and omissions that amount to the breach.

The required foreseeability, causation and reasonable certainty elements have been presented in the equitable adjustment claim above and the quantum section below. The following is a brief overview.

(a) Progress Payment Failures.

The suspension of progress payments, interference with suppliers and financiers and other acts of interference by the Government resulted in a five (5) month delay in completion of the pre-production period. Pre-production was supposed to be completed by May 1985 and instead was not completed until October 1985. R4, tab FT443; Findings 86-256.

The Government's actions in its administration of progress payment necessitated the use of less efficient and more labor-intense equipment by Freedom and required additional

manpower. Tr. 891-891, 904-905, 1081-1084. The use of less efficient and more labor-intense equipment extended the production schedule by several months. Tr. 906-907; Tr. 1081-1084; R4, tab FT 444; Findings 208-232.

Other costly delays were encountered because the Government's failure to make timely progress payments caused the late installation of the automated lot tracking system. The Government also improperly rejected MREs that were fully compliant (Findings 336-337), caused materials that had been manufactured for Freedom to be diverted to other suppliers (Finding 281.a.), failed to provide GFM resulting in production shut downs and the inability of Freedom to complete the 114,658 cases in the MRE-6 configuration (Findings 314-323), and failed to make payments (DD 250s) for MRE units delivered and accepted. Findings 296-303.

(b) Self Financing Costs.

The unreasonable and inappropriate financing requirements forced on Freedom by the Government's breach caused Freedom to incur interest expense in an amount far greater than was reasonably anticipated. *See* Quantum below.

The recovery of the cost of debt capital during a period of payment delay does not infringe upon the statutory prohibition against the award of interest and Freedom would not be so precluded. *Framlau Corp. v. United States,* 568 F.2d 687, 694 (Ct. Cl. 1977); *Kollsman Instrument Corp.* ASBCA No. 14849, 74-2 BCA ¶ 10,837; *see also Wickham Contracting Co., Inc.*, 12 F.3d 1574 (Fed. Cir. 1994).

Freedom has introduced ample evidence into the record of its additional costs to self-finance the program. As previously indicated, Freedom's plans to self finance this contract were based upon the orderly and timely receipt of progress payments at 95% as set forth in the

Contract. Freedom's planned financing to cover the balance was identified in the spreadsheets and other agreed upon documentation that supported the negotiated final settlement of the contract. R4, tab FT062; Findings 38-64. Because of the Government's delays, suspensions and arbitrary reductions to the progress payments requested, Freedom was required to self-fund all of its pre-production costs during the first 5 months of the contract and a significant portion of the production costs thereafter. *See* R4, tab FT413.

The record is clear that as a result of the Government's withholding, suspension and reduction in progress payments, Freedom was forced to seek other sources of financing. Findings 128-148, 166-175. There would have been no other way for Freedom to have proceeded as far as it did in the performance of the Contract. Freedom completed the delivery of all MRE units with the exception of the units in the MRE-6 configuration which it was unable to because the Government failed to provide the necessary GFM. Freedom would not have increased and carried its additional debt if the Government had provided progress payments as required by the terms of the Contract.

Freedom has introduced documentation which shows the increased costs of self-financing. These costs have been accepted by DCAA (R4, tab FT413) and should be recoverable as detrimental reliance damages. *See* Quantum Section.

ii. Tax Penalties and Interest Charged Freedom Because of the Government's Payment Failures.

All tax penalties and interest that may be levied against Freedom on account of non-payment of taxes associated with MRE-5 performance are consequential damages stemming from the Government's breach of MRE-5.

Foreseeability: Penalties and interest that attach to non-payment of taxes are a matter of Federal law. The Federal Government and its agents are charged with knowledge of its own laws. The contracting officers responsible for the breach of Freedom's MRE contract could foresee that their payment failure would prevent tax payment. They knew that if they breached their obligation to make payment, Freedom could not pay its taxes. They knew, or should have known, that penalties and interest would follow.

Causation: With the exception of Federal income and excess profits tax, taxes levied against a contractor during the course of performance are allowable for progress payments. DAR 15-205.41(a). Freedom, as a small business, only had to accrue tax liability, not actually pay it, in order to be eligible for progress payment reimbursement. Had the Government met its progress payment obligations, Freedom's taxes would have been paid.

The Government's breach of MRE-5 manifested itself primarily in a planned bad faith attack on Freedom's sources of working capital. This included intentional acts that stymied both Government obligated financing (progress payments) and private financing.

The Government's payment failures were directly responsible for Freedom's working capital problem. Accordingly, the Government's intentional throttling of Freedom financially is the direct cause of Freedom's inability to pay payroll and other allowable taxes to New York City, New York State and the Federal Government.

The Government not only failed in its payment obligation, but it took steps to assure Freedom's inability to pay accrued taxes. On October 9, 1985, DLA's William Keating, then Chief of DLA's Contract Administration Division, instructed his New York office as follows:

> 2. The reference reported that subject contractor was indebted to the City and State of New York and the Federal Government in the approximate total of $549,256. From the data in the report, it appears that the contractor is delinquent not only in payment of the company's liabilities but also delinquent in payment of employee withholding.
>
> 3. **Please advise whether the progress payments have been appropriately reduced to exclude these unreimbursed costs from the progress payments base. . . .**

R4, tab FT312 (emphasis added).

The New York office told Mr. Keating that he need not worry. They told him that progress payment were already substantially reduced on account of DCAA disallowances and the loss ratio. R4, tab FT314. The campaign had worked. There would be no progress payments available for taxes.

Reasonable Certainty: The assessment of tax penalties and interest is a function of the taxing authorities. As such, it will be an amount determined with absolute certainty. To date, however, no such assessments have been issued. Freedom requests, therefore, that the Board simply determine Government responsibility. Further, Freedom requests that the Board order the Government to pay such assessments when they attach.

iii. Damages Incurred in Reliance on the Continued Performance of the Implied-in Fact Agreement (Diminution in Business Value).

It is undisputed that the Government's breaches also impact Freedom's value as a going business. "It is well settled that, where a regular and established business is wrongfully injured, interrupted, or destroyed, its owner may recover the damages sustained." *Yates v. Whyel Coke Co.*, 221 F. 603 (6th Cir. 1915); *see also Industrial Indemnity Co., et. al., v. United States,*

26 Cl. Ct. 443 (Fed. Cir. 1992)(recognizing a claim of damage to the business if foreseeable at the time of contracting); *accord*, 25 C.J.S. §90 (1966) (and cases cited therein). In order to make Freedom truly whole, it would be necessary to compensate Freedom for the additional damage caused to its good will and other business value that also resulted from the Government's breaches.

Foreseeability: Given the unusual history of the MRE program, this case is clearly distinguishable from the many cases in which diminution of business was not foreseeable. *Cf. Wells Fargo Bank v. United States*, 33 Fed. Cl. Ct. 233 1995, *rev'd. in part*, 88 F.3d 1012 (Fed. Cir. 1996) (cases denying recovery for loss of other business are decided on foreseeability grounds). The Government was fully aware of Freedom's dependence on progress payments and upon completion of the MRE-5 Contract to stay in the program. The Government was fully aware that Freedom's continuation in the program as a supplier was also contingent upon progress payments and the Government's fullest cooperation.

Causation: As with Freedom's claim for lost profits, the Government's breaches as indicated in the Findings are shown to be the "substantial cause" of the damage to Freedom's business. The record as previously discussed provides an unclouded and unbroken chain of events leading to Freedom's fiscal collapse.

Reasonable Certainty: There is no dispute that Freedom's business became essentially worthless after these breaches. After Freedom was eliminated from consideration for the MRE-7 and was forced to shut down its operation, the value of Freedom's business became zero.

c. Other Equitable Relief (*Status Quo Ante*).

As fully explained above, the truly guiding principle of breach damages is, at a minimum, to return the injured party to the position it would have held but for the Government's breach. *Miller v. Robertson, supra; San Carlos Irrigation v. United States, supra; Estate of Berg v. United States, supra; Needles v. United States.* Freedom respectfully requests the Board to take all actions possible, as follows, to realize that principle.

The Government termination of the MRE-5 Contract in June 1987 constituted a breach of the implied-in-fact agreement as well. Although Freedom desperately attempted to remain in the program, it is now abundantly clear that the Government's MRE 5 administration intentionally doomed that effort.

The law on termination for convenience in 1987 was governed by *Ronald A. Torncello and Soledad Enterprises Inc. v. United States,* 681 F.2d 756 (Ct. Cl. 1982). *Torncello* held that the Government could not terminate a contract for convenience if the requirement remained in existence. Even in light of the gloss that has since been applied to Torncello, a bad faith termination for convenience is converted to a breach of contract.

At the time the Government illegally defaulted Freedom's MRE-5 Contract and thereby breached its implied-in-fact agreement, the MRE mobilization planned producer requirement continued to exist. It exists today.

In order to be fully restored to the condition it held as of the breach, Freedom must be restored to the program. Freedom respectfully requests that the Board grant such relief, return Freedom to the *status quo ante,* and order Freedom's restoration.

d. Prompt Payment Interest.

The Government was under an obligation to make prompt payment on invoices submitted by Freedom. Pursuant to DAC #76-42, dated February 28, 1983, such payment was to be made "within 5-10 days of a proper request." Finding 90. Failure to make such payment subjects the Government to liability for interest under the Prompt Payment Act. 31 USC §3901 *et seq.*

Freedom submitted timely acceptable invoices, both for progress payment and delivered product (DD250s). Government payment was substantially late in almost every instance. The Government's delinquent payment record is set forth in R4, tab FT396. Freedom respectfully requests Freedom entitled to prompt payment interest, as set forth in Section III.E, below.

E. QUANTUM.[41]

1. Introduction

For the Quantum aspect of this case, and as detailed in **Figure 1**, Freedom seeks:

Equitable Adjustment to Contract To Recover Increased Costs for Constructive Changes	**$ 9,686,129.**
Unrecovered Program Investment Costs	**$ 1,062,138.**
Lost Profits on Successive MRE Awards	**$ 20,748,290.**
Financial Damages	**$ 16,611,660.**
TOTAL	**$ 48,108,217**

[41]The charts referenced in this Quantum section are attached as an Appendix to the Brief.

a. **Equitable Adjustment**.

$9,686,129 is requested as an equitable adjustment to the contract price to compensate Freedom for the additional costs incurred resulting from performing a contract with numerous constructive changes described in Section III.A. above. These constructive changes caused a series of delays and disruptions that stretched the program from 14 months to more than 30 months. Freedom was forced to expend considerable additional costs for production labor because it had to use slower and more labor intensive production equipment and because of numerous inefficiencies stemming from starts, stops, layoffs, rehiring and retraining. In addition, there were instances of unnecessary rework.

Freedom also incurred interest expense beyond which the parties had contemplated because Freedom was forced to rely heavily on private financing when the Government failed to fulfill its obligations to provide 95% progress payments financing.

b. **Unrecovered Program Investment Costs.**

$1,062,138 is requested for unrecovered program investment costs, plus an appropriate profit application. The amount is for expenditures for equipment, plant renovation and leasehold alterations which were reviewed and contemplated as necessary by the parties when the MRE-5 Contract was negotiated. The parties recognized that the investment was necessary for Freedom, a start-up MRE producer, to become established in the program and to enable Freedom to perform on the MRE-5 Contract. See Restitution Breach Damages above.

It was agreed that a portion of the investment amount was allowed during negotiation of the Contract as direct costs to the Contract. It was understood by both Freedom and the Government negotiating team that the balance of the investment would be carried as an asset by

Freedom to be amortized over a period of time that the parties believed to be a promising future of follow-on MRE awards. The amount requested ($1,062,138) is that portion of the total investment, although actually incurred, that was not charged to the Contract as a cost incurred. Rather, it was capitalized as an asset by Freedom and written-off upon the demise of the business.

c. Lost Profits.

$20,748,290 in lost profits is claimed. It is determined by applying Freedom's MRE 5 negotiated profit rate of 14.88% to the estimated cost base of contracts awarded to Freedom's successor/replacement MRE supplier, CINPAC, on MRE awards 7 through 12 plus the application of a profit rate of 10% on the estimated cost base of post MRE-12 MRE awards since 1991. *See* Expectation Breach Damages above.

The calculation of lost profits represents an estimate of what profits Freedom would have earned over future program awards as an established MRE supplier but for the egregious and bad faith Government actions which resulted in Freedom's removal from the IPP program and the destruction of its business. *See* Section III.B and C above.

As a consequence of CINPAC's wrongful entry into the program, the wrongful negative preaward survey finding for MRE-7 in late 1986, and the wrongful termination for default of the Freedom Contract, Freedom was excluded from the program. In its place, CINPAC received a series of follow-on MRE awards that would have been received by Freedom. Further, Freedom has demonstrated that for a period of time during performance of the MRE-5 Contract it had achieved high rate production on a profitable basis. It is reasonable to assume that this ability to operate profitably would be enhanced and sustainable on follow-on contracts. Tr. 999-1002.

d. Miscellaneous Financial Damages.

$16,611,660 is claimed for miscellaneous financial damages resulting from the Government's breaches of the Contract and the resultant financial destruction of both Freedom as a business entity and of its owner, Henry Thomas, personally, as guarantor. *See* Restitution Breach Damages above.

Freedom is also entitled to receive interest pursuant to the Contract Disputes Act on amounts which were in dispute and which were ultimately found to be due and owing. Freedom has not provided a calculation of this amount at the present time but will do so, when the disputed claim is resolved. *See* Restitution Breach Damages above.

2. Analysis of Contract Cost Overrun and Allocation.

Freedom and the PCO agreed on a total cost amount of $14,970,142 (R4, tab FT062, tab FT443) as being necessary for performance of the Contract. This amount was recognized during the 1984 negotiations as the total direct costs considered in establishing the MRE-5 Contract price. This same amount was budgeted by Freedom for completion of the Contract. It was the amount that Freedom reasonably anticipated would be necessary to complete performance of the Contract.

At the time the Contract was terminated for default in June of 1987, Freedom had delivered more than 505,000 MRE cases and was in process on the remaining 107,538. Freedom had incurred a total of $22,174,628. R4, tab FT408, tab FT413. Had termination not occurred, Freedom expected to expend an additional $1,499,489 to complete the Contract. The total

amount at completion, $23,674,117, compared with the negotiated and budgeted amount of $14,970,142, equates to a contract cost overrun of $8,703,975. **Figure 2** presents a detailed summary of the cost overrun.

Figure 3 presents an overview of the direct material cost growth experienced by Freedom. $8,193,637 was negotiated and budgeted for this element of cost. The total incurred cost for materials plus the estimate of material costs to complete the job amounted to $8,596,827. Thus, a total material overrun of $403,190.

In order to understand the basis of this overrun, Freedom compared a detailed analysis of the original negotiated priced bill of materials with the actual amounts for materials expended by Freedom. The bill of materials consisted of numerous items of contractor furnished material (CFM) incorporated into the MRE. These included various meat product patties, dessert cakes, cracker bags, accessory bags, meal bags, boxes with sleeves, etc.

Prices per unit of a material item ranged from a low of $ .02821 for accessory bags to $1.1022 for the ham and chicken loaf. Freedom compared the budgeted (negotiated) material cost with the item prices set forth in the actual purchase orders. Freedom also examined the costs for items as billed to the Government in the various progress payments requests. The result of this comparison/analysis revealed an unexplained growth in total material cost of $48,035. This cost growth appears to be independent of any act on the part of the Government. It is not being included as part of the Freedom request for equitable adjustment.

A comparison was made of actual costs per item experienced during the contemplated performance period with prices imposed by suppliers during the year long extension. There were a number of vendor price increases, significantly for meat items and beans, resulting in a material

cost increase of $355,155. These increases resulted from "out of period" purchases.. This escalation is directly attributable to Government caused delays which extended the preproduction period and the production period for more than a year. See Schedule Chart, R4, tab FT 443; tab FT444.

Brian Freck, the developer of this Quantum section, presented the analysis and findings of this material review in his unrebutted testimony. Tr. 1037-1038. The material analysis was also reviewed and verified by Jordan Fishbane, Appellant's accounting expert. Mr. Fishbane testified that he had reviewed and concurred in the cost findings of Brian Freck. Tr. 1002.

Figure 4 is an overview of the amount of production labor that Freedom had negotiated and intended to use for completion of the 620,304 MRE 5 cases. It compares that amount with labor costs actually incurred.

As part of price negotiations, Freedom and the PCO agreed that Freedom required a production labor force of 134 for 8 months, from May 1985 to December 1985. The resulting budgeted amount was $811,002. R4, tab F18, tab FT062, tab FT443. At the time the Contract was terminated, Freedom had incurred production labor costs of $2,526,746. That amount (plus a nominal $61,164 as an estimate of labor costs to complete (ETC) the remaining 107,538 in process cases) compared with the budgeted (negotiated) amount, resulted in a labor cost overrun of $1,776,908.

An analysis of the labor cost overrun indicates that the entire amount is directly linked to Government-responsible acts and omissions. These acts and omissions denied Freedom the efficient high-tech equipment planned. The loss of the equipment forced Freedom to hire far more people than otherwise necessary. Government acts and omission, causing various delays,

inefficiencies, disruptions and rework also stretched the planned production labor period from 8 to 16 months.

But for the Government's interference, Freedom would have commenced production with a fully trained and motivated workforce. In fact, in advance of any incurred contract labor, Freedom, using a training grant, had conducted a very successful pilot training program.

In his unrebutted testimony, Phillip Lewis, Freedom's technical consultant and training coordinator, stated that the pilot workforce had been trained on two units of the extended high-tech equipment components that Freedom had brought into the plant. He stated that Freedom expected to begin immediately. Instead, there was a gap of several weeks before the substitute equipment arrived. During that "down" time there was attrition, and loss of interest and motivation on the part of the workforce. Many key people were lost. A major part of the workforce had to be re-recruited and trained. Tr 1083-1084.

As a reasonable basis for recovery of the labor cost overrun portion of its claim, Freedom has allocated the total $1,776,908 overrun among a number of the various claim elements comprising the total equitable adjustment request. These various claim elements and allocations are identified in **Figure 6** and are discussed in detail below.

The labor overrun has two (2) components. The first is the cost of additional manpower that was required because more labor intensive equipment had to be used. The second component is the added cost that resulted from a production labor force that was in place for 16 vice the 8 month planned. This component of the labor cost overrun has been allocated to various claim elements on a monthly labor cost basis.

Figure 5 presents an overview of the overrun experienced in manufacturing overhead costs and general and administrative (G&A) costs of $3,925,813 and $2,629,397, respectively. Specific overhead and G&A amounts were agreed to by the parties during the negotiation of the Contract price. Since this was Freedom's only contract, the amounts were classified as direct costs to the Contract. The overruns occurred, for the most part, as a result of Government caused delays which stretched the contract period to June 22, 1987 (date of termination) from the December 31, 1985 scheduled completion date. Although this total delay and extension period was 17 ½ months, increased costs for continuing overhead and G&A expenses are only being claimed for an extended period of 16 months. Although the Contract was terminated on June 22, 1987, no costs were recorded by Freedom on its books during May and June of that year. Therefore, the cost impact of the Government caused delay and disruption was only experienced for 16 months.

Continuing overhead and G&A costs were incurred, on a consistent month to month level, while Freedom suffered major Government caused program delays. In addition, the program was extended for several months because Freedom had to perform additional labor tasks. In each instance of delay, Freedom had no way of determining the exact or even the approximate time a delay would last. Accordingly, it was unable to reduce or eliminate facilities and supporting personnel. Further, since this was Freedom's only contract, it was unable to allocate resources to any other cost objective. For those extended months during which Freedom needed additional labor resources to work with slower production equipment or to perform unnecessary rework, overhead and G&A costs continued to be incurred as an inherent component of its operating structure.

The total cost overrun for overhead and G&A has been allocated to a number of the claim elements identified in **Figure 6** and will be discussed in detail below. An amount of $313,236, although charged by Freedom as an expense to the G&A cost pool, has been deducted from the overhead and G&A cost overrun allocation in this Quantum calculation. This figure represents "additional financing" interest costs which are being presented as a separate claim element. In order to equitably allocate the overrun costs to the various claim elements which comprise the 16 months of claimed additional overhead and G&A cost, the total overrun amount of $6,555,210, less the excluded interest claim of $313,236, has been divided by 16 months to arrive at an average monthly increase in overhead and G&A costs of $390,123 per month.

3. Equitable Adjustment - Increased Costs for Constructive Changes Individual Claim Elements.

a. Suspension of progress payments, interference with suppliers and financiers, and use of unplanned equipment

b. Failure to pay for allowable incurred costs

c. Improper rejection of MRE units

d. Failure to receive Contractor Furnished Material (CFM)

e. Failure to provide Government Furnished Material (GFM)

f. Failure to make payments for completed MRE units

g. Increased costs of unreasonable financing requirements

Figure 6 presents each of the individual elements which make up the aggregate equitable adjustment claim of $8,466,039. Dollar amounts of that total are allocated to each element. This allocation of the increased contract costs to the various elements **(Figure 6)** represents a distribution of the total claimed.

a. Suspension Of Progress Payments, Interference With Suppliers And Financiers, And Use Of Unplanned Equipment (Figure 7).

The total amount of cost impact claimed for suspension of progress payments, etc. is $4,416,830. It comprises the impacts of three separate components:

(i) a 5 month delay in completion of the preproduction period;

(ii) additional manpower required by having to use less efficient and more labor intense equipment; and

(iii) a 3½ month extension of the production schedule because of slower production time attributable to less efficient equipment.

Freedom considers these components to be a part of the same claim element. They arose out of the same set of circumstances: the failure of the Government to meet its progress payment obligations early on and the breach of the Government's duty not to interfere with Freedom's suppliers and potential financiers.

(i) Five (5) Month Delay In Completion Of Preproduction.

During contract negotiations, Freedom and the PCO agreed on contract performance milestones. R4, tab FT062, tab FT443. The agreed milestones included a six (6) month preproduction period during which Freedom was to make all necessary alterations to the plant, bring in necessary equipment for production, set up the production lines, comply with sanitary requirements, conduct required training, develop an approved inspection plan, and a number of other related tasks. After completion of this period, an eight (8) month production period was to commence where production labor would be in place.

As a result of the Government's refusal to meet its financing obligations (*see* progress payment financing spreadsheet; R4, tab FT062), Freedom was unable to accomplish the scheduled preproduction tasks. Even under the circumstances - six months of initial progress payment denial coupled with the ACO's refusal to provide accurate information to suppliers and financiers concerning Government financing obligations - Freedom continued working and made important progress. The rate of expenditure and level of accomplishment, however, was considerably short of planned levels. R4, tab FT444.

After award, Freedom expeditiously contracted for the acquisition of all the necessary hi-speed modern production equipment including Koch Multivac, Doboys, and the International Paper machine. R4, tab FT086, tab FT098, tab FT093, tab FT109, tab FT425, tab FT426, tab FT427. Government-caused financing problems prevented the utilization of this equipment. After a significant and costly delay, slower and inferior equipment had to be procured. R4, tab FT132, tab FT136, tab FT139, tab FT432.

One of the critical milestone tasks associated with the preproduction period was plant renovations. These were to be performed immediately after award. The Government's financing failure, and its refusal to even confirm progress payment cash flows to vendors and financiers, caused Freedom to lose the planned renovation contractor. Only later could the work be completed with a different source. R4, tab F32.

The training of a pilot workforce on the hi-speed machines was completed early on. This, barring Government failures, would have facilitated the start of production in May of 1987. The

training, however, went to waste because of the Government's financing failure. The planned equipment was lost, the alternative equipment was delayed and a production labor force could not be reassembled for several months.

In summary, the impact of the Government-caused delay in completion of the preproduction period lasted five (5) months until October 1985 This component of the claim element has been costed at $1,950,615 which represents 5 months of delay at the average monthly overhead and G&A expenditures. **(Figure 7)** The monthly delay cost does not include any allocation of the production labor cost overrun, *i.e.*, average production labor cost per month, since the production labor force had not yet been put in place during the preproduction period.

(ii) Cost of Additional Labor.

The second component of this claim element is the cost of additional resources caused by the imposition of inferior and more labor intense production equipment. Again, the Government's financing failures were at fault. Because of those failures, Freedom was unable to use the planned and budgeted high-tech equipment arranged for. Freedom had to expend approximately $548,057 in additional production level staffing costs to maintain a workforce that averaged almost double the 134 persons negotiated.

In his unrebutted expert testimony, Martin Bernstein, industrial engineering expert, stated that he was familiar with the manufacturing process for the MRE units. He was also familiar with the planned equipment and with the equipment that actually was used. In his opinion, use of the intended equipment could have reduced assembly time by 70%. Further, the equipment actually used required additional labor hours and forced Freedom to put additional production workers on the line. Tr. 892, 896, 899, 903, 907

The claimed cost for this component of this claim element is $548,057. This represents the direct labor cost of an average of 95 additional production workers for an 8 month period.

(iii) Extension of Production Schedule.

The third component of this claim element is the extension in the production schedule. The use of inferior production equipment considerably lengthened the time required to accomplish the necessary tasks of assembly and production. Thus the planned production schedule had to be extended. Freedom estimates that an additional 3 ½ months was added to the contract period. The impact to Freedom was $1,918,158, which represents the additional cost of 3½ months of continued overhead and G&A costs plus the average monthly labor costs for this extended period. **(Figure 7)**

Phil Lewis was Freedom's technical consultant and training coordinator. In his unrebutted testimony, he stated that Freedom was forced to use considerably slower equipment. This substitute equipment had an adverse impact on food handling and assembly operation speed. Further, he noted that every employee had the same conclusion. The round tables were not efficient. Lewis testified that the high-tech equipment would have allowed the use of high speed conveyor lines. Tr. 1082-1084.

In unrebutted testimony, Martin Bernstein, industrial engineering expert, stated that the planned Doboy continuous band sealer had more heating and cooling capacity than the equipment forced on Freedom. The machines Freedom had to use ran at approximately 150 inches per minute whereas the Doboy ran at 350 inches per minute. The Doboy would have allowed the line to move twice as fast.

Mr. Bernstein noted that Freedom intended to use an International Paper machine but ended up having to use a Marq Equipment machine. Based upon his experience the Marq machine was not as sturdy and often broke down while working with the rigid boxes. This would have had a negative effect on productivity. Further, Mr. Bernstein testified that, in his opinion, use of the equipment Freedom was forced to use instead of the planned high-tech equipment required the operation to take longer. Tr 900, 901, 905.

b. Failure to pay for allowable incurred costs (Figure 8).

In several instances, primarily from July 1985 to June 1986, Liebman refused to make payments to Freedom against customary progress payment requests for reimbursement of allowable incurred costs. In one instance, Liebman arbitrarily offset a progress payment invoice by $400,000, improperly categorizing the matter as a forgiveness of rent. See Section III.A.1.j.i above. This reduction impacted Freedom's ability to perform under the Contract.

Liebman also withheld several hundred thousand dollars from progress payment requests demanding a DAR deviation before he would honor an existing advance cost agreement between the parties. Findings 189-208. In another instance, Liebman made no payment at all against a progress payment request in the amount of $807,348. Instead he denied the payment saying, incredulously, that the amounts claimed represented costs associated with starting up a new business and were not related to production. *Id.* As a result, Freedom incurred performance costs without essential, and promised, Government reimbursement so as to render performance impossible in accordance with scheduled performance milestones.

Freedom was faced with a continuing operating cash deficit. This placed Freedom in a management dilemma. Which bills to pay and which bills to hold. This constant crisis had an

adverse impact on performance. Freedom estimates that over the course of the July 1985 to June 1986 the contract was delayed a full month because of it.

To illustrate how this problem affected performance, production equipment manufacturers wrote Freedom (R4, tab FT209, tab FT216) and informed Freedom that absent payment of invoices, they would not be able to provide service and spare parts. Normal equipment breakdowns and maintenance needs escalated into unnecessary delays.

The cash flow crisis caused by the Government financing failure also prevented Freedom from receiving and setting up its critical automated lot tracking system. In a Government technical report on Freedom's production capability as of November 29. 1985 (R4, tab G26), the DCASR-NY-NAPB engineer identified the lack of the computerized inventory and lot tracking system and the impact on Freedom's ability to control the flow of material as a cause of Freedom's schedule slippage.

In unrebutted expert testimony, Martin Bernstein stated that because Freedom did not have its planned automated tracking system in place everything had to be done manually. As a result, there were numerous problems with control and tracking materials. Tr. 913.

The estimated one month delay caused by the payment problems is costed at $548,045. This is the average overhead, G&A and production labor cost of the additional month of contract performance.

c. <u>Improper Rejection of MRE Units (Figure 8)</u>.

During October and November 1985, Government inspectors (AVI) improperly rejected case lots of MREs. Freedom was forced to do unnecessary rework and experienced delays in getting completed cases accepted. In unrebutted testimony, Leon Cabes, Freedom Director of

Technical Services, stated that he developed the Plan for the inspection job during the early part of the Freedom contract. He did this in conjunction with the AVI staff and gained their approval. Tr. 2076. Mr. Cabes testified that the Plan called for a point of inspection on a moving lot basis. This means that samples would be pulled from the production line belt after each case was assembled, strapped and sleeved but before the cases were pelletized. Tr 2084, 2085. Mr. Cabes explained that the AVI deviated from the approved Plan and changed the inspection point causing delay in cases acceptance. *Id.*

Mr. Cabes also testified that the he believed that the AVI inspectors were very inexperienced. Their inexperience led to a costly mistake in judgment regarding strapping material. *Id.*

As part of the lot rejections and subsequent rework, Freedom had to open up the cases after they had been palletized. Freedom had been willing to accommodate the stationary lot inspections in order to help move things along. AVI, however, would not perform any inspections because they had erroneously judged the strapping material to be unreliable. In fact, there had been nothing wrong with the strapping material. Liebman later confirmed that fact in writing. R4, tab FT 437. When the fully strapped and capped loads were eventually opened, Freedom had to do significant rework as a result of rejections. This rework could have been avoided if inspections had been done, as agreed, on the moving lot. The corrective action involved a simple deburring operation to remove a sharp edge on a machine that was causing small tears. This could have been done quickly if detected during the moving lot. The simple correction would have eliminated most of the rejections. Tr. 2090.

Freedom estimates that this rework and delay resulted in an additional month to the contract schedule. This claim element is costed at $548,045. The amount represents the average monthly overhead, G&A and production labor cost for the extended contract period.

d. Failure to Receive Contract Furnished Material (CFM) (Figure 8).

The Government breached Mod 20 by improperly diverting materials designated for Freedom and located at Freedom's suppliers. These materials had been produced for Freedom's Contract. The Government, in order to support its repurchase contract with Rafco (R4, tab FT239, tab G-32), diverted items of CFM to Rafco. R4, tab FT239, tab G32, tab FT255. As a result, Freedom did not have critical materials needed to meet early 1986 incremental deliveries scheduled under Mod 20.

Freedom had authorized its supplier, Sterling Bakery, to "ship in place" the items it had produced for Freedom's Contract. The purpose was to assure that these items were unavailable for any other use or customer. PCO Bankoff rescinded the ship in place instructions. He then allowed Rafco to order these items directly from Sterling Bakery. Freedom was not notified. Findings 292-293.

Freedom believed these CFM items were available. It approached Sterling for its CFM it needed to meet Mod 20 delivery requirements. To its dismay, Freedom discovered that it had no CFM. *Id.*

Freedom had ramped up its production to meet the required Mod 20 schedule. Freedom was forced to halt this production because the Government had commandeered its CFM. R4, tab FT436. The Government knew that Freedom relied on its vendor materials to support Modification P00020 delivery requirements. The Government, unconscionably, had induced

Freedom to accept the schedule knowing it would pirate Freedom's CFM. A temporary production shutdown and contract delay was the inevitable result.

Mod 20 provided for the reinstatement of 114,758 improperly terminated cases. The reinstatement was contingent on delivery schedule compliance. The CFM "theft" prevented compliance.

A further delay resulted from Freedom's inability to utilize materials from its subcontractor, Star Foods. A temporary medical hold had been placed on those products involving micro holes in the pouches. Zyglo testing documents. R4, tab FT258. PCO Bankoff, in an April 1986 memo (R4, tab FT435) declared that the inclusion of Freedom in the medical hold issue constituted a constructive change.

In the testimony of Leon Cabes, Freedom's technical director, testified that Freedom was unable to use the Star Foods products. These unuseable products included pouches currently being produced by Star Foods as well as those previously produced and in Freedom's warehouse as inventory. R4, tab Tr. 2099. The problem arose because Star Foods was working extra shifts. This, in turn, was caused by additional requirements imposed on account of CINPAC's illegal entry into the program.

Mr. Cabes testified (Tr. 2103-2104) that although substitutions were authorized, Freedom's production was slowed due to different sizes of the substitutions as well as bulging and sealing problems. Mr. Cabes also testified that Freedom was required to conduct extra-contractual on-line micro hole testing. This added inspection requirement resulted in slowed production. The duration of this additional effort, according to Mr. Cabes, was 6 to 8 months. Tr. 2107-2108.

Freedom estimates that the production schedule was extended 1½ months on account of the CFM,.the medical hold and the added Zyglo testing. The impact is costed at $822,068. This represents the average monthly overhead and G&A cost plus average monthly production labor cost for 1½ months.

e. **Failure to provide Government Furnished Material (GFM) (Figure 8).**

On several occasions primarily in late 1986, the Government failed to supply required GFM. This resulted in production shutdowns, layoffs, and schedule delays.

Of particular note, the Government intentionally failed to arrange for MRE 6 configuration GFM needed to produce 114,658 cases reinstated by Mod. P00025. This Government failure prevented Freedom from meeting contractual delivery schedules. In addition, Freedom shipped only 46,260 cases towards a September 1986 requirement of 80,000 cases because of slippages and downtime caused by stock outages of GFM fruit mix and potato patties. Further, during the last week of September 1986, accessory production had to be shut down for approximately one week due to a stock outage of GFM cream. Freedom then received a shipment of 1.1M packets of cream substitute on 3 October 1986 and resumed accessory production on 6 October 1986.

By October 22, 1986, Freedom had received all the CFM needed to begin producing cases in the MRE 6 configuration. They had still not received the GFM beef slices, diced turkey, ground beef or ham slices. By letter dated October 22, 1986 (R4, tab 161), Freedom notified the Government that it was shutting down MRE 6 assembly production and laying off 146 production workers.

Liebman's report of July 25, 1986 (R4, tab F145) cites GFM as one of the problems impacting the delivery schedule. Liebman's report of October 3, 1986 (R4, tab F164) noted the accessory shutdown due to lack of GFM. The DCASMA November 3. 1986 technical report (R4, tab F178) to the ACO noted that Freedom could not perform due to the lack of GFM.

In unrebutted testimony, Martin Bernstein, industrial engineering expert, stated that a lack of GFM, or the receipt of substituted GFM, would create an inefficient operation. Meals would have to be put on the side with a lot of balancing of lines and people. Tr. 895. He further testified (Tr. 909) that the lack of a required GFM item could result in a line shutdown. GFM delay, he said, was not a one for one delay because it would take time to get people back. Tr. 914.

Philip Lewis, Freedom's technical consultant and training coordinator, testified that without the necessary GFM it was impossible to perform any work on the product. Tr. 1086. He maintained that a delay in the delivery of GFM would result in a schedule delay that was greater than the actual length of the GFM delivery delay. Tr. 1088.

Leon Cabes, Freedom's Director of Technical Services, testified that even when there were substitutions available there were inefficiency problems related to bulging and sealing. Tr. 2103-2104. Mr. Cabes testified that the Government agreed that it was its responsibility to replace damaged GFM crackers and that any damaged crackers would be removed from production and issued for troop use. Tr. 2115-2116.

Freedom estimates that the failure to receive GFM over a several month period resulted in inefficiencies, delays, and shutdowns. This failure, in the aggregate, extended the contract period

by three months. The delay was experienced during 1986, as well as into early 1987, while Freedom was ready to resume production if GFM arrived.

This element of Freedom's claim has been costed at $1,170,369 which represents the average monthly cost of overhead and G&A for three additional months of contract performance. Production labor costs have been excluded from this claim element as production labor costs ceased in late 1986. Further, other elements of Freedom's claim have provided for a full absorption of labor overrun costs. Additionally, pursuant to the release in Modification P00028, Freedom's increased costs for non-receipt of GFM fruit jellies has been excluded. See **Figure 9.**

f. Failure to Make Payments (Figure 8).

Freedom believed in, and relied on, the Government's compliance in good faith with contract payment provisions. Throughout 1986 and into 1987 the government failed to comply. The failure included non-payment of invoices or DD250s for shipped and accepted end items contract, improper imposition of a 100% liquidation rate by Liebman, effective as of October 29, 1986, and wrongful suspension of progress payments in December 1986. Additionally, Freedom was denied financing in the form of the guaranteed loan relied on when it agreed to Modification P00025.

The Government's funding failures caused delay and disruption. Freedom, in an attempt to resolve the problem, was required to expend considerable management effort to secure alternate funding and to deal with the Government. Freedom letters (R4, tab F126, tab FT276) to Liebman list the unpaid invoices and request for payment.

Liebman's own reports confirm that cash flow problems were causing delivery delays (R4, tab F175) and that the impact of finances is one of the causes of delay. R4, tab F145.

Freedom estimates that the impact of the Government's refusal to make required payments resulted in a month of delay and disruption to the Contract. This element of the Freedom claim has been costed at $548,045. The amount represents one month of the average monthly cost of overhead, G&A and production labor during the extended contract period.

g. Government Imposed Unreasonable Financing Requirements (Figure 8).

The parties agreed at contract formation (November 1984) that the Government would provide prompt financing in the form of progress payment reimbursement of 95% of incurred costs. Accordingly, Freedom projected an amount of $171,664 as working capital interest expense to cover its share of working capital financing. The detailed exhibits to Freedom's proposal and incorporated in the Contract (R4, tab FT062) reflect the agreement with respect to this financing and interest requirement.

Liebman breached this agreement. He forced Freedom to obtain an outside line of credit beyond what Freedom reasonably expected or required. As a result, Freedom incurred $484,900 in working capital interest expense. This was substantially above what the parties contemplated.

The added interest cost was included as part of the G&A incurred cost base and verified by the Defense Contract Audit Agency. R4, tab FT413. The actions of Liebman in forcing Freedom to bear an undue share of the contract financing risk is evident by the Government's financial analysis distortion known as "backwards induction." Findings 248-260. Freedom is seeking an amount of $313,236 which represents the additional working capital interest expense incurred under the Contract.

Summary of Claim for Increased Costs for Constructive Changes (Equitable Adjustment)

Freedom's claim for equitable adjustment is based on the total amount of cost overruns resulting on account of the alleged constructive changes. A number of the changes to the Contract were occurring simultaneously and had overlapping cost impacts. Accordingly, Freedom has allocated the claimable overrun total to the claim elements on a "best estimate" basis. Freedom's responsibility for cost overruns or costs associated with a release of Government liability (Modification P00028) have been excluded from the equitable adjustment cost base. **Figure 9**.

Freedom's claim for equitable adjustment, comprising the claim elements previously discussed, seeks a total contract price adjustment of **$9,686,129**. This claim, as depicted in **Figure 10**, consists of the total claimed cost overrun of $8,431,519 plus a profit at the14.88% rate negotiated and contemplated at the outset of the Contract.

A $9,686,129 equitable adjustment will establish the correct and final contract price. This price will permit Freedom to be reimbursed its total allowable incurred costs under the Contract, plus appropriate profit through a revised and final termination settlement computation.

4. Unrecovered Program Investment Costs.

Freedom seeks **$1,062,138** for expenditures made by Freedom at the outset of the Contract in order to "start up" and get ready to perform the MRE-5 Contract. The expenditures were necessary for plant alterations (leasehold improvements/building repairs) and certain equipment such as quality control equipment, office equipment, and furniture and fixtures.

During negotiations leading to the award of the contract, the parties identified those costs that would be allowable as direct costs to the contract. These costs were reflected in the manufacturing overhead/G&A spreadsheet that, as part of Freedom's proposal were incorporated in and became part of the Contract. R4, tab FT062; Exhibit 9. Specifically, the agreement provided for $187,500 for building repairs, $54,000 for quality control equipment, $80,000 for office equipment, and $75,000 for automated building management system.

Freedom and the PCO knew that an investment by Freedom well in excess of these amounts, especially for building repairs would be required. This added investment was required for Freedom to become established in the MRE program. Freedom agreed to make the investment because of the Government's promise to maintain it in the program. Only with fruition of that promise could Freedom amortize the additional start-up costs not charged to the MRE-5 Contract. Because the Government breached this promise, *i.e.*, the implied-in-fact agreement, Freedom lost its investment.

During contract performance, Freedom could not expense even the negotiated portion of the costs as agreed. Instead, it was forced to capitalize the entire amount as assets. This treatment was driven by Liebman's refusal to honor the Government's commitment to treat all allowable costs and direct costs. Freedom kept the full amount of the items in question, specifically, the building alterations and the equipment described above, in an asset account.

After termination of the Contract, Freedom removed the portion which was intended to be a direct expense to the contract and included these costs in its revised termination settlement proposal. R4, tab FT408, Other Costs, Schedule B of SF1436. These costs have been audited by the Government and recommended for acceptance in the DCAA audit report. R4, tab FT413,

pgs. 4 and 5. They have been allowed in the termination settlement between Freedom and the TCO.

The balance of the "investment" was written off as a loss by Freedom upon the demise of the business, remains unrecovered, and is claimed herein.

Figure 11 provides an overview of the asset accounts with the total amounts capitalized. Deducted from this total amount are those portions allocated to the contract and recovered under the termination settlement as costs incurred. The amounts of $651,010 and $273,553 for leasehold improvements (building repairs) and furniture, fixtures, and equipment, respectively, have been written off by Freedom as a loss owing to the Government's wrongful termination for default and the destruction of Freedom's business. Freedom's financial statements as of October 31, 1986 and June 22, 1987 (R4, tab FT439) reflect the assets and the write off. Freedom now seeks to recover the cost of these lost program investments, together with an appropriate profit applied thereon, for a total amount of $1,062,138.

5. **Lost Profits On Successive MRE Awards.**

Freedom seeks an amount of **$20,748,290 (Figure 12)** in lost profits as a consequence of the Government's actions of breach and bad faith. These actions caused a wrongful termination of the MRE-5 Contract and a breach of the implied-in-fact agreement, *i.e.*, Freedom's exclusion from the MRE program which caused the destruction of its business.

Freedom had been designated and established as an IPP producer. Inherent in this designation was that Freedom would be maintained as an ongoing producer to be kept available in times of war or national emergency. If not for the bad faith termination of the MRE 5 Contract, the wrongful inclusion of CINPAC into the program as a replacement for Freedom, and the

improper negative preaward survey of Freedom in connection with the MRE 7 award, Freedom would have remained in the program to this day and would have received the continuing stream of minimum sustaining rate contracts that CINPAC has received.

Freedom does not currently have the specific contract prices and quantities of each award to CINPAC for its MRE contracts from MRE 7 through the present. These amounts are a matter of public record. Freedom estimates the total value of the contract awards for MREs 7 through 12 to be $90,000,000 and another $100,000,000 in post-MRE-12 contract awards since 1991. Freedom's calculation of lost profits had it been permitted to remain in the program, is determined by applying its negotiated profit rate of 14.88% (R4, tab FT062) for the MRE 5 Contract to the estimated CINPAC cost base of $78,342,618 for its MREs 7 though 12 contracts. This results in a lost profit amount of $11,657,381.

For MRE awards since 1991, Freedom has applied a 10% profit rate to the estimated CINPAC cost base of $90,909,090. This results in a calculation of lost profit in the amount of $9,090,909. The 10% rate was utilized based on the Government's "Industrial Assessment for the Meals, Ready to Eat (MRE) Program." R4, tab FT393. The Government has maintained producers in this program at a profit rate of 10% since 1991. Freedom's entitlement to lost profits is presented as an equation and is depicted in **Figure 12**.

6. Miscellaneous Financial Damages.

As a result of the Government's destruction of Freedom as a business and the Government's economic stranglehold on any contract relief for the past 15 years, both Freedom, as a business, and Henry Thomas, personally as guarantor, have tremendous financial consequences. Amounts payable as loans from banks and amounts due suppliers for goods and

services under the Contract remain outstanding. However, the damages addressed here are limited to the growing financial burden of interest and penalties on certain outstanding debts plus the outstanding principal on one particular bank loan, together with the salary that Henry Thomas has been deprived of earning.

As an example, Dollar Dry Dock Saving Bank made an investment in Freedom in the early 1980s that enabled Freedom to set up the Hunts Point, Bronx, NY, facility and be positioned for entry into the MRE program. Freedom carried a $1,429,012 liability on its books as the principal amount due Dollar. R4, tab FT016d, tab FT016i. Both Freedom and the bank anticipated that repayment of that loan, as well as future loans, would be forthcoming from expected future MRE awards. Freedom and its principal, Henry Thomas, need to repay that loan principle from proceeds awarded from the Board in order to clear its record.

During MRE-5 Contract performance, Freedom obtained financing from Bankers Leasing Association by assigning accounts receivable. However, the flow of progress payments never proved to be sufficient to cover operating cash needs. As Government caused contract losses deepened, the investment from Bankers, in the form of unpaid loans grew to $3.5 million. That amount plus interest remains due and payable today.

Additionally, Freedom was unable to pay all expenses as they were incurred under the contract because of Government withheld progress payments and mounting increased costs caused by Government acts and omissions. When the contract was terminated for default, Freedom had accounts payable of approximately $3.3 million, including $1.4 million owing to Freedom's landlord, Pilot Realty, plus varying amounts due numerous vendors. In addition, Freedom had an outstanding liability of $500,000 for unpaid taxes plus interest and penalties.

These payables have been well documented and analyzed. These amounts are still due and owing and many carry significant interest and penalties.

The DCAA audit report of the termination settlement proposal reviewed the $3.3 million accounts payable. R4, tab FT413. The recent settlement negotiations with the TCO have fully addressed the matter of the $3.3 million accounts payable plus the $500,000 in unpaid taxes. As part of the negotiations, Freedom supplied current documentation supporting the payables for the large dollar items together with documentation which attested to the running interest and penalties. However, only the principal amount of the outstanding balances was proposed by Freedom as part of the termination proposal and only that principal amount was confirmed in the DCAA audit report (*id.*) as part of the cost incurred under the contract. No provision was made in that settlement to provide Freedom with any relief for the interest and penalties accruing on the payables even though the growing debt is unquestionably attributable to the Government's wrongful actions and the intervening 15 year period. During the negotiation of the termination settlement, the parties recognized that relief in the form of reimbursement of interest and penalties costs would have to be sought from the Board. As shown in **Figure** 13, Freedom calculates its request for reimbursement for financial damages resulting from the breach of the MRE-5 contact and/or the implied-in-fact agreement as follows:

Dollar Dry Dock (now Emigrant Savings) $1,429,012

Loan Principal to be Repaid	=	$ 1,429,012

Bankers Leasing Association $3.5M

10% per annum X 14 years	=	$ 4,900,000

Pilot Realty $1,434,069

24% Default Interest (G-22/FT161) X 15 years	=	$ 5,162,648
Miscellaneous Vendors, Taxes $2.4M		
10% X 13 years	=	$ 3,120,000
Last Salary, Henry Thomas		
16 years x $125,000.	=	$ 2,000,000
Total		**$16,611,660**

7. **Lost Profits on MRE-5.**

Additionally, as a result of the Government's breaches of the MRE-5 Contract, Freedom is entitled to receive the profit that it would have earned on the reinstated 114,758 MRE cases that it never had the opportunity to deliver. To the extent that Freedom had already performed work and incurred costs against this in-process portion of the Contract, appropriate profit has already been included by Freedom in its termination settlement proposal and presented to the Termination Contracting Officer.

The current request for equitable adjustment before the Board, in conjunction with that proposal, would permit recovery of that portion of profit applicable to incurred costs for the 114,758 cases. In addition to that profit and not included in the amounts previously requested, as described above and as depicted in the attached Figures, Freedom is entitled to and requests those lost profits on the protion of the 114,758 cases that it had not yet performed work or incurred costs against. This MRE-5 breach remedy is calculated by applying the contract negotiated profit rate of 14.88% to the noegotiated and agreed to cost estimate-to-complete of $1,499,489 and equates to lost profits of $223,124.

8. Prompt Payment Interest For Payment Delinquency.

Additionally, and again not included in the amounts previously requested, as described above and in the attached Figures, Freedom requests that it be paid interest to which it is entitled under the Prompt Payment Act because of late and/or non-payment of acceptable invoices, *i.e.*, progress payments and DD250s. The submission of these invoices and the record of their payments and the extent of the delays are shown under R4, tab FT396. Freedom understands that the Government payment/finance office will automatically compute the amounts due and make the payments, upon appropriate direction, in this case, an award of entitlement by the Board.

IV. CONCLUSION

More than 15 years ago, a minority owned company called Freedom Industries set out to partake of the American Dream. Not only did it strive to enter the mainstream American economy, it also had dreams of providing badly needed jobs in its own community. Following their dream, Freedom Industries contracted to provide sustenance for the American service men and women.

Instead of the American dream, Freedom Industries found Armaggaedon. Its initial success provoked jealousy and racial bias among many people it relied on for cooperation. These people, United States Government contracting officials, purposely and with malice of forethought destroyed Freedom Industries.

Freedom respectfully requests the Board to redress the damage done. Freedom requests that the Board find entitlement both under the Contract and for breach of the Contract, and award

the damages as set forth above. Freedom also requests that the Board find entitlement to the appropriate amount of Contract Disputes Act interest, professional fees under the Equal Access to Justice Act and any other relief that the Board finds appropriate.

Respectfully submitted,

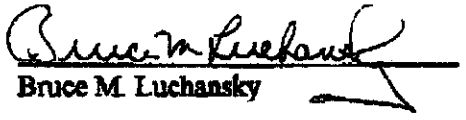
Norman A. Steiger, Esquire
Goldberg & Connolly
66 North Village Avenue
Rockville Centre
New York, NY 11570

Bruce M. Luchansky
Kollman & Sheehan, P.A.
Sun Life Building
20 S. Charles Street, 8th Floor
Baltimore, MD 21201
(410) 727-4300

Counsel for Appellant

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this 8th day of March, 2001 a copy of the foregoing Appellant's Corrected Post-Hearing Brief was sent by overnight delivery, postage pre-paid, to Kathleen D. Hallam, Esquire, Chief Trial Attorney, Defense Supply Center, Philadelphia, (DSCP-G), 700 Robbins Avenue, Philadelphia, Pennsylvania 19111, attorney for the Government.



Bruce M. Luchansky