DEFENSE LOGISTICS AGENCY
DEFENSE SUPPLY CENTER PHILADELPHIA
700 ROBBINS AVENUE
PHILADELPHIA, PENNSYLVANIA 19111-5092

IN REPLY
REFER TO DSCP-GA (Hallam K. D. /215-737-2647)

June 11, 2001

Edward. S. Adamkewicz
Recorder
Armed Services Board of Contract Appeals
Six Skyline Place, Seventh Floor
5109 Leesburg Pike
Falls Church, VA 22041

RE: ASBCA Nos.43965 & 52438
Appeals of Freedom, NY.
Under Contract No. DLA13H-85-C-0591

Dear Mr. Adamkewicz:

Enclosed, for filing in the above referenced appeals, is the Government's Response To Appellant's Post hearing Brief. Thank you for your cooperation in this matter.

Sincerely,

Kathleen D. Hallam,
Chief Trial Attorney

Encls

cc w/encl

Henry Thomas
President
Freedom NY
420 E. Martin Luther King Blvd. Suite 100
Mt. Vernon, NY 10550

BEFORE THE
ARMED SERVICES BOARD OF CONTRACT APPEALS
Falls Church, Virginia 22332 – 0700

Appeals of	:	
	:	
FREEDOM NY, INC.	:	ASBCA Nos. 43965 & 52438
	:	
Under Contract Number DLA13H-85-C-0591	:	

GOVERNMENT'S RESPONSE TO APPELLANT'S POST HEARING BRIEF

Dated June 11, 2001

KATHLEEN D. HALLAM
Chief Trial Attorney

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Dated June 11, 2001

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Chief Trial Attorney

STATEMENT OF THE CASE

This case arises from Appellant's $55 million breach of contract and equitable adjustment claim under an MRE assembly contract. Among other things, Appellant alleges that the Government (i) failed to properly administer progress payments, (ii) failed to cooperate, (iii) failed to provide timely GFM, (iv) failed to compensate Appellant for certain contract changes and/or constructive changes, (v) improperly coerced Appellant into signing certain modifications which waived or unjustly compromised Appellant's claims, and (vi) failed to honor an alleged "side agreement" in which the Government would provide Appellant with financial and technical assistance, as well as, future MRE and Section 8(a) contracts.

GOVERNMENT'S PROPOSED FINDINGS OF FACT

The MRE V Program

1. Meal, Ready-To-Eat, Individual, ["MRE"] Rations and Meal, Flight Feeding, Individual, ["MFF"], Rations have been determined to be essential to national defense and therefore are procured only from those companies that have negotiated Industrial Preparedness Agreements with Defense Personnel Support Center, ["DPSC"]. (R 4, tab 4, p. 1, para. I(C)); R4, tab 2, p. 78, Section M-1(A)[1]; Joint Stipulation #1).

[1]. The "M" documents were submitted on behalf of Appellant by the law firm of Maupin Taylor & Ellis during the original litigation of ASBCA Nos.35671 and 43965. The "M" documents include tabs M 1 -M 75.

2. Participation in the Industrial Preparedness Program is established through the use of an Industrial Preparedness Agreement, DD Form 1519. (See for example F-6 which is FI's agreement relative to retort entrees). Said agreements are effective for a limited duration of time. (See F-6). Nothing in the agreement obligates the Government or the producer to enter into a new agreement after a particular agreement has expired. (F-6). To the contrary, the Agreement specifically states that "the signatures hereon in no way bind the named firm(s) nor the Government in any contractual relationship, nor is acceptance to be construed as an agreement by industry to maintain production capability as indicated herein." (F-6, p. 1). Moreover, the Agreement does not guarantee that any given producer will be awarded a contract for the items covered by its Industrial Preparedness Agreement, even when there are outstanding requirements for the items. (F-6). In this regard, the Agreement states: "nor is the Government obligated to convert production planning schedules to contracts, to contract with the named firm if procurement of the items specified herein is required, or ..." (F-6, p. 1).

3. Four MRE procurements have been undertaken by early 1984. A Determination and Findings, signed by the Acting Under Secretary of Defense, James P. Wade, Jr., was issued on February 7, 1984 and authorized the fifth MRE procurement ["MRE 5"] to be negotiated with the three then-current planned producers for assembly: Right Away Foods

Corporation, ["RAFCO"], Southern Packaging & Storage Company ["SOPACKO"], and Freedom Industries, Appellant's predecessor. (R4, tab 4, p. 1, para. 1(C); Joint Stipulation # 2).

4. Accordingly, on February 15, 1984, DPSC issued Solicitation Number DLA13H-84-R-8257, ["solicitation 8257"] to So-Pak-Co, RAFCO, and Freedom Industries. (R4, tab 4, p. 1, para. I (D); Joint Stipulation # 6). Solicitation 8257 sought offers on the assembly and delivery of 3,101,520 MREs including MFFs. (R4, tab 4, p. 1, paras. I(B) and II(A)(1); Joint Stipulation # 6). The solicitation anticipated the award of three contracts - one for 45% of the requirement, one for 35% of the requirement and one for 20% of the requirement. (R4, tab 4, p. 2, para. II(A)(1)(c)); R4, tab 2, p. 79, Section M-1(B); Joint Stipulation # 6).

5. Solicitation 8257 and the resultant contracts required contractors to assemble the rations in cases containing twelve menu bags. (R4, tab 2, p. 28; tab 10, p. 2). Each menu bag was to contain a meat entree, crackers and an accessory packet. (R4, tab 2, p. 28; tab 10, p. 2: Joint Stipulation # 7). The MRE 5 program provided for the following twelve menus:

Menu 1 - Pork Patty, Accessory Packet D
Menu 2 Ham and Chicken Loaf, Accessory Packet A
Menu 3 - Beef Patty, Accessory Packet B
Menu 4 - Beef Slices, Accessory Packet C
Menu 5 - Beef Stew, Accessory Packet A
Menu 6 - Frankfurters, Accessory Packet E
Menu 7 - Turkey diced, Accessory Packet A
Menu 8 - Beef diced, Accessory Packet A

Menu 9 - Chicken ala king, Accessory Packet A
Menu 10 Meatballs, Accessory Packet A
Menu 11 Ham Slices, Accessory Packet A
Menu 12 Ground Beef, Accessory Packet C

(See R4, tab 2, p. 28; Joint Stipulation # 7). MREs were to be assembled in cases containing one each of -menus 1 through 12. (R4, tab 2, p. 28; tab 10, p. 2).

6. The MRE V procurement required the Government to provide certain Government furnished material, ["GFM"], including the following meat entrees: beef stew, turkey diced, beef diced, ham slices, chicken ala king frankfurters beef slices, and ground beef. (R4, tab 2, p. 57, Section H-5 (c); Joint Stipulation # 7). The assembly contractors were required to provide the other four meat entrees - ham & chicken loaf, meatballs, beef patties and pork patties as contractor furnished material, ["CFM"]. (R4, tab 2, p. 10; Joint Stipulation # 7).

7. Solicitation 8257 incorporated, by reference, Form 3595, DPSC Master Solicitation for Nonperishable Subsistence, Jun 83. (R4, tab 2, p. 85).

8. As issued the solicitation provided for a limitation on progress payments. (R4, tab 2, p. 66, DPSC Clause L-4; Joint Stipulation # 10). Specifically-I the -solicitation -provided:

> Prior to the receipt of the respective CFM First Article, a ceiling of 25% of the dollar value of that item or subcontract of CFM, as delineated in line items 000201 thru 000220 of the schedule, is established for the purposes of progress payments. After acceptance of the First Article, the progress payment ceiling is increased to a maximum of 50% of the total item or subcontract dollar value whichever applies. Requests for increases beyond this 50% ceiling rate must be accompanied by a cash flow analysis detailing the necessity of the increase by showing the impact of progress payments on operations over and above the impact on profit. No other costs or increase in the progress payment rate will be allowed unless written approval is received from the PCO. in addition, a total progress payment ceiling for the entire contract is established at $9,000,000 or 50% of the contract value whichever is lesser. ... The progress payments shall be for only those costs that are determined by the Defense Contract Administration office as reasonable, allowable to the contract, and consultant with sound and generally accepted accounting principles and practices.

(Emphasis Added) (R4, tab 2, p. 66, Clause 1-4; Joint Stipulation # 10).

Freedom Industries' Offer And Price Negotiations

9. Freedom industries ["FI"] submitted its initial offer of $25.376 per case on April 11, 1984. (R4, tab 4, p. 2, para. II(A)(2), tab 2; Joint Stipulation # 12). FI's offered price of $25.376 per case was 12.63% higher than RAFCO's low offer. (R4, tab 4, p. 4. para. II(C)(1)(a)). Due to the large price differential and to the fact that FI had not previously performed an assembly contract, an audit of FI's offer was conducted by Defense Contract Audit Agency, ["DCAA"). (R4, tab 4, p. 4, para. (II)(C)(1)(a)). Prior to the completion of the audit, FI changed its place of performance, which facilitated a new audit. (R4, tab 9, p. 3, para. B).

10. A preaward survey was also conducted. (R4, tab 1). FI initially received a negative recommendation in the financial area. (R4, tab 1, p. 28; Joint Stipulation # 14). The negative recommendation was based on FI's lack of financial support. (R4, tab 1, p. 26-28; Joint Stipulation # 14). FI's banker, Dollar Dry Dock Savings Bank ["DDD"], advised the Government, on June 6, 1984, that any commitment letter from the bank would be so qualified that it would be meaningless. (R4, tab 1, p. 28; Joint Stipulation # 14). FI had submitted a number of letters of commitment which were not acceptable because they did not contain the necessary firm financial commitment. (See G-8).

11. Best and final offers were closed on August 2, 1984 with FI offering the following alternative prices:

a) $34.81 + EPA
b) $31.285 + EPA + $2,187,000
c) $33.282 + EPA + follow on contract
d) $29.757 + EPA + $2,187,000 + follow on contract

(R4, tab 9, p. 2).

12. On August 9, 1984, FI obtained a letter of commitment from DDD which provided for a line of credit up to $7,244,000. (R4, tab 1, p. 38, tab 5). FI could not perform the contract without a tremendous infusion of equity and/or debt financing and to justify a complete award recommendation, the DCASR Financial Analyst relied upon August 9, 1984 commitment letter from DDD. (R4, tab 1, p. 42-43, tab 25, para. a).

At first, the PCO was concerned about the letter because it was conditioned on FI receiving an award of a specific dollar value. (G-71, p. 2). However, the PCO's reservations about the letter were set aside after the preaward survey monitor indicated in his findings that the letter was sound. (G-71, p. 4).

13. On August 10, 1984, FI obtained another letter of commitment from DDD which set forth the following qualification:

> It is contemplated that any credit facilities extended will be done in conjunction with the various governmental guaranty programs available to disadvantaged small business companies.

(R4, tab 6). The August 10, 1984 makes no reference at all to DDD's August 9, 1984 commitment letter, (R4, tab 6), and was not presented to the Government prior to award. (Tr. 1161). Had the Government negotiation team been aware of the letter, it would have impacted on its ability to award the contract. (Tr. 1161).

14. On September 13, 1984, Henry Thomas, in his capacity as President of H. T. Food Products, ["HT Foods"], advised FI's Corporate Secretary, Jacene Thomas that:

> To date, Freedom's expected financial support from Dollar Dry Dock Savings Bank has been futile. Dollar has provided no funds to meet Freedom's obligations over the past ten months or so, despite the many appeals for financial help.

> H.T. Food Products, Inc. cannot depend on Dollar to standby Freedom to provide the necessary funds to meet rental payments.

(R4, tab 8).

15. Mr. Thomas, who was also the President of FI, had recognized the futility of obtaining financing from DDD at least as early as April 4, 1984 when FI entered into an assignment with H. T. Foods. (G-5). The April 1984 agreement of assignment specifically states that DDD "has, in more recent times, failed, neglected and/or refused to honor its underwriting obligations and failed, neglected or refused to honor letters of credit to certain creditors ..." (G-5, p. 2). Mr. Thomas further realized that DDD's failure to provide financing placed FI in the position where it was unable to retain or acquire credit, plant space, equipment and other materials and resources to perform the pending MRE contract. (G-5, p. 2). Hence, Mr. Thomas attempted to obtain credit through H. T. Foods which, unlike FI, was not heavily indebted. (G-5).

16. On October 30, 1984, preliminary discussions were conducted between FI and the Government. (R4, tab 9, para. C). During the discussions, the areas of FI's proposal in which there was a significant difference between the Government's position and FI's position were discussed. (R4, tab 9, p. 31 para. C). After presenting these differences, the Government requested that FI re-examine its proposal and be

prepared to negotiate during the week of November 5 through 9, 1984. (R4, tab 9, p. 3, para. C).

17. On November 5, 1984, the Government obtained a copy of the DCAS Pricing Analysis and the DCAA Audit, (R4, tab 9, p. 3 para. C), and negotiations resumed on November 6, 1984. (R4, tab 9, p. 6). At no time during negotiations, did the Government have any intention to set FI up in business by financing 100% of its total expenses for the contract. (G-71, p. 3). This point was conveyed to Mr. Thomas through out the negotiation. (G-71, p. 3, 6). The Government and FI went through FI's proposal line by line and Mr. Thomas was told where the Government could and could not help FI (G-71, p. 3, 6). Each line item was the subject of proposals by FI and counterproposals by the Government. (G-71, p. 3). In many instances, FI would come back with a counterproposal that would recognize that only a portion of its costs would be paid including building repairs, maintenance and other costs. (G-71, p. 3). In instances where the Government gave FI less than the amount it proposed, the PCO asked Mr. Thomas how FI was going to pay for the difference, Mr. Thomas explained that he did not see it as a problem and that he would "eat" the difference. (G-71, p. 3).

18. As a result of the negotiations, agreements were reached on the allowable costs for materials, (R4, tab 9, p. 7), direct labor, (R4, tab 9, p.

7-8), manufacturing overhead, (R4, tab 9, p. 8), depreciation, (R4, tab 9, p. 8), packaging materials, (R4, tab 9, p. 8), G & A, (R4, tab 9, p. 9), and profit. (R4, tab 9, p. 9). In addition to the allowance for depreciation, 100% of the costs of certain equipment was allowed to be cover by the contract price. (Joint Stipulation # 21). There was no agreement that the cost of this equipment could be recovered through progress payments. (Tr. 1160, 1480). The subject of progress payments wasn't really considered in the main negotiations as an important point, and the Government never considered requesting "unusual" progress payments under the contract. (G-71, p. 1).

19. FI and the Government signed a Memorandum of Understanding, ["MOU"] on November 6, 1984. (F 17[2]; Joint Stipulation # 21). The MOU served to document the costs that were negotiated for each element. (Joint Stipulation # 21). The MOU does not relate to progress payments. (F 17). During the negotiations, there was no agreement that the Government would apply an 82.6% liquidation rate. (R4, tab 12; Tr. 1157; F-6, p. 1).

20. After the negotiations, the PCO prepared a Price Negotiation Memorandum And Price Analysis which sets forth all the areas that were discussed during the negotiations. (R4, tab 9). The document does not

[2] The "F" documents were submitted during the original litigation of ASBCA Nos. 35671 and 43965 and include F 1 - F 232.

evidence any discussion relative to costs which may or may not be recovered through progress payments or any discussion concerning an alterative liquidation rate for progress payments. (R4, tab 9).

21. The Government never led FI to believe that it would be possible to perform the contract without outside financing. (Tr. 1155-1156). To the contrary, the Government's concern that FI have outside financing was no secret. FI initially received a negative preaward survey based on its lack of financial capacity. (R4, tab 1, p. 28). FI knew full well that the award of the instant contract was based on it obtaining outside financing. (R4, tab 1, p. 27). As there was never any agreement or understanding on the part of the Government that the contract price would cover all costs associated with FI's start up, (Tr. 1155; G-71, p. 3), the Government required FI to demonstrate that it did have such financing. (R4, tab 1, p. 26-28).

The Contract

22 Contract Number DLA13H-85-C-0591, ["contract 0591" or "the contract"], was awarded to FI on November 15, 1984 for a unit price of $27.725 per case and a total contract price of $17,197,928.00. (R4, tab 10; Joint Stipulation # 25). Of this amount, $14,970,140 represented FI's negotiated costs. (F-17). At the time of award, the Government believed that FI had sufficient outside financing, as demonstrated by the August 9,

1984 a letter of commitment from DDD which provided for a line of credit up to $7,244,000. (R4, tab 1, p. 38, tab 5; R4, tab 1, p. 42-43, tab 25, para. a; G-71, p. 4; Tr. 1156).

23. The contract required FI to assemble 620,304 cases of MREs in accordance with the following schedule:

100,000 by Jul 2-31, 1985
100,000 by Aug 1-31, 1985
100,000 by Sep 3-28, 1985
100,000 by Oct 1-31, 1985
100,000 by Nov 1-30, 1985
120,304 by Dec 1-31, 1985

(R4, tab 10, p. 4; Joint Stipulation # 25). The contract set forth schedules for the delivery of GFM in monthly increments beginning in November 1984. (R4, tab 2, p-.60, Section H-5 (j)).

24 FI was required to forward to the PCO completed Material Inspection and Receiving Reports for all shipments of GFM within seven calendar days of receipt of shipments. (R4, tab 2, p. 63, Section H-5 (p)). Failure to forward this documentation as stipulated would result in the finding by the PCO that the assembler will be the cause of all delays in the assembly operations by reason of insufficient GFM, and is therefore liable for all resultant costs. (R4, tab 2, p. 63, Section H-5 (p)).

25 FI was also required to immediately notify the PCO of the failure of any components to be delivered in accordance with the GFM delivery schedule. (R4, tab 2, p. 60, Section H-5 (j)). Additionally, FI was required to notify the PCO "no less than five (5) working days in advance of any component shortage," and stipulated that "[i]f the Contractor fails to provide [such] notice ... resulting assembly delays damages would not be accessible (sic) against the Government." (R4, tab 2, p. 59, Section H-5 (h)). Notwithstanding the GFM schedules set forth in the contract, the Government was not liable for assembly delays caused by delinquent components if the components were delivered before the first day of the corresponding final delivery assembly period. (R4, tab 2, p. 60, Section H-5 (j)).

26 The Government reserved the right to substitute any of the GFM candies, spreads, fruits or meat entrees without compensation to FI, as long as, the substituted items were of substantially the same size as the components for which they were substituted. (R4, tab 2, p. 59, Section H-5 (h)).

27 Section H of the contract required FI to store and safeguard all property, (R4, tab 2, p. 61, Section H, para. k), to segregate useful product from nonuseful product, (R4, tab 2, p. 62, Section H, para. o), and to use, prepare for shipment or dispose of, as instructed, all Government property

for up to 90 days after completion of the contract. (R4, tab 2, p. 61, Section H, para. 1). Section L of the contract required FI to:

> (1) ... establish a system, either manual or mechanized which will assure adequate control for all Government Property provided under this contract, The system shall assure that records created and maintained provide the true physical and financial accounting of Government Property, contract items shipped into the contractor's plant by other contractors, property in the possession of subcontractors, assembly contractor acquired material converted to Government Property under the terms of this contract, and property furnished by the Government to use by the contractor under the terms of this contract. The property control system for the Government Property shall comply with the requirements of DAR Appendix B, "Control of Government Property in Possession of Contractors", dated 1 July 1976.

(R4, tab 2, p. 70).

28. The contract incorporated, by reference, standard Defense Acquisition Regulation, ["DAR"] Clause 7-104.35(b), entitled "Progress Payments for Small Business Concerns, 1982 Sept". (R4, tab 2, p. 81, G-2; Joint Stipulation # 9). The clause provides for a progress payment rate of 95% and a liquidation rate of 95%. (G-2; Joint Stipulation # 9). Clause 7-104.35(b) states in part:

> The Contractor's total costs ... shall not include ... (iii) costs ordinarily capitalized and subject to depreciation or amortization except for the properly depreciated or amortized portion of such costs.

(G-2; Joint Stipulation # 9). The clause further states:

> The Contracting Officer may reduce or suspend progress payments, or liquidate them at a higher rate ... whenever he

> finds upon substantial evidence that the Contractor (i) has failed to comply with any material requirement of this contract, (ii) has so failed to make progress, or is in such unsatisfactory financial condition, as to endanger performance of this contract, (iii) has allocated inventory to this contract substantially exceeding reasonable requirements, (vi) is delinquent in payment of the costs of performance of this contract in the ordinary course of business, (v) has so failed to make progress that the unliquidated progress payments exceed the fair value of the work accomplished or the undelivered portion of this contract, or (vi) is realizing less profit than the established profit ...

(G-2; Joint Stipulation # 9).

29. The contract amended the solicitation's limitation on progress payments as follows:

> Clause L-4, page 66 of 96 of Solicitation DLA13H-84-R8257; the limitation on Progress Payments shall increase by $2,000,000 after the first delivery increment (100,000 cases) has been completed. This limitation shall increase by another $2,000,000 after the second delivery increment (100,000 cases) has been completed.

(R4, tab 10, p. 7; Joint Stipulation # 26). The L clause was one of a series of local clauses developed for the ration program and its use was standard for ration contracts. (Tr. 1150).

30. The contract provided for inspection and acceptance and origin by the Army Veterinary Inspectors ["AVI"]. (R4, tab 10, p. 4). The AVIs were Government employees assigned to FIs facility to inspect the product on behalf of the Government, and as such basically performed verification

inspection. (Tr. 1332). The AVIs did not work for FI, and did not have any obligation to perform quality assurance for FI's benefit. (Tr. Tr. 1332). FI was, at all times, solely reasonable for the quality assurance of the items it produced. (Tr. 1332; see also R4, tab 2, p. 97, para. 5(d)).

31. The specific examination criteria (tests, defects, etc) are set forth in the various end item specifications identified in Section C and the packaging specifications identified in Section D of the contract's underlying solicitation. (R4, tab 2, p. 12-28). Additional inspection criteria are set for in Section E of the solicitation. (R4, tab 2, p. 29). In particular, the procedure FI followed in performing its inspections was to conform to the requirements set forth in DPSC Manual 4155.5 and Subsistence Contractor Inspection Procedures Manual. (R4, tab 2, p. 29). The contractor was also required to develop a Contractor Inspection System ["CIS"]. (R4, tab 2, p. 29). FI's CIS was developed by Leon Cabes, FI's Director of Technical Services. (Tr. 2074). A CIS is simply a document that indicates how a contractor intends to comply with the various quality assurance requirements of the contract; in FI's case, the CIS was a flow diagram that let FI's people visually see what testing had to be done on each component. (Tr. 2130). The CIS, as the name implies, is only applicable to the contractor's inspection; it did not bind the Government inspectors, nor did it trump the quality assurance requirements set forth in the specifications. FI used its CIS as a training tool. (Tr. 2130-31).

32. The contract provided that each shipment of GFM was to be examined for count, condition and identity. (R4, tab 2, p. 31). The examination for condition was to be performed in accordance with the applicable tables set forth in the specifications. (R4, tab 2, p. 32-37). In each instance, FI was required to perform exclusively visual examination. (R4, tab 2, p. 32-37). None of the tables requires any physical testing (such as burst strength or tinsel strength), or chemical testing (such as testing for bacteria). (R4, tab 2, p. 32-37). The contract did not require FI to perform any receipt inspection on CFM, but encouraged FI to do a count, condition and identity examination of CFM. (R4, tab 2, p. 39).

The Lease For The Bronxdale Facility

33. Prior to the award of the subject contract, FI had relocated its facilities. (See R4, tab 9, p.3, para. B). FI's "new" facility (the Bronxdale facility) was leased from Richard Penzer of Penco Inc., through Appellant, H. T. Food Products, Inc. ["H. T Foods"]. (See G-18, p. 9-14). According to the terms of the lease, H.T Foods had the right to sublet the premises to FI. (G-18, p. 11, para. 44). (G-18, p. 14). At the time the lease was signed (September 12, 1984), the second floor of the premises was occupied by Southland Corporation. (G-18, p. 12, para. 48).

34. The lease provided for an annual rent of $1,074,000 ($89,500 per month) for the first year. The lease provided that as soon as HT Foods provided one month's rent and the security deposit, Mr. Penzer would give Southland notice to vacate the premises. (G-18, p. 12, para. 48). The lease further provided that HT Foods was not obligated to pay any real estate taxes for the premises until Southland vacated. (G-18, p. 12, para. 48).

35. Shortly after contract award, on November 28, 1984, Henry Thomas, the President of FI and the owner of HT Foods entered into a second agreement with Richard Penzer. (See G-12). Pursuant to that bilateral agreement, Mr. Thomas acknowledged that the lease for the Bronxdale facility had not become effective and that HT Foods no right to sublease or occupy the premises. (G-12).

36. According to the sworn Affidavit of Henry Thomas[3], Mr. Penzer approached him at the end of November 1984 and told him that he had the opportunity to sell the building and requested that H.T. Foods agree to give up its option to buy the building. (G-18, p. 22, para. 19). In return, Mr. Penzer agreed to reimburse H.T. Foods $400,000 from any rental payments that it made in the future after the Government stated making progress payments. (G-18, p. 23, para. 21). Mr. Thomas and Mr. Penzer

[3] The Affidavit, dated July 11, 1985, was submitted to the Supreme Court of the State of New York in connection with a civil action captioned Richard Penzer v. H.T. Food Products, Inc.

anticipated that progress payments would commence in March 1985 "based upon [a] guesstimate of the various approvals that were still required by sub-agencies of the Department of Defense after the contract was issued, including the qualification of the building." (G-18, p. 23, para. 21).

37. Mr. Thomas and Mr. Penzer agreed to implement this change by canceling the September 12, 1994 lease and preparing a new lease. (G-18, p. 24, para. 24). After the cancellation, until a new lease was entered into by the parties, H.T. Foods agreed that its use of the 400,000 square foot building was restricted to 800 square feet. (G-18, p. 24, para. 24). In return, H.T. Foods was only responsible to pay for out-of-pocket costs for security, Con Edison and limited use and occupancy for any time that H.T. Foods was actually in the building. (G-18, p. 24, para. 24).

38. In April 1985, Mr. Thomas paid Mr. Penzer a total of $100,000 to cover all these miscellaneous costs for the period of November 1984 to April 1985. (G-18, p. 29, para. 36). H.T. Foods had absolutely no obligation to pay full rent as provided for under the rent schedule of the September 1984 agreement, until H.T. Foods actually took over the entire building. (G-18, p. 24, para. 24). In the instant case, H.T. Foods did not gain full access to the building until April 8, 1985. (G-18, p. 26, para. 27). Hence, from November 28, 1984 until April 8, 1985 while the oral

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(G-18, p. 17- 35).

agreement was in effect, H.T. Foods had no right to use the facility as a manufacturing plant and had no obligation to pay the $89,000 per month rent or the $16,000 per month tax escrow. (G-18, p. 24, para. 24, p. 26, para 27).

39. On or about April 8, 1995, Mr. Penzer sold the building to Pilot Realty Co. (G18, p. 28, para. 34). In order to facilitate Pilot's mortgage application, Mr. Penzer and H.T. Foods executed a new lease on or about March 16, 1985. (G-18, p. 27-29, paras. 30, 31, 34).

40. FI/HT Foods made its first rental payment in April 1985. (G-18, p. 29, para. 35). The rental payment covered the month of April 1985. (G-18, p. 29, para. 35). Other than the April 1985 lump sum payment of $100,000 for incidentals, no rent or tax payments were made for November 1984, December 1984, January 1985, February 1985, or March 1995. (G-18, para. 35).

<u>The February 6 1985 Suspension of Progress Payments</u>

41. On or about November 29, 1984, FI submitted its first request for progress payments ["PP"]. (R4, tab 16, p. 1). The request, dated November 15, 1984, sought $100,310 which amount reflected 95% of FI's alleged incurred costs of $105,589. (F 232, subtab "FI's PP #1", unnumbered p. 5-6). The incurred costs included rent in the amount of

$89,500 and real estate taxes in the amount of $16,089. (F 232, subtab "FI's PP #1", unnumbered p. 6). The PP request was signed by Mr. Thomas. (F 232, subtab "FI's PP #1", unnumbered p. 5).

42. At the time the request was dated, FI via H.T. Foods was functioning under the terms of the original September 1994 lease. Pursuant to the terms of that lease, H.T. Foods did not have any obligation to pay real estate taxes until Southland vacated the premises, which would occur sometime after H.T Foods began paying rent. (G-18, p. 26, para. 28). Southland did not vacate the premises until April 1985 at which point, H.T. Foods had full access to the building. (G-18, p. 24, para. 24). When Mr. Thomas signed FI's first PP request, dated November 15, 1984, Mr. Thomas knew neither H.T. Foods, nor FI had any obligation to pay real estate taxes. (G-18, p. 24, para. 24, p. 26, para. 27). Hence, FI, in the form of Henry Thomas, began defrauding the federal Government on day one of the contract.

43. On or about December 7, 1984, FI revised and resubmitted its first request for PPs. (R4, tab 21, subtab b). The resubmittal sought $252,150 which reflected 95% of the alleged incurred costs of $265,421. (R4, tab 21, subtab b, p. 1). The PP request was signed by Henry Thomas. (R4, tab 21, subtab b, p. 1). The incurred costs claimed under the resubmitted request included rent for the months of November ($89,500) and

December ($89,500) and real estate tax for the months of November ($16,089) and December ($89,500). (R4, tab 21, subtab b, p. 2).

44. At the time, Henry Thomas signed the resubmitted request, H.T. Foods' lease had been set aside by mutual agreement of the parties. (G-12, G-18, para. 24). Pursuant to the oral agreement of the parties neither H.T. Foods nor FI had any rental obligation whatsoever until a new lease was executed. (G-18, p. 24, para. 24). A new lease had not been executed as of the date of the submittal, nor had FI or H.T. Foods taken possession of the entire building. (G-18, p. 24, para. 24, p. 29, para. 35). Nonetheless, Mr. Thomas represented to the Government that FI had incurred rental costs of $179,000. (R4, tab 21, subtab b, p. 2). Also, at the time Mr. Thomas signed the resubmital, Mr. Thomas knew that neither H. T. Foods nor FI had any obligation to pay real estate taxes. (G-18, p. 24, para. 24). Nonetheless, Mr. Thomas represented to the Government that FI had incurred real estate tax obligations in the amount of $32,198. (R4, tab 21, subtab b, p. 2).

45. The ACO requested an audit on the request since FI had never received PP prior to the subject contract. (Tr. 1509). Such action was in accordance with DCAA's recommended. In particular, the DCAA auditor who had conducted the evaluation of FI's proposal stated that FI's accounting system, at present, is adequate for the administration of PP,

however as there were no jobs in house, DCAA could not be assured of the continuance of this system and therefore recommended that another review be made when the contract was awarded. (See R 4, tab 1, p. 29) The ACO's action was also in accordance with DAR Appendix E-506 which requires a determination that the contractor's accounting system and controls are adequate for the proper administration of PPs. (G-1, p. 8). Based upon DCAA's findings in connection with FI's PP request 1, the ACO initially intended to deny the PP based upon the fact that Freedom had incurred any direct costs. (See R4, tab 15). However, this became a moot point when the Government discovered that FI did not have any outside financing. (G-71, p. 4 - 5, G-15, p. 3).

46. During a post award conference held on December 14, 1984, FI revealed that it had been unsuccessful in obtaining any financing through DDD and that FI saw little hope of obtaining financing from DDD. (G-15, p. 3; Tr. 1499-1500). FI advised that it was attempting to secure financial support from Broadway Bank. (G-15, p. 3; Tr. 1499). The information concerning the lack of financing from DDD came as a surprise to the Government since DDD's commitment was the reason FI received a positive preaward survey. (Tr. 1500).

47. One of the problems with obtaining another financial backer was that FI was so heavily burdened with prior debts that financial institutions were

not willing to commit to FI, as a result, FI attempted to circumvent this problem by using H.T. Foods as a go-between. (G-5; R4, tab 23, 24, 25, p. 2, para. c). However, H.T. Foods had no assets, consequently, it was no more attractive to creditors than FI. (R4, tab 25, p. 2, para. d). FI, therefore, attempted to officially assign its MRE contract to H.T. Foods who in turn would assign the contract to a financial institution. (See R4, tab 23).

48. Because FI owed approximately $3 million in past debts, and had no financing to pay these debts off, the Government was concerned that FI's creditors could force it out of business. (R4, tab 72; Tr. 1500). Due to this concern, and as part of the progress payment, ["PP"], review process, DCASR contacted DDD on December 17, 1984 to obtain the status of DDD's financing. (Tr. 1498-1500).

49. At that time, DDD advised that the August 9, 1984 commitment letter that the Government relied upon in awarding the contract was actually only a draft, (Tr. 1500; R4, tab 14), and the intended commitment letter was one that was dated August 10, 1984. (R4, tabs 14, 17). Up until this time, DCASR and DPSC were unaware of the existence of the August 10, 1984 commitment letter. (Tr. 1498-1500; G-71, p. 4). DDD also advised that before it would extend any credit to FI, FI would have to enter into payback agreements with its creditors, (Tr. 1499 -1500; R4, tabs 14, 17),

and the Government would have to guarantee any funds advanced by DDD. (Tr. 1499-1500; R4, tabs 14, 17).

50. By letter dated December 18, 1984, the ACO requested certain financial information from FI as part of the PP request review process. (R4, tab 12). specifically, FI was asked to provide (i) the amount of funding needed to perform the contract and the anticipated source of the funding, (ii) the time frame for its submission of loan applications, (iii) the date of its creditors' meeting and a time table for paying *its* outstanding debts, (iv) information concerning its possible eviction, (v) the status of it credit from DDD and is (vi) a copy of the August 10, 1984 letter from DDD. (R4, tab 12).

51. FI responded to the ACO's request for financial information by letter dated December 26, 1984. (R4, tab 13). FI advised that the working capital needed for completion of the contract was $415,164. (R4, tab 13). FI calculated this figure by taking its total costs of performance, i.e. $14,970,140 and subtracting 95% for progress payments leaving a total of $748,507 that would have to be financed through private financing. (R4, tab 13). FI then subtracted from this amount, the $333,333 that it had been allowed for depreciation. (R4, tab 13). FI also advised, among other things, that submission of its loan applications was being withheld until the Government committed to paying PP 1; that processing of its $550,000

SBA loan application was being withheld at its request until PP 1 was paid; that it would designate an assignee after the Government agreed to pay PP 1; and that there had been no change in the credit cited by DDD in its commitment letter. (R4, tab 13).

52. In brief, FI failed to provide any information that demonstrated that it had the financial wherewithal to perform the contract. The ACO did not find FI's response to be adequate to relieve his concerns as there was no commitment from any financial source. (Tr. 1502). Accordingly, by letter dated January 4, 1985, the ACO informed FI that he was considering returning PP 1 unpaid and suspending progress payments because evidence indicated that FI was in such unsatisfactory financial condition as to endanger performance of the contract. (R4, tab 16; Tr. 1501). The ACO noted that DDD had stated that it would not provide funding until an arrangement was in place to settle FI's past debts. (R4, tab 16). The ACO also advised FI of the results of DCAA's review and afforded FI the opportunity to respond to the ACO's concerns. (R4, tab 16).

53. Also on January 4, 1985, DCAA issued its audit report on FI's revised progress payment request No. 1. (R4, tab 15). Of the $252,150.00 claimed, DCAA recommended that $0 be paid. (R4, tab 15). DCAA questioned the following costs:

a. costs claimed for certain employee salaries which represented unbooked accrued salaries and related estimated

payroll taxes. (R4, tab 15, p. 2, 3). These costs were also questioned because there was no evidence that Freedom paid or would pay the claimed costs. (R4, tab 15, p. 2, 3).

b. salaries claimed for three employees which were actually for guards furnished by Penco, Inc. and billed to H. T. Food Products rather than to Freedom. (R4, tab 15, p. 3). Additionally, there was no documentation to support the claim that these individuals actually worked. (R4, tab 15, p. 2).

c. occupancy costs which represented unbooked costs billed to H. T. Food Products by Penco, Inc. and to some extent represented advanced billings. (R4, tab 15, p. 3).

d. costs claimed for insurance which were unbooked costs billed to H. T. Food Products by Penco, Inc. (R4, tab 15, p. 4).

e. costs claimed for legal and accounting fees which represented unbooked costs for services provided prior to contract award and as such were not eligible for progress payments. (R4, tab 15, p. 4).

f. costs claimed for transportation which represented unbooked costs which included personal automobile costs for Pat Marra and Henry Thomas that were unallowable. (R4, tab 15, p.4).

g, costs claimed for recruitment which represented unbooked costs for the placement of Pat Marra and were incurred prior to award and not eligible for progress payments. (R4, tab 15, p. 4)

h. costs claimed for telephone expenses which represented unbooked costs generated by Henry Thomas from his home telephone. (R4, tab 15, p. 4).

54. The questions raised by DCAA with respect to the above costs were warranted under DAR Appendix E-509.4 which provides:

> For progress payment purposes, costs, ... include all expenses of contract performance which are reasonable, allocable to the contract, consistent with sound and generally accepted accounting principles and practices

(G-1) and under the applicable progress payment clause, which similarly

provides:

> The Contractor's total costs ... shall be reasonable, allocable to this contract, and consistent with sound and generally accepted accounting principles and practices

(DAR Clause 7-104.35(b)(a)(2) at G-2). In the instant case, FI's failure to record its costs was "not consistent with sound and generally accepted accounting principles and practices." Similarly, FI's lack of receipts and/or supporting data was "not consistent with sound and generally accepted accounting principles and practices." Additionally, costs which were billed to a third parties, costs incurred prior to award and personal expenditures are not properly characterized as "allocable to the contract".

55. DCAA also found that FI did not provide books of account in support of the progress payment request, consequently, DCAA was unable to determine the accuracy of the accounting system for progress payment purposes. (R4, tab 15, p. 4). DAR Appendix E-506 requires the contractor to maintain an accounting system and controls which are adequate for the proper administration of progress payments. (G-1).

56. On January 14, 1985, DCAA issued an updated report on FI's progress payment request No. 1. (R4, tab 21). DCAA again recommended that $0 be paid even though FI had entered the claimed expenses on its books. (R4, tab 21). DCAA found that the information submitted in support

of the PP request was not sufficient to determine the adequacy and reliability of the accounting system. (R4, tab 21).

57. On or about January 14, 1985, FI submitted PP request 2 in the amount of $299,683. (FT, tab 422, p. 2927-2956). The request, which was signed by Henry Thomas, represented that FI had incurred a rent obligation of $89,500 and a real estate tax obligation of $16,089 for the month of January 1985. (FT, tab 422, p. 2928, 2950). At the time, Mr. Thomas signed PP request 2, he was fully aware that neither FI nor H.T. Foods had any rental obligation or any real estate tax obligation. (G-18, p. 24, para. 24, p. 26, para. 27).

58. By letter dated January 18, 1985, FI responded to the ACO's notice of possible suspension of PPs, essentially claiming that its insolvency was due to the lack of PPs. (R4, tab 22). FI also blamed the ACO for its lack of credit, claiming that the ACO was providing incorrect information to FI's backers. (R4, tab 22; Joint Stipulation #33). FI's claim that Mr. Liebman's statements, prior to January 18, 1985, destroyed its ability to conclude financing arrangements with bankers, suppliers and equipment manufacturers does not reconcile with the facts. No supplier or equipment manufacturer was ever willing to extend credit to FI even prior to award. All credit from suppliers and subcontractors was extended to H. T. Foods, not FI. For instance, Gemini Remodeling Corp. extended

$500,000.00 credit to H. T. Foods, FI. (R4, tab 18,, p. 2). Similarly, New Ventures Business Services, Inc. extended $2,000,000.00 credit to H. T. Food Products, not FI. (R4, tab 37, p. 7). Also, New Ventures Personnel Services, Inc. extended $75,000.00 in credit to H. T. Food Products, not FI. (R4, tab 37, p. 8).

59. Moreover, no financial institution was willing to deal with FI. DDD which purportedly was willing to extend credit to FI withdrew all financial support prior to award. (R4, tab 8). Broadway Bank which willing accepted an assignment from H. T. Foods was not willing to accept a letter of assignment from FI. (See R4, tab 23). Bankers Leasing extended credit under the contract to H. T. Foods, but not to FI. (R4, tab 37, p. 9).

60. FI had in excess of $2 million in debt when the contract was awarded. (R4, tab 1, p. 25). The debt was owed primarily to DDD. On behalf of FI, H. T. Foods requested that DDD subordinate its UCC 1 filing on accounts receivables so that new financing could be put into place. (R4, tab 27, p. 2). DDD refused to do this. (R4, tab 27, p. 2). According to Mr. Thomas, this refusal was detrimental to the refinancing of FI. (R4, tab 27, p. 2). Hence, FI was unable to get financing from any other financial institution due to DDD's refusal to subordinate, not because of *any statements* made by the ACO.

61. On January 24, 1985, a Subordination Agreement to the ACO which purportedly assigned FI's rights under, and the proceeds of the MRE contract to HT foods. (R4, tab 24). However, since H.T. Foods was not a financial institution, the assignment was unacceptable under the DAR and was ultimately withdrawn by FI. (See R4, tab 23).

62. On or about January 30, 1985, the ACO received further evidence of FI's unsatisfactory financial position by way of a Post-award Financial Surveillance Report issued by the DCASR's Financial Branch. (R4, tab 25; Tr. 1502). The report advised that FI's financial statements show a deficit $3,727,239. (R4, tab 25, para. b). Based on the adverse information provided in the surveillance report and the fact that FI did not have a financial backer, the ACO returned PP requests 1 and 2 and notified FI on February 6, 1985 that PPs were suspended due to FI's unsatisfactory financial position. (R4, tab 26; Joint Stipulation # 34). The specific reasons given were: (i) FI's financial backer advised that no credit would be forthcoming until an arrangement was in place to settle amounts owed to creditors, (ii) FI had not applied for/received loans from any financial institution, (iii) FI had a deficit of approximately $3.7 million, (iv) FI was the defendant in an number of claims arising from non payment of bills, and (v) HT Foods had no bank of record thereby putting itself in the position of not having an audit trail and rendering any financial statements unverifiable. (R4, tab 26; Joint Stipulation # 34).

63. The ACO's actions were justified under the guidance governing the suspension of PPs as set forth in Section E-524.2 of DAR, Appendix E provides:

> If unsatisfactory financial condition, or failure to make progress, endangering contract performance, as described in paragraph (c)(ii) of the clauses in 7104.35 is found to exist, arrangements reasonably assuring contract completion without loss to the Government will be required in connection with the making of further progress payments and the making of other payments so long as progress payments are unliquidated. Within the meaning of paragraph (c)(ii) of the clauses in 7-104.35, performance of the contract includes full liquidation of progress payments. Further payments will be withheld so long as any progress payments remain unliquidated, only upon full consideration of all pertinent facts, and upon concluding that further payments will serve to increase the probable loss to the Government.

(G-1, Section E-524.2). The ACO's actions were also justified under the applicable PP clause which provides:

> The Contracting Officer may reduce or suspend progress payments, ... whenever he finds upon substantial evidence that the contractor ... (ii) has so failed to make progress, or is in such unsatisfactory financial condition, as to endanger performance of this contract

(DAR Clause 7-104.35(b)(c) at G-2).

64. On February 14, 1985, FI met with Government personnel to discuss what actions FI would have to take in order to receive PPs. (R4, tab 27, p. 2). At that time, FI was informed that in order to cure its financial deficiencies, FI would have to obtain a line of credit of $3.8

million. (R4, tab 27, p. 2; Joint Stipulation #35; Tr. 1505). This was subsequently confirmed by the ACO in writing. (F1, subtab 31).

65. By letter dated February 14, 1985, FI wrote to DDD to relate the discussions that occurred at the meeting. (R4, tab 27). In particular, FI advised that "It was concluded at this meeting that in order for Freedom Industries to cure its financial deficiencies, it is necessary for it to replace the financial commitment from Dollar Dry Dock with a line of credit of $3.8 million. (R4, tab 27). Thereafter, on February 22, 1985, FI advised the ACO that it had been unable to secure the required financial banking and as a result, would novate its contract to HT Foods. (R4, tab 29). The novation was suggested to FI by its attorney Neil Ruttenberg, who subsequently prepared the necessary documentation. (G-94, p. 1, para. 4). Mr. Ruttenberg was so proud of his accomplishments in this regard that he boasted about them on the front page of a solicitous letter he prepared to attract another client. (G-94).

66. On February 26, 1985, DCAA issued a Report on Contractor in Financial Jeopardy which advised of FI's insolvency. (R4, tab 35). DCAA concluded that FI could not perform the contract given its financial condition and recommended that the Government exercise extreme caution in its consideration of any financial arrangements with FI especially since the practices employed by FI were designed to

deliberately delay and circumvent existing obligations to its creditors. (R4, tab 35).

67. On February 25, 1985, FI's PP request 3, dated February 8, 1985, was received by the ACO. (F 232, subtab "FI PP 3"; See also G-95, p. 1). The payment sought $231,555. (F 232, subtab "FI PP 3). The claimed incurred costs included $89,500 for rent and $16,089 for real estate taxes for February. (FT 422, p. 2960). The PP was signed by Henry Thomas. (FT 422, p. 2960). At the time, Mr. Thomas signed PP request 2, he was fully aware that neither FI nor H.T. Foods had any rental obligation or any real estate tax obligation. (G-18, p. 24, para. 24, p. 26, para. 27).

68. On February 28, 1985, HT Foods received an accounts receivable line of credit from Bankers Leasing Association, ["Bankers"], in the amount of $5,000,000. (R4, tab 36).

69. By letter dated March 12, 1985, FI requested a 90-day delivery schedule extension. (R4, tab 37). The PCO denied the request stating that the reasons given by FI for its delay, i.e. lack of progress payments was not beyond FI's control. (R4, tab 41). The PCO explained that progress payments were suspended due to FI's poor financial condition and that FI had been provided, more than once, with the information necessary to correct its financial deficiencies and has failed to do so. (R4,

tab 41). The PCO advised that should FI request a nonexcusable delivery extension, said request should include an offer of reasonable consideration. (R4, tab 41).

Reinstatement of Progress Payments

70. On March 26, 1985, FI entered into a Novation Agreement with HT Foods. (F-64; Joint Stipulation 36). The Agreement provided in part: "... the Transferee has acquired all obligations and liabilities of the Transferor under contract DLA13H-85C-0591 by virtue of the Transfer Agreement ... the Transferee also assumes all obligations and liabilities of, and all claims against the Transferor under the Contract." (F-64). The Novation was ultimately approved by the ACO on April 17, 1985. (Joint Stipulation # 36; F-64).

71. The Novation, which had the effect of shielding H. T. Foods from FI's creditors, was not a novel concept to FI. From the onset of the procurement process, FI had attempted to shield itself from its creditors through the use of commercial assignments to H. T. Foods. (G-5; R4, tab 24). Prior to approving the Novation, the Government convened several meetings to discuss the propriety of the Novation because there was some concern that the Government could be accused of shielding FI from its creditors and possibly exposing itself to law suits from FI's creditors. (Tr. 1508).

72. On April 18, 1985, the ACO received H. T. Foods' PP request 1, dated April 10, 1985. (See G-95, p. 1; Joint Stipulation # 37). The PP request rolled up the claimed costs contained in FI's requests 1 – 3 and added additional costs allegedly incurred after the submission of FI's PP request 3. (Joint Stipulation # 37). HT Foods' PP 1 sought $1,766,923. (F232, subtab PP #1, p. 2). The PP request was signed by Henry Thomas. (F232, subtab PP #1, p. 2). The payment was referred for a prepayment audit, as were most subsequent PP requests because the ACO could not place any reliance on FI's submissions. (Tr. 1510). This lack of faith in FI's submissions was due to the fact that FI routinely sought recovery of: (i) costs that were not booked, (ii) costs for which FI was not liable, (iii) costs that were incurred prior to award, (iv) costs that were excessive, (v) costs that should have been capitalized, (vi) costs that were unallowable under the DAR, and (vii) costs that were duplicative. (Tr. 1510-11). Moreover, FI routinely did not pay its bills in the ordinary course of business. (Tr. 1510-11).

73. Included in the claimed costs was $730,073 for occupancy costs. (FT 422, subtab HT PP # 1, p. 3037). Of this amount, $447,500 represented rent for November, 1984, December 1984, January 1985, February 1985 and March 1985, and $70,445 represented real estate taxes for November, 1984, December 1984, January 1985, February 1985

and March 1985. At the time, Mr. Thomas signed PP request 2, he was fully aware that neither FI nor H.T. Foods had any rental obligation or any real estate tax obligation for the period of November 84 through March 1985. (G-18, p. 24, para. 24, p. 26, para. 27).

74. The ACO reduced the payment by $66,192 which represented capital costs. (G-95). The ACO's nonpayment of the cost of capital costs was in accordance with DLA Clause 7-104.35(b) which provides:

> The Contractor's total cost ... shall not include ...
> (iii) costs ordinarily capitalized and subject to depreciation or amortization except for the properly depreciated or amortized portion of such costs.

(DAR Clause 7-104.35(b)(a)(2)(iii) at G-2). Although DCAA recommended a payment of $0, (FT 422, subtab HT PP # 1, p. 3036), the ACO authorized payment of $1.7 million and a check in that amount was issued on or about May 6, 1985. (Joint Stipulation # 37; F-232, subtab PP #1, p. 4). FI did not use any portion of this money to pay rent or real estate taxes for the months of November 1984 through March 1985. (See G-18, p. 29, para. 35 wherein Mr. Thomas swore that "The first rental check was delivered to Pilot Realty Co. for the April, 1985 rent. This was actually paid somewhere in the beginning of May, 1985").

76. On or about May 15, 1985, H.T Foods submitted PP request # 2, dated May 16, 1985. (F232, subtab PP #2, p. 3; Joint Stipulation # 39). The request sought $673,074. (F232, subtab PP #2, p. 3). Included in the

request were subcontractor costs in the amount of $209,266: Cadillac $117,021, Del Monte $36,536 and Trans Packers $55,711[4] which were set aside pending a prepayment review. (F232, subtab PP #2, p. 4).

DCAA questioned the following costs:

> a. salaries and related payroll taxes which had been withheld for approximately six weeks
>
> b. costs which were associated with setting up a new business and were administrative in nature and not related to production under the contract
>
> c costs for quality control equipment for which H. T. Food Products was unable to furnish vendor receipts or proper supporting data. DCAA also noted that said costs were generally capitalized
>
> d. costs for automation building equipment which were normally capitalized
>
> e. costs for office equipment which were generally capitalized

(R4, tab 54). DCAA recommended that $0 be paid. (R4, tab 54). The ACO however, did not follow this recommendation.

77. The ACO backed out the subcontractor costs and further reduced the payment by $138,300 which were capital costs: quality control equipment $37,960, automated building management $84,092, office equipment $16,248[5]. (R4, tab 54; F232, subtab PP #2, p. 4). A check in the amount of $332,421 was issued on June 6, 1985, approximately three

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[4] These subcontractor costs were all ultimately paid in full in PP 3 and 4.

5. The DCAA lists these costs as they were submitted by the contractor, i. e. at 100%. (See R4, tab 54). The ACO's reductions, however, were taken at 95% for contractor costs and 100% for subcontractor costs since subcontractor's costs are already reduced to 95% when they are submitted to the contractor. (Tr. 1557-1558).

weeks after the date of the request. F232, subtab PP #2, p. 1; Joint Stipulation # 39).

78. H.T. Foods submitted PP request 3, in the amount of $544,086, on or about June 1, 1985. (F-232, subtab PP #3, p. 2; Joint Stipulation # 39). The request was revised on June 3, 1985 and sought $523,767. (F-232, subtab PP #3, p. 3; Tr. 1558). The request included Cadillac subcontractor costs of $53,668[6] which were deducted from the payment pending DCAA review. DCAA questioned the following costs:

a. salaries and related payroll taxes which had been withheld for approximately six to eight weeks

b. costs which are associated with setting up a new business and are administrative in nature and not related to production under the contract

c. costs for building repair and renovation for which H. T. Foods was unable to furnish vendor receipts or proper supporting data

d. costs for telephone installation and security deposit for which H. T. Foods did not furnish vendor receipts or proper supporting data

e. costs for traveling expenses, (air fare costs), for which H. T. Foods did not furnish proper supporting data

f. certain costs relating to consulting management services which were considered excessive,

g. costs for local transportation for which H. T. Foods did not furnish proper supporting data.

(R4, tab 57). As indicated above, the majority of H. T. Foods' costs were

questioned because H.T. Foods could not produce receipts or other evidence to establish that the costs were actually incurred.

79. In spite of the fact that DCAA recommended $0, the ACO nonetheless paid $535,767.00. (R4, tab F-232, subtab PP # 3). In arriving at this amount, The ACO backed out $53,660.00 in subcontractor claims and further reduced by $49,367 which represented capital costs questioned by DCAA. (F-232, subtab PP #3, p. 3). The payment for PP 3 was then increased by $92,247 which represented subcontractor costs (Del Monte $36,536, Trans Packers $55,711) that had previously been set-aside in PP 2 pending DCAA review. (F-232, subtab PP #3, p. 3). Although DCAA recommended $0, (R4, tab 57, p.1), the ACO authorized a payment and a check in the amount of $535,767 was issued on June 24, 1985, a little more than three weeks after the date of the original request. (F-232, subtab PP #3, p. 1; Joint Stipulation # 39).

80. By June 1985, H. T. Foods, had not begun production under the contract. (R4, tab 193, p. 15). At that point in time, H. T. Foods was still in the process of repairing its building and receiving CFM. (R4, tab 193, p. 15). As a result, bilateral modification P00011 issued on June 14, 1985 under the default clause and extended the delivery schedule as follows:

line item	Quantity	Delivery Date

[6] The subcontractor costs for Cadilliac were reported as $56,492 in DCAA's audit report for PP3. (R4, tab 57, p. 2,3). However, this was subsequently corrected in DCAA's audit report for subcontractor costs. (R4, tab 58).

0001CP	100,000	1-31 Oct	1985
0001CQ	100,000	1-30 Nov	1985
0001CR	100,000	1-30 Dec	1985
0001CS	100,000	1-31 Jan	1986
0001CT	100,000	1-28 Feb	1986
0001CU	100,000	1-31 Mar	1986

(R4, tab 55). No claims were reserved in the modification.

81. In consideration for the extension, H. T Foods agreed to pay $99,900.00 plus $100.00 for the administrative costs of issuing the modification. (R4, tab 55). H. T. Foods did not submit a payment of $100,000 for the consideration, nor was H. T. Foods required to do so. (R4, tab 55, p. 3, para. (e)). Pursuant to the modification, the consideration would be "deducted by the Government from any money which is or may become due and owing to the Government". (R4, tab 55, p. 3, para. (e))

82. Under the terms of Modification P00011, H. T. Foods also agreed to be financially liable for all costs incurred for storage of GFM which H. T. Foods had been unable to receive in accordance with the terms of the contract. (R4, tab 55). H. T. Foods had been unable to accept receipt of the GFM due to its failure to past Health Services Command's ["HSC"] sanitation inspection. (R4, tab 55). H. T. Foods' failure to bring the building up to HSC standards arises from:

1. the fact that H.T Foods did not gain full access to its Bronxdale facility until April 1985, consequently neither H. T. Foods nor its

predecessor were not in the position to receive GFM in a timely manner, (G-18, p. 26, para. 27; G-14, p. 7, para. A)

2. the fact that FI had no money and no source of financing contrary to its preaward representations

3. the fact that H. T. Foods made a business decision not to draw down against its $5 million line of credit it had obtained from Bankers in March 1985

4. the fact that H. T. Foods made a business decision not to use its $500,000 + windfall it fraudulently obtained in PP 1 to finance the building repairs.

The August 85 Proposed Suspension of Progress Payments

83. On July 25, 1985, the ACO received H. T. Foods PP request 4, dated July 25,1985. (See G-95). The request sought $170,689. (F232, subtab PP #4, p. 2). The costs claimed reflected Cadillac subcontractor costs originally submitted in H.T. Foods PP request 2 ($117,021) and request 3 ($53,668). (Tr. 1559; See F 232, subtab PP #5, p. 1). A check in the amount of $170,689 was issued on July 29, 1985. (See F 232, subtab PP #4, p. 1).

84. Also on July 25, 1985, the ACO received H.T. Foods PP request 5[7],

[7] The request was original submitted as request No. 4, but was administratively renumbered by the ACO since the subcontractor costs had been paid as PP 4.

dated July 5, 1985. (G-95). The request sought $807,348. (R4, tab 60, subtab c). The request was submitted to DCAA for a prepayment audit. (See R4, tab 60). The ACO's request for a prepayment audit was in accordance with DAR Appendix E-521 which provides:

> Progress Payment Clauses cannot be self-executing, and require careful administration to insure against overpayments and losses . ... It is necessary for adequate supervision of progress payments that the administering office keep itself informed concerning the contractor's overall operations and financial condition .. For contracts with those contractors whose financial condition is doubtful or not strong in relation to progress payments outstanding or to be outstanding, or whose management is of doubtful capacity or whose accounting controls are found by experience to be weak, or who are encountering substantial difficulties in performance, full information concerning both the progress under the contracts involved ... and concerning the contractor's other operations and financial condition, should be obtained and analyzed at frequent intervals, with a view to the better protection of the interest of the Government and taking of such action as may be proper to make contract performance more certain.

(G-1)

85. On August 2, 1985, DCAA issued, to its Regional Director, a Report of Suspected Irregular Conduct relative to Appellant's bookkeeping and questionable business practices. (F1, subtab 32). Among other things, the report advised that:

> a. We found inadequate documentation supporting disbursement, namely, in some instances no invoices to support payment. In other instances, especially on major expenditures, no purchase orders were issued.
>
> b. Lack of internal control of disbursements. All transactions were solely disbursed by Henry Thomas. After the disbursement were made, the accounting department was advised of the transaction and nature thereof, without adequate justification and

documentation. This resulted in questionable expenditures and business practices, some of which are listed below.

(1) *Gemini Remodeling Corporation.* This company was contracted to perform clean up, building repair and renovations. Only one purchase order totaling $50 thousand was awarded to Gemini. Total payments to date amount to $132 thousand. The majority of payments were made personally to an official of Gemini. These checks were all cashed at Citibank – (bank used by Freedom). In certain cases the checks that were cashed were not endorsed. Invoices in support of work performed were handwritten on Gemini letterhead with no indication of work performed or where it was performed.

(2) Payroll – Freedom had originally accrued payroll together with related payroll taxes for employees who worked on this contract from inception November 1984 through 29 March 1985. This accrued payroll was reversed on the books and the individuals paid as though they were consultants. The payroll taxes were avoided and taken off the books.

(3) Freedom had entered into a lease for the building in which they occupy with Penco, Inc. Included in the lease agreement was an option by freedom to purchase the building. Penco subsequently sold the building to a third party and freedom contends that they received $400 thousand as a buy-out of their option. Freedom had submitted and was reimbursed for full occupancy costs. Freedom id not nor do they intend on reducing the costs to give affect to the lease buy-out. Freedom is treating this item as other income.

(F-32, p 2-3).

86. On or about August 8, 1985, H.T. Foods submitted PP request 6 seeking $607,348. (R4, tab 66, subtab c). The request was submitted to DCAA for a prepayment audit. (See tab 66).

87. On August 13, 1985, DCAA issued its audit report on PP request 5, which was originally submitted as 4. (R4, tab 60). DCAA recommended

$0 payment. (R4, tab 60, p.1). Among other things, DCAA questioned (i) a rental income credit of $400,000, which H. T. Foods treated as profit rather than a reduction of occupancy costs. (R3, tab 60, p. 3). DCAA also questioned (i) $96,530 in duplicate real estate taxes, (ii) ineligible costs, (iii) costs not supported by documentation, (iv) costs inapplicable to the instant contract, and (v) unreasonable and unnecessary costs. (R4, tab 60, p. 3-4). DCAA further questioned costs for which H. T. Foods was not liable such as phone bills for New Venture Tax Services and costs for repossessed AT&T equipment. (R4, tab 60, p. 4).

88. DCAA also reported that H. T. Foods had not obtained any personal financing to date and was attempting to perform the contract solely on monies received from the Government on progress payments. (R4, tab 60, p. 5). DCAA noted that many expenses had arisen, such as deposits required on utilities and capital equipment, bank interest for a line of credit, large amount of legal and accounting and repayment of personal loans, which were paid for from PPs resulting in many vendors and expenses going unpaid. (R4, tab 60, p. 5). DCAA concluded that H. T. Foods would not be able to operate without personal financing, therefore should this condition continue the entire contract performance will be in grave financial jeopardy. (R4,tab 60, p. 5).

89. Finally, DCAA found that H. T. Foods' accounting system was inadequate for the purposes of progress payments. (R4, tab 60, p. 4). In this regard, DCAA noted that H. T. Foods:

a) did not properly record liabilities on its books,
b) did not record all subcontractor invoices on its books even though the invoices were submitted for PPs
c) did not have adequate and in some instances any supporting documentation
d) did not maintain a cash disbursement journal, or subsidiary ledger to trace the transactions from the check register to the general books of accounts

(R4, tab 60, p. 4). DCAA also noted that it was unable to reconcile the claimed PP amounts requested and the total costs claimed through PP request 4. (R4, tab 60, p. 4 -5).

90. HT Foods changed its name to Freedom, N.Y., Inc. [hereinafter "FNY" or Appellant], and Modification A0002 issued on August 14, 1985 acknowledging the name change. (R4, tab 61).

91. By letter dated August 23, 1985, the ACO advised that he was considering returning PP request No. 5, (originally submitted as PP request No. 4), and suspending PPs based on a finding by DCAA that Appellant's current cost accounting system and controls were not considered adequate for accumulating contract costs in support of progress payments requests. (R4, tab 61; Tr. 1513). Essentially, the flaws in Appellant's accounting system had become so flagrant, numerous and pervasive that the system was no longer reliable. (Tr. 1511-1512).

92. In order for a contractor to receive PPs, its accounting system must be deemed acceptable for PP purposes and the agency that makes that determination is DCAA. (Tr. 1513: G-1, Section E-506). If DCAA makes a finding that the accounting system is inadequate for the purposes of PPs, the ACO is prevented from paying PPs. (Tr. 1513). DAR Appendix E, Section E-506 states:

> The contractor's accounting system and controls must be adequate for the proper administration of progress payments. If the contractor's accounting system and controls have been found (by experience or by Defense Contract Audit Agency) to be sufficient and reliable for segregation and accumulation of contract costs, no further examination should be necessary so long as the efficiency and reliability of the contractor's system and controls are maintained. In all doubtful cases, including contracts with contractors with whom the Defense Contract Audit Agency has had no experience within the next preceding twelve months, the adequacy of the contractor's accounting system and controls shall be determined, and any necessary changes shall be accomplished. Until such time as the necessary changes are made, the accounting system shall be deemed inadequate and progress payments suspended. For this purpose, the services of the Defense Contract Audit Agency should be utilized to the greatest extent practicable.

(G-1, Section E-506).

93. On or about September 12, 1985, DCAA issued its Audit Report for PP request 6. (R4, tab 66). DCAA recommended a payment of $0. (R4, tab 66, p. 2). DCAA also found that there had been no significant changes in Appellant's accounting system since the last audit. (R4, tab 66, p. 4).

94. On September 25, 1995, emergency, same day, progress payments totaling $11,076 (PP 5 paid in the amount of $6687.46 and PP 6 paid in the amount of $4,389.29) were made to Appellant for utility bills. (G-14, p. 16; G-95; Tr. 1515, 24, 25). The emergency payment was necessary in order to prevent a shut-off of electricity and gas at Appellant's facility. (G-14, p. 16; Tr. 1515). As of this date, Appellant had not commence any assembly or production of accessory packs; production of crackers had begun only two days earlier. (R4, tab 193, p. 26).

95. On October 2, 1985, Appellant submitted revised PP request 7, which included the following:

PP 5	$ 807,348
PP 6	$ 640,767
PP 7	$1,557,122
total	$3,005,231
payments received (PP 5 & 6)	- $ 11,077
Amount claimed	$2,994,154

(R4, tab 73).

96. The ACO reduced the payment by $543,273 which reflected the following questioned costs: (i) an equipment lease for $343,000 which was actually a financing arrangement in that the first payment amounted to 90% of the total payments, (ii) salaries relating to renovation of the building in the amount of $101,757, (iii) other capital costs in the amount of $47,880, (iv) costs capitalized on the books but billed at 100% in the

amount of $30,106 and (v) excessive legal and accounting fees of $20,530. (G-95; R4, tab 76). The payment was also reduced by Del Monte's subcontractor claim in the amount of $534,456, which was referred for audit. (G-95; R4, tab 76, p. 5). The Del Monte subcontractor claim was subsequently withdrawn by Del Monte as it refused to deliver the subject supplies or any further supplies to Appellant unless it was paid in advance. (Tr. 1527-28). Del Monte's decision to demand cash up front was based on the fact that Appellant had never paid for previously delivered goods. (Tr. 1527-28). A check in the amount of $1,913,726 was issued on October 11, 1985. (F232, subtab PP #7, p. 1).

Delivery Extension And Increase In PPs

97. By letter dated August 30, 1985, the PCO issued a cure notice stating that Appellant's lack of financial capacity and lack of vital production equipment endangered performance. (R4, tab 63). Appellant responded to the cure notice by letter dated September 13, 1985. (R4, tab 67). Appellant advised that all necessary equipment was in house, argued that DCAA's finding concerning Appellant's accounting system was wrong, and alleged the dispute over expensing capital expenditures was based on a misunderstanding of the negotiated terms of the contract. (R4, tab 67).

98. Appellant proposed two plans and delivery schedules to cure its delinquency. (R4, tab 67). Plan 1 called for the redistribution of the production of MREs with no slip in the delivery schedule past the March 31, 1986 delivery date. The plan allowed for a smaller quantity of cases to be delivered during the first three months of production and an accelerated production for the last three months. (R4, tab 67; see also R4, tab 65). Plan 2 called for up front time to implement the computerized lot tracking and inventory systems and time to train new personnel in the production of MRE. This plan called for a 60-day slip in the final shipment of MRES to the Government. Production would gradually increase each month and end with a production output equal to Appellant's minimum sustaining rate for the MRE 6. (R4, tab 67; see also R4, tab 65).

99. To adequately consider Appellant's revised delivery schedules the Government performed a complete survey to ascertain the viability of Appellant's offers. (R4, tabs 75, para. 4, 70, 71). In particular, the Government confirmed that Appellant had in-place "all equipment necessary to accomplish the required tasks for sub-assembly and final assembly operations relative to MRE ration assembly" (R4, tab 70, p.1) (Emphasis added). While Appellant did not have sufficient quantities of CFM (for instance, pork patties, beef patties, chicken loaf, ham & chicken loaf), Appellant assured the Government that sufficient quantities would be in-house by October 10, 1985. (R, tab 70, p. 1). Based upon these

confirmations and assurances, the Government determined that plan 2 was feasible from a technical standpoint and more suitable due to its flexibility. (R4, tab 70, 71).

100. On September 30, 1985, DCASR Financial Analysis advised the ACO that Appellant had a "Cash Short Fall" of $1,000,000. (R4, tab 72). Appellant had drawn down $2 million of its $5 million line of credit, (See R4, tab 75, p. 5), but Appellant had not shown the ability to obtain additional financing from Bankers. (R4, tab 72). Government personnel met on October 2, 1985 to determine whether Appellant's delivery schedule should be extended. (R4, tab 75, para. 7). During that meeting, it was determined that Appellant would need additional funding in the following amount:

$1 million deficit working capital
$1.5 million October 1985 working capital
$1 million capital over & above progress payments total $3.5 million.

(R4, tab 75, para. 4). The $3.5 million figure increased Appellant's original line of credit from $5 million to $5.5 million. The additional $500,000 took into consideration a DAR deviation for capital expenses being denied. (R4, tab 75, para. 7). In the afternoon of October 2, 1985, the Government advised Appellant of the financial conditions that must be meet in order to receive a delivery schedule extension. (R4, tab 75, para. 7).

101. On October 3, 1985, Government personnel met with Appellant and it was mutually agreed that pending Government confirmation that the $3.5 million was available to Appellant and that Appellant had drawn on these monies to pay all subcontractor bills over 30 days past due, the Government would extend Appellant's delivery schedule in accordance with Plan 2. (R4, tab 75, para. 8). It was also agreed that the frequency of the contract's increases in the progress payment ceiling would be amended. (R4, tab 75, para. 8).

102. The matter of capitalized vs. expensed costs, as negotiated on November 6, 1984, was also discussed. (R4, tab 75, para. 8). The contract was interpreted to allow the following capital costs to be expensed:

Cost Element	$ Amount
Quality Control Equipment And Supplies	54,000
Maintenance Equipment	23,380
Building Repair	160,000
Automated Bldg Mgmt and Control System	177,838
Lockers	25,000
Office Equipment	80,000
Total	522,218

(R4, tab 75, p. 7, para. 8). Appellant was informed that this allowance would be implemented in a modification pending approval of a DOD DAR deviation request. (R4, tab 75, para. 8). The DAR deviation request had been submitted, by the ACO, in the July 1985 time frame on the advice of Counsel. (F-85, F-87). The request had been forwarded by DPSC to DLA on August 27, 1985. (G-14, p. 13, para. 4). DLA then forwarded it to

DoD. (G-14, p. 13, para. 4). At some point in the October 1985 time frame, DoD sent the request back to DPSC for "redefinition". (G-14, p.19, para. 5).

103. On October 11, 1985, Appellant submitted progress payment request 8 seeking $869,688. (F-232, subtab PP #8, p.3). The following questioned costs were deducted from the payment: $9,644 for maintenance, and $42, 657 for manufacturing salaries. (See R4, tab 80, p. 2-3; G-95, p. 2; R4, tab 80-, subtab a, p. 2-3). The ACO also deducted $33,622 for DCAA adjustments to this and previous requests, and $400,000 for a questionable rental expense that had been previously paid by the ACO (G-95, p. 2; R4, tab 80, subtab a, p. 2-3: Tr. 1530). PP 8 was pay in the amount of $869,688 on November 13, 1985, a little more than a month after the date of the request. (F-232, subtab PP 8, p. 1).

104. The claim for rental expense arose because Appellant had surrendered its right to buy the Bronxdale facility so that the owner could sell the property to a third party. (See R4, tab 76, p. 3). Appellant claimed that the $400,000 represented the amount it was informally offered for giving up its option. (See R4, tab 76, p. 3). In actually, the $400,000 arose from a settlement agreement wherein the landlord forgave $400,000 of unpaid back rent in exchange for Appellant's release of the option. (See G-22). DCAA determined that the forgiveness of rent should be

treated as a reduction in occupancy cost. (R4, tab 76, p. 3). In the instant case, Appellant had submitted PP requests and had been paid for all the forgiven back rent (plus more). (See PFF 65, above).

105. On October 29, 1985, Appellant commenced assembly of final cases. (R4, tab 193, p. 29).

106 On or about November 8, 1985, Appellant submitted PP #9 seeking $979,156. (F232, subpart PP # 9, p. 3). The PP request made "retroactive" reductions to PP requests 7 and 8 in connection to the Technic Lease. (F-108). The Technic lease had been the subject of an ongoing dispute due to the fact that the original proposed lease called for an initial payment of approximately 90% of the total payment. (Tr. 1526-27, 1533-35; R4, tab 76, p.2; tab 80, p. 2). DCAA viewed the costs Appellant categorized as equipment leasing ($176,500) and prepaid expenses ($169,488) to actually be the purchase of equipment which should be capitalized and depreciated. (R4, tab 76, p.2; tab 80, p. 2). Ultimately, Appellant developed a lease agreement which was accepted by DCAA as an operating lease rather than a purchasing instrument. (Tr. 1533-35).

107. The ACO reduced the payment by $88,357 which reflected a deduction of $17,697 for excessive legal and accounting fees and a

reduction of $214,285 for the "old" Technic equipment lease. (F232, subpart PP # 9, p. 4). These reductions were offset by the addition of $140,625 for the "new" Technic equipment lease and a $3,000 adjustment due to the contractor's error. (F232, subpart PP # 9, p. 4). The ACO authorized payment of $895,217 and a check in that amount was issued on December 6, 1985, less than a month after the date of the request. (F232, subpart PP # 9, p. 1).

108. As of November 8, 1986, no final cases had been shipped. (R4, tab 193, p. 30). Bilateral contract Modification P00018 issued on November 15, 1985 extending the delivery schedule as follows:

Line item	Quantity	Delivery Date		
0001CP	49,960	1-30	Nov	85
0001CV	1	1-30	Nov	85
0001CW	30	1-30	Nov	85
0001CQ	65,000	1-31	Dec	85
0001CR	75,000	1-31	Jan	86
0001CS	90,000	1-28	Feb	86
0001CT	100,000	1-31	Mar	86
0001CU	120,000	1-30	Apr	86
0001KK	120,304	1-31	May	86

(R4, tab 85, para. (a)). The modification also provided that "the limitation on Progress Payments shall increase by $1,000,000 after each incremental production of 50,000 cases has been completed and accepted by the Government. This limitation shall be limited to $4,000,000 ... (R4, tab 82, para. (f)).

109. In consideration of the extension and increase in PPs, Appellant agreed to pay the Government $99,900.00 plus $100.00 for the execution of the modification. (R4, tab 85, para. (b)). Appellant was not required to make, and did not make, an actual payment of $100,000, rather pursuant to the terms of the modification, Appellant agreed that the consideration would be effectuated by "any appropriate deduction by the Government from any monies which is or may become due and owing to the Contractor." (R4, tab 85, para. (d)). No claims were reserved in the modification. R4, tab 85).

Performance Under Modification P00018's Schedule

110. As of November 22, 1985, Appellant had produced 19,326 finished cases. (R4, tab 193, p. 33). As of November 21, 1985, only two lots had been presented to the AVI for final inspection. (R4, tab 193, p. 33). Lot 1 consisting of 242 cases was accepted: lot 3 consisting of 1,215 cases was rejected. (R4, tab 193, p. 33). Lot 2 was never presented to the AVI as it had been rejected by Appellant's quality control department. (R4, tab 193, p. 33). As of December 2, 1985, Appellant had produced 24,088 final cases. (R4, tab 193, p. 35). Only lot 1 consisting of 242 cases had been accepted, (R4, tab 193, p. 35). Lot 5 and 2A were rejected for failure to have one of each menu per case. (R4, tab 193, p. 35). Lot 7 was rejected for vacuum loss. (R4, tab 193, p. 35). Lots 8, 9 and 10 were undergoing

inspection as of December 2, 1985 and lots 6, 11, 12 and 13 had not yet been presented for inspection. (R4, tab 193, p. 35).

111. On November 29, 1985, Appellant submitted PP request 10 seeking $353,081. A check in this amount was issued January 30, 1986. (F232, subtab PP #10, p. 1). The payment reflected a reconciliation of previous payments and included $308,542 for G&A and manufacturing salaries claimed, but not paid, in previous requests, plus a $44,539 adjustment to correct the amount previously deducted for the lease option. (F-232, subtab # 10, p. 4).

112. The $44,539 adjustment relative to the lease option was made as a result of Appellant's representation that the $400,000 was only an approximate amount under the terms of a settlement agreement with its former landlord; the actual amount was $374,180[8]. (R4, tab 89). Among other things, the Settlement Agreement resolved the dispute between Appellant and its former landlord relative to various issues arising from a lease the parties entered into in March 1985. (See G-22). Under the March 1985 lease, Appellant gave up its option to purchase the building and also gave up the "free" use of certain racks and forklifts. (See G-22). Appellant claimed that it had been tricked into signing the lease by Mr. Penzer, and never intended to give up its option or its use of the racks and

[8] Neither Appellant nor its predecessor paid any rent or real estate taxes from November 1984 through March 1985, consequently, the total forgiveness exceeded a half a million dollars. (See FPP , above)

forklift. (See generally G-18). In May 1985, when Appellant discovered that the new March 1985 lease eliminated the use of the racks and forklifts, Appellant purchased the racks and forklifts for $295,000. (G-18, p. 31, para. 37). This amount was more than the value given the equipment by Mr. Penzer. (See G-18, p. 32, para. 40). For some unknown reason, under the Settlement Agreement, Appellant agreed to purchase the racks and forklifts a second time for the additional sum of $335,000. (G-22, p 4-7).

113. Appellant contended that the ACO should offset its obligation to pay $335,000 for the equipment against the $400,000 (adjusted to $374,180) gain arising from debt forgiveness. (R4, tab 89). The ACO did not accept this contention, and the adjustment payable made under PP 10 was limited to $44,539. (See F232, subtab PP #10, p. 4: Tr. 1542).

114. By December 2, 1985, Appellant had only shipped 242 cases of MREs, (R4, tab 193, p. 35), which was 49,758 cases short of the amount due by November 30, 1985. (R4, tab 90, para. 3)., Appellant's delay was attributed to:

1. production problems related to its lack of experience and training of its personnel, (G-14, p. 20; R4, tab 193, p. 33, 37, 40)
2. failure to work to capacity by utilizing all 12 assembly lines, (G-14, p. 20; R4, tab 193, p. 29, 32)
3. high rejection rates, (G-14, p. 18, 23; R4, tab 193, p. 37, 40)
4 numerous quality problems related to its failure to follow the procedures set forth in the quality assurance requirements of

the contract and in its own Contractor Inspection System. (R4, tabs 67, 91, 95)
5 problems encountered with subcontractors (R4, tabs 59, 88, tab 193, p. 16).

115. Appellant attributed it delay to an alleged seven month delay in paying progress payments which caused it to incurred $770,000 for additional rent plus other sums for salaries, insurance, etc. (R4, tab 100, p. 2, para.4). The contention that there was a seven month delay in paying progress payments does not reconcile with Mr. Thomas' sworn Affidavit wherein he stated at the time the contract was awarded, he did not expect PP to begin until the March 1985 time frame. (G-18, p. 9, para. 21). The contention that the allege delay caused a $770,000 increase in occupancy costs does not reconcile with the fact that in May 1985, Appellant received a PP which included over one a half a million dollars which was claimed for rent and real estate taxes that Appellant has never paid and has never been obligation to pay. (PFF 74, above).

116. The PCO made a determination to terminate the November 1985 increment. (R4, tab 90; Joint Stipulation # 44). In making this decision, the PCO considered the supply situation and determined that the requirements were urgently required and could not be foregone. (R4, tab 90, para. 4). The PCO also considered the amount of time it would take to obtain the supplies from another source as opposed to obtaining the supplies from Appellant. The PCO determined that it would take Appellant

minimally two months to replace the delinquent quantity. On the other hand, one of the other two MRE assemblers who could have definitely produced the supplies within a two month period. (R4, tab 90, para. 4). In considering the degree of essentiality of Appellant and the impact a termination would have on Appellant, it was determined that the need for timely deliveries must remain the primary concern of the Government. (R4, tab 90). By wire dated December 6, 1985, the PCO terminated the November 1985 delivery increment of the contract. (F 112; Joint Stipulation # 44).

117. Government personnel met with Appellant on December 9, 1985 to discuss the future of the contract balance. (See R4, tab 100, para. 1). At this time, it was apparent that Appellant would fail to meet its December 1985 delivery increment. (R4, tab 100, para. 3). The Government needed the supplies to comply with its pre-position, war reserves levels and considered terminating Appellant's December increment since it could obtain the supplies more quickly through a repurchase than through Appellant. (R4, tab 100, para. 3). During the December 9, 1985 meeting, Appellant suggested that the December 31, 1986 delivery increment be terminated and that it and the November increment be added to the end of the contract. (R4, tab 100, para. 8). Appellant also advised that the contract was in a loss position and that Appellant would need an additional $1.4 million to complete the contract. (G-14, p. 24, para. 9).

118. On December 6, 1985 the GAO issued a decision denying Appellant's protest docketed as B-219676. (R4, tab 93). The protest challenged DPSC's decision to expand the industrial base for MRE assembly by included a new company – CINPAC. (See R4, tab 93). Appellant contended that the expansion was improper, that DLA improperly determined that requirements for MREs and that CINPAC was not eligible for participation in the program. (See R4, tab 93).

119. On or about December 11, 1985, Appellant submitted PP request 11 seeking $1,159,473. (F232, subtab PP #11). Payment, in the amount of $1,152,015, was authorized January 29, 1985. (See R4, tab 194, p. 2). Notwithstanding the fact that the PP request included $29,000 for insurance costs which had previously been billed for the same period and coverage (R4, tab 117), the only reduction taken by the ACO was $7,458 for excessive legal and accounting fees. (G-95).

120. On January 2, 1986, the PCO issued a Determination and Findings wherein he determined to terminate the December increment of the delivery schedule for failure to deliver. (R4, tab 100). In making that determination, the PCO considered, among other things, Appellant's 7 month delay claim and found that it had no merit. (R4, tab 100, para. 4, 5).

121 By wire dated January 2, 1986, the PCO issued a notice of partial termination. (R4, tab 99). Specifically, the December increment of the contract was terminated for default per Appellant's request. (R4, tab 99; Joint Stipulation # 44). By letter dated January 23, 1986, the PCO confirmed the Government's telegraphic notices of termination dated December 6, 1985 and January 2, 1986 and issued his findings of fact and final decision. (R4, tab 103).

122. Bilateral Contract Modification P00020 issued on January 29, 1986 reducing the contract quantity from 620,304 cases to 505,546, which reduction represented the terminations of the undelivered quantity for the November 1985 delivery increment and the entire December 1985 delivery increment. (R4, tab 104). The modification also removed the limitation that restricted initial PPs to 50% of the contract price. (R4, tab 104, p. 3, para. 4). Modification P00020 revised the delivery schedule for the contract balance as follows:

Item	Date	Quantity
0001CR	1-31 Jan 86	20,000 cases
0001CS	1-28 Feb 86	30,000 cases
0001CT	1-31 Mar 86	50,000 cases
0001CU	1-30 Apr 86	80,000 cases
0001KK	1-31 May 86	100,000 cases
0001KM	1-30 Jun 86	120,000 cases
0001KN	1-31 Jul 86	105,304 cases

(R4, tab 104, para. 2). The Modification further provided that "[i]n the event the contractor meets the 1-31 Jan through 1-30 Apr. 86 increments as set forth in paragraph 2 above, the Government may reinstate the

114,758 cases terminated for default. Such units are to be delivered 1-31 Aug 86, based on reinstatement by 9 May 86. Reinstatement will be at the sole discretion of the Government." (R4, tab 104, para. 3).

123. As a result of the partial termination for default, the PCO removed 114,000 cases of GFM from Appellant's plant so that it could be provided for use in the repurchase contract that had been awarded to RAFCO. (Tr. 1260-61). This was done because the MRE meat manufacturers were no longer producing MRE meat entrees. (Tr. 1260) At this point in time, the suppliers were manufacturing MRE 6 meat entrees, which had a different configuration than the MRE 5 entrees (5 oz vs. 8 oz). (Tr. 1260, 1271). The transfer of 114,000 cases of GFM meats from Appellant to RAFCO did not impact on Appellant's ability to complete the remaining 505,000 cases not terminated for default because Appellant had received sufficient GFM to complete the original contract quantity. (Tr. 1261). Consequently, after the removal, Appellant still had for all intents and purposes the necessary 505,000 cases of GFM. (Tr. 1261). The PCO did not remove any CFM from Appellant's plant, nor did the PCO ever contact any of Appellant's suppliers relative to diverting shipments to RAFCO. (Tr. 1261-64).

Performance Under Modification P00020's Schedule

124. On January 30, 1986, one day after the issuance of Modification P00020, Appellant ceased meal bag and case production due to the outage of CFM brownies. (R4, tab 194, p. 2, para. 3). This outage of CFM was not cured until February 10, 1986. (R4, tab 194, para. 1).

125. On or about January 15, 1986, Appellant submitted PP request 12 in the amount of $638,034. (R4, tab 107, subtab c). This was later revised to $623,371. (F232, subtab PP #12, p. 2). The only reduction taken was in the amount of $20,185, which represented excessive legal and accounting fees. (R4, tab 107). The Price Analysis applied a loss ratio factor of 95.18% against the total costs incurred and recommended a payment of $182,163. (R4, tab 107, subtab a). The ACO decided not to apply a loss ratio and authorized payment of $603,183 which was paid on March 4, 1986. (F-232, subtab PP # 12, p.3). On March 5, the Appellant was advised of the Government's concern and was asked to submit a revised breakdown of costs and an estimate to complete. (R4, tab 108). After this was accomplished the Government planned to establish a tiger team to review the information to determine Appellant's projected loss. (R4, tab 108).

126. On or about February 13, 1986, Appellant submitted PP request 13 in the amount of $1,002,223. (R4, tab 109, subtab c). DCAA did not

apply a loss ratio factor and recommended a payment of $984,507, after the disallowance of excess legal fees. (R4, tab 109, p. 1). The Price Analysis did apply a loss ratio factor (95.29%) and recommended a payment of $557,967. (R4, tab 109, subtab a). The ACO reduced the payment by the excess legal fees and withheld an additional $284,507 pending the results of the tiger team's review, (R4, tab 113), and a cheek in the amount of $700,000 was issued on March 13, 1986. (F232, subtab PP # 13). This represents the first PP in which the ACO gave consideration to Appellant's loss position. (Tr. 1547). The ACO advised Appellant that depending upon the results of the Tiger Team's review, payment of the outstanding $284,507 would be reconsidered. (R4, tab 113).

127. On March 19, 1986, Appellant submitted PP request 14 in the amount of $1,412,276. (See F232, subtab PP # 14, p. 4). Subsequently, on April 22, 1986, Appellant revised the PP request to $2,101,386. (F232, subtab PP # 14, p. 2). The April 22, 1986 revision reflected adjustments to subcontractor costs. (G-95). The payment review was conducted on the originally submitted request. (See R4, tab 117, subtab a). DCAA questioned costs of $358,262, which reflected 95% of the following costs: occupancy costs of $335,000 (racks and forklifts), insurance costs of $29,086 which had been previously submitted on several occasions, and excessive legal and accounting fees of $13,032. (See R4, tab 117, subtab

a, para. 6). DCAA did not apply a loss ratio factor and recommended a payment of $1,054,014 on the original submission. (G-14).

128. The Price Analysts recommended a payment of $437,090 based upon the application of a 95.29% loss factor against total costs incurred under the contract. (R4, tab 117). The ACO reduced the requested payment by the amount of questioned costs, then applied a loss ratio factor of 83.6% which was developed from Appellant's revised loss of $2.6 million. (Tr. 1549 – 51; F 127, p. 2, para. c). The loss factor was applied against the amount requested in the PP request rather than the total costs incurred, which resulted in more money being paid to Appellant. (Tr. 1549-51, 61). A check in the amount of $1,125,437 was issued on April 25, 1986. (F 232, subtab PP # 14, p. 1).

129. On or about March 21, 1986, Appellant submitted a claim for equitable adjustment. (See R4, tab 194, p. 7, para. 1). The Government originally attempted to settle the claim in March during a negotiation that included discussions of an extended delivery schedule, reinstatement of the terminated quantity and payment for certain capital equipment, but no resolution materialized at that time. (See R4, tab 194, p. 7, para. 1).

130. On or about April 14, 1986,[9] Appellant submitted PP request 15 in the amount of $791,264. (F232, PP # 15, p. 3). DCAA questioned costs of $15,789, which represented $1,134 for insurance and $14,655 for excess legal and accounting fees and recommended payment of the balance - $776,264. (R4, tab 118, para. 6). The Price Analyst used a loss ratio factor of 81.31% which resulted in a net overpayment ($1,391,046) of progress payments and therefore recommended $0. (R4, tab 118). The ACO reduced the requested payment by the amount of questioned costs, then applied a loss ratio factor against the amount requested rather than the total costs incurred under the contract. (Tr. 1561; F131, p. 2, para. c). A check in the amount of $615,824 was issued on May 20, 1986. (F232, subpara PP # 15, p.1). Had the ACO used the Price Analyst's loss ratio calculation instead of the modified calculation, Appellant's payment would have been $0. (Tr. 1561-62).

131. On or about May 6, 1986, Appellant submitted PP request 16 in the amount of $2,790,634. (R4, tab 120, subtab c). DCAA recommended payment of $1,112,883.00 (R4, tab 120). The difference of $1,677,751.00 which was not recommended consisted of:

a. prior period costs in the amount of $1,674,824.00 which included (i) re-submitted costs for progress payment request Nos. 14 and 15 which had not been paid, (ii) costs which had been previously disallowed or withheld

[9] Appellant submitted this progress before it submitted the revision to PP request 14.

resulting from the application of the loss factor

b. legal and accounting fees in the amount of $2,927.00 which were in excess of the amount negotiated.

(R4, tab 120, p. 2, paras. a and c). DCAA advised that it was currently evaluating Appellant's submitted estimate to complete in order to determine the extent of a loss factor, noting that the audit results were subject to that evaluation. (R4, tab 120, p. 2, para. b).

132. Prior to payment of this request, Appellant submitted a request for an adjustment to PP requests13, 14, 15, and 16 based upon Appellant's recalculation and application of the loss ratio factor. (F-135; Tr. 1565). In brief, Appellant proposed using a loss ratio factor of 88.73%. (F 135). Appellant calculated its proposed loss ratio factor by reducing the amount of its claimed cost. (R4, tab 135; Tr. 1566-1566). For purposes of calculating the loss factor, Appellant backed out all the costs that had been questioned by DCAA.[10] (Tr. 1566-57). This decreased Appellant's apparent loss under the contract and thereby increased its recovery of progress payment. (Tr. 1566-57). According to Appellant's submission, Appellant was entitled to $1,172,654, which included the amounts due under PP 16, as well as, the additional amounts Appellant believed it was entitled to for requests 13, 14, and 15. (F 135). The ACO accepted Appellant's loss ratio adjustment and authorized payment of $1,172,654

[10] Appellant still continued to include all the previously disallowed costs in its request for progress payments

and a check in that amount was issued on June 18, 1986. (F 232, subtab PP # 16, p. 1; Tr. 1566-67).

Modification P00025

133. Appellant failed to meet its April 1986 delivery increment by 7,073. (R4, tab 194, p. 11: Tr. 1350). The reasons for Appellant's failure to meet the delivery schedule include:

1. Three final assembly lots (88, 90 and 91) had been placed on medical hold, (R4, tab193, p.60), one lots (90) had not been released prior to the April delivery date. (R4, tab 193, p. 64). The reason for the medical hold was that Appellant had incorporated sub-lots of CFM into the meal bag assembly prior to AVI inspection. (R4, tab 193, p. 60).
2. On April 10, 1986, Appellant ceased final case production. (R4, tab 193, p. 62). Initially, Appellant elected to suspend final case production to enable the AVI to progress further on vendor sub-lot inspections of CFM, however, a stock outage of CFM maple nut cake occurred which forced Appellant to remain down until April 21, 1986. (R4, tab 193, p. 62, para. 3, p. 64, para. 3).

134. On or about May 2, Appellant submitted an unsigned draft letter to the PCO. (G-39, p. 5-8). The letter set forth an alleged agreement which

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which created the illusion that the requests were seeking significantly larger sums of monies than Appellant had incurred since the submission of the prior request.

Appellant purportedly entered into with DLA HQ. (G-39, p. 5-8). The PCO had drafted a response to the letter stating that he had no knowledge of or involvement in the alleged agreement and could not confirm the contents of the May 2, 1986 letter. (Tr. 1268, 1381). A copy of the draft was faxed to Frank Francois, a consultant for Appellant, at Mr. Francios' request. (Tr. 1267-68). Thereafter, Appellant advised the PCO not to formally respond to the March 2, 1986 letter; that it was being withdrawn. (Tr. 1268, 1381). The letter was subsequently formally withdrawn by Appellant's Counsel on May 15, 1986. (G-37).

135. On May 15, 1986, Mr. Thomas called Vice President Bush's office claiming that he had reached an agreement with DLA HQ, but that he could not get it in writing. (F-1, subtab 17). Mr. Chiesa, Executive Director Contracting at DLA HQ was asked to provide information to to Vice President Bush's staff concerning this claim. (F-1, subtab 17). In response to the allegation, Mr. Chiesa telephonically advised that the agreement that had been reached had been reduced to writing in the form of modification. (F-1, subtabs 17, 18).

136. Negotiations involving a new delivery schedule, waiver of Appellant's $3.4 million equitable adjustment claim, reinstatement of the terminated quantity and payment of capital equipment costs reconvened in May 1986

and resulted in the signing of bilateral Modification P00025. (R4, tab 11, tab 194, p. 10, 13-14; F131, p. 4, para. 5; R4, tab 119).

137. During the negotiation meeting held at DPSC on May 29, 1986, Appellant alleged that it had made a number of agreements with DLA that should be included in the settlement modification. Specifically, the agreements, ["side agreement"], Appellant claimed it had with DLA were:

1. If Freedom is otherwise qualified, DPSC will negotiate a fair and reasonable [MRE 7] contract with Freedom.
2. As appropriate DPSC and DLA will process a request for a guaranteed loan ...
3. Provide all reasonable assistance to Freedom in obtaining traypack and pouch contracts through the ... SBA.
4. Provide technical and production assistance to Freedom to rework and reprocess ... approximately 46,000 cases on medical hold.

(F-1, subtab 1).

138. Prior to the execution of the modification, Appellant indicated that it wanted the alleged side agreement to be part of the modification. (Tr. 1386). The PCO advised Appellant that there is no side agreement; there is no attachment to the modification; there is no addendum. (Tr. 1270, 1385- 86). The PCO refused to incorporate the alleged side agreement as he had not been involved in any of the discussions between Appellant's representatives and DLA HQ and he refused to rubber stamp something he knew nothing about. (Tr. 1270, 1387).

139. Appellant agreed to the modification as written and signed it without the incorporation of the alleged side agreement. (Tr. 1270). Because Appellant had initially wanted to attach the alleged side agreement to the modification, the PCO stressed the modification's language relative to the modification being a discrete agreement and that there was no side agreement. (Tr. 1270-71).

140. Under the modification, the Government agreed to reinstate the 114,758 cases that had previously been terminated for default, (R4, tab 119, p. 2 para. I(a). In bilateral Modification P00020, the parties agreed that this quantity may be reinstated, at the Government's discretion, if Appellant successfully completed the January through April 1986 delivery requirement. (R4, tab 104). In the instant case, Appellant had not successfully completed the January through April 1986 delivery requirement. (R4, tab 194, p. 11: Tr. 1350). However, the Government knew that Appellant could not survive on a contract of 505,000 cases; it needed the entire original quantity of 620,000. (Tr. 1351). The Government knew this because it had looked at forecast and conducted a financial capacity study in connection with the issuance of Modification P00020. (Tr. 1361; see also R4, tab 100, para. 9, 11). At that time, the Government realized that Appellant would be in financial jeopardy if it did not have the entire quantity of 620,000. Nonetheless, the Government needed to keep its supply position sound which required an immediate

repurchase. (Tr. 1361-1362, R4, tab 100). Hence, the Government partially terminated the contract, but for Appellant's benefit provided for the possible reinstatement in Modification P00020. (Tr. 1362, R4, tab 100).

141. The reinstated quantities were to be manufactured in the MRE VI configuration. (R4, tab 119, p. 2, para. I(a)). The change in configuration was due to the lack of MRE V components because there wasn't sufficient quantities of the 5 oz MRE 5 meat entrees in existence at this point in time. (Tr. 1271- 72). The MRE 6 meat entrées were for the most part 8 oz. (Tr. 1271). The change from 5oz entrees to 8 oz entrees did not impact on the size of the entrée's carton. (Tr. 1274). The cartons that contained the entrée bag were relatively the same size for the 5 oz bag as for the 8 oz bag. (Tr. 1274). The MRE (entrée) bag and the menu bag size did not change in MRE 6 – those bags were the same size utilized in MRE 5. (Tr. 1274). The anticipated savings to Appellant arising from the use of the 8 oz entrée in lieu of the 5 oz was approximated at $1.00 per case. (Tr. 1272-73; R4, tab 131).

142. Under Modification P00025, the Government also agreed to pay $399,111 to cover various listed capital expenditures which were allowed to be expensed under the contract. (R4, tab 119, p. 3, para. 2). In establishing the amount of the lump sum payment, the Government

reviewed Appellant's cost data and determined that there was a total of $522,218 in costs that could be considered capital in nature, and from this amount, subtracted $123,107, which sum represented the total amount the ACO had already paid for these costs. (See R4, tab 194, p. 14). The difference of $399,111 was paid to Appellant in full, not at 95% by check dated June 13, 1986.[11] (F 232, subtab Mod 25 Payment[12]).

143. Under the modification, the Government agreed to extend the delivery schedule as follows:

1-30	May	65,000
1-30	June	85,000
1-31	July	80,000
1-31	August	80,000
1-30	September	80,000
1-31	October	50,000

(R4, tab 119, p. 3, para. 1(c)), and to rescind the $200,000 consideration for modifications P00018 and P00011 and upwardly adjust the contract price. (R4, tab 119, p. 3, para. 4).

[11] The payment for the capital equipment expenditures resolved a long disputed issue relative to Appellant's claim that, prior to award, it had proposed and the Government had agreed that it would pay PP on certain capital equipment expensed under the contract. Mr. Marra, Appellant's accountant, testified that he understood this to be the case because during negotiations, the Government had agreed that all costs were direct. (Tr. 190). Mr. Marra also testified that he had specifically asked if costs were properly incurred on this contract was the Government going to give a 95% progress payment?" and the answer was yes. (Tr. 191).

[12] This subtab is located between subtab PP # 15 and PP # 16).

144. Appellant agreed to withdraw its ASBCA appeal, docketed as ASBCA No. 32570 with prejudice, (R4, tab 119, p. 2, para. 1(b)), and further agreed to waive

> all claims for all happenings and/or occurrences which have arisen to date under law and/or relating to the contract DLA13H-85-C-0591, except for any claims that may have arisen from the manufacturing of contractor furnished material by Star Food Processing under Government specifications: MIL-B-44057A, MIL-B-44066A, MIL-F44067A. Both parties have had counsel. Both parties expressly state that the aforesaid recitals are the complete and total terms and conditions of their Agreement and that this Agreement has been entered into free from duress or coercion.

(R4, tab 119, p. 4, para. 5). The reserved claim relative to CFM arose due to the medical hold placed against certain CFM produced by Star as a result of the discovery of micro-holes in product produced by Star. (See R4, tab 93, p. 52). During MRE 6, micro holes were discovered in a number of retort items produced by Star (both CFM and GFM) and as a result, Star product at the assembly plants was put on medical hold until it was inspected and cleared by the AVI. (Tr. 1255-56, 1488, see also R4, tab 194, 52). Freedom had a number of finished lots that it could not ship until the medical hold was lifted. (R4, tab 194, p 52-65). The placement of a hold on finished cases did not impact the assembler's production, only its ability to ship and get paid for the product, however, the placement of a medical hold against bulk lots (product not yet incorporated in finished cases) could impact on an assembler's production. (Tr, 1255-56, 1484). To remedy this situation, the PCO authorized substitutions of GFM for CFM as well as GFM. (Tr. 1255-56, 1484). The PCO viewed this as a

production problem and like any other production problem if the defective product was provided as GFM, the Government was responsible, if the defective product was CFM it was a contractor problem. (Tr. 1256, 1484-85). In order to clear a lot from medical hold at the assembly level, a visual inspection was conducted at the assembly plant, in most cases by the AVI. (Tr. 1257). In instances where holes were found, samples from the lot were sent to Health Service Command for zyglo testing. (Tr. 1257).

145. By letter dated May 30, 1986, Mr. Chiesa responded to a letter, dated May 13, 1986. (F 1, subtab 133). The letter, which set forth certain commitments DLA HQ purportedly agreed to, had been faxed to him the day before by DPSC[13]. (F1, sub tab 133, p. 1). In response to the letter, Mr. Chiasa advised that the May 15, 1986 letter was basically the same as a May 2, 1986 draft letter, addressed to the PCO, that he had already commented on to Mr. Francois and Appellant's attorney, Mr. Lambert. (F1, sub tab 133, p. 1). Mr. Chiesa advised that the agreement DLA reached with Appellant had been encompassed in whole and in its entirety in Modification P00025. (F1, subtab 133, p. 1). Mr. Chiesa further advised that:

> 1. DLA never agreed to negotiate an MRE 7 assembly contract with Appellant, but as an approved IPP producer, Appellant would be solicited in the upcoming MRE 7
> 2 DLA never agreed to process a loan request in accordance with the conditions listed in the letter, but putting aside the conditions, DLA was willing to process a guaranteed loan request expeditiously

[13] Mr. Chiesa believed the fax came from the PCO, Frank Bankoff. However, the PCO testified that he never faxed the letter; he believed that perhaps Bob Appellian did. (Tr. 1387).

3. DLA would provide the same assistance to Appellant as it would to any other contractor relative to obtaining SBA 8(A), and
4. DLA would be willing to provide technical assistance related to Appellant's rework effort if it is clearly in our interest, the same as for any other contractor.

(F1, sub tab 133).

146. Thereafter, Mr. Thomas wrote to Mr. Chiesa acknowledging the fact that the "side agreement" was not part of Modification P00025, and seeking a confirmation that DLA would take action on various commitments. (F-139). The commitments that Mr. Thomas sought confirmation of were the same ones that Mr. Chiesa had already addressed in May 30, 1986 letter. (F-139). Mr. Thomas further confirmed that the modification did not include the side agreement on August 22, 1986, when he and Mr. Francois met with General Russo, Director of DLA, to discuss the issues that were still "outstanding" after the execution of Modification P00028. (See G-45). The issues included a number of the provisions of the "side agreement". (G-45).

Performance under Modification P00025's Schedule

147. On June 2, 1986, Appellant requested that the PP limitation of $13,000,000 be increased and based upon incremental deliveries of 50,000 cases as follows:

Present limit	200,000 cases	$13,000,000
Increment	50,000 cases	1,000,000
Increment	50,000 cases	1,000,000
Increment	50,000 cases	1,000,000

Increment	50,000 cases	337,937
Maximum (95% x $17,197,828)		$16,337,937

(R4, tab 123). The PCO was willing to raise the PP ceiling to $15,800,000 as follows:

Deliveries	Cases	PP Limit
Through June	330,242	$13,000,000
July	80,000	1,000,000
August	80,000	1,000,000
September	80,000	800,000
October	50,000	

(See R4, tab 131). The $15,800,000 ceiling proposed by the PCO represented 95% of the contract price based on an adjusted contract value of $16,683,823. (R4, tab 131). That value took into consideration the fact that Appellant had been allowed the full payment of $399,111 rather than payment of 95% and the fact that the cost of the MRE 6 GFM was approximately one dollar per case less than the MRE 5 GFM. (R4, tab 131).

148 Appellant was not satisfied with the ceiling or the schedule for the incremental increases as proposed by the PCO and by letter dated June 26, 1986, Appellant requested that the ceiling be raised to $16,000,000 as follows:

Deliveries	Cases	PP Limit
Through May	245,242	$13,000,000
June	85,000	1,000,000
July	80,000	1,000,000
August	80,000	1,000,000
September	80,000	
October	50,000	

(R4, tab 130, p. 2). Appellant's proposed schedule for the incremental increases in PPs was not acceptable to the Government. (R4, tab 131). The PCO explained that additional PPs must be tied to contract performance to maintain Appellant's contract financing and uninterrupted production and ensure contract completion and liquidation of outstanding PPs. (R4, tab 131).

149 On or about June 12, 1986, Appellant submitted PP request 17 in the amount of $3,453,700. (R4, tab 136, subtab c). Although the request was in the amount of $3,453,700, Appellant's cover letter indicated that the maximum balance eligible for PP was $1,572,097. (F232, subtab PP # 17, p. 4). DCAA questioned prior period costs in the amount of $2,274,313, and current period costs of $66,274, which included excessive legal and accounting fees of $18,774 and lease of equipment costs in the amount of $47,500, which had been recovered in prior PPs. (R4, tab 136(a), para. 6). DCAA did not apply a loss factor and recommended a payment of $1,505,825. (R4, tab 136). The Price Analyst did apply a loss ratio and recommended $0. (R4, tab 136, sub tab a). The ACO reduced the payment by questioned costs and applied a modified loss ratio against the amount requested to arrive at $1,325,327. (Tr. 1568). A check in the amount of $1,325,327 was issued on July 15, 1986. (F232, subtab PP # 17, p. 1).

150. Appellant did not meet its June 30, 1986 delivery date until July 10, 1986, (R4, tab 141, para. 4), leaving only 15 production days to make the July 31, 1986 delivery date. (R4, tab 141, para. 6; R4, tab 135). Because of the anticipated shortfall for July 1986, the PCO issued a notice on July 11, 1986, advising Appellant to cure its delinquency, as well as, its failure to supply timely reports and correspondence. (R4, tab 135).

151. On or about July 14, 1986, Appellant submitted PP request 18 in the amount of $3,124,274. (F 232, subtab PP # 18, p. 3). Although the request sought $3,124,274, Appellant's cover letter indicated that the balance eligible was only $1,054,612. (F232, subtab PP # 18, p. 4). DCAA recommended a payment of $42,895.[14] (R4, tab 142). DCAA questioned $3,081,329, which consisted of $2,069,612 for prior period costs, $23,750 for an equipment lease, and $987,967 as excess of the PP limitation. (R4, tab 142). The ACO determined the amount of payment as follows:

Partial increase in PP ceiling per Mod P28	$774,350	($1,000,000 x .77435 representing % of cases shipped, i.e. 61,948 out of a delivery increment of 80,000)
Amount remaining from prior ceiling	$ 42,895	
Maximum PPs payable as of 8/15/86	$817,245	
Less costs questioned by DCAA	$ 23,750	
Subtotal	$795,495	
X loss ratio	.8873	
Amount approved for payment	$704,068	

[14] The report was issued before the PP ceiling was increased in Modification P00028

A check in the amount of $704,068 was issued on August 19, 1986. (F232, subtab PP # 18, p. 1; Joint Stipulation 65).

152. On July 15, 1986, Appellant notified the Government that it would run out of jelly on July 16, 1986. (R4, tab 141, para. 8). Appellant asserted excusable delay by virtue of the lack of GFM jellies based on its belief that it had given the Government sufficient notice of GFM shortage via a June 30, 1986 wire which listed its GFM inventories. (R4, tab 141, para. 8). The Government informed Appellant that its June 30, 1986 wire was not considered notice of GFM shortage as this was not the purpose of the wire and the wire contained so many discrepancies in the inventory that it was meaningless. (R4, tab 141, para. 8). Moreover, prior to June 30, 1986, Appellant had been advised that it would have to make use of the jellies in its rejected cases or rework those cases toward the its July requirement. (R4, tab 141, para. 9). Appellant responded to the cure notice by letter dated July 23, 1986. (F-144). Appellant attributed its delivery shortfall in July to problems with its box erector and sealer and a lack of GFM jellies. (F-144). Appellant also advised of the status of its rework. (F-144).

153. Subsequently, Appellant reported a problem with the USDA inspection at Appellant's facility. (R4, tab 139). Specifically, Appellant advised that the USDA refused to inspect Appellant's product due to

Appellant's failure to pay monies owed. (R4, tab 139). Appellant felt that USDA's demand for payment from Freedom, NY was improper as the debts were incurred by Freedom Industries. Consequently, Appellant concluded that USDA's actions provide excusable delay. (R4, tab 139). The PCO informed Appellant that its citing excusable delay in this regard was premature as the USDA had not ceased inspections at that point in time and had even scheduled future inspections. (R4, tab 140).

154. On August 1, 1986, the PCO made a determination that it was in the best interest of the Government to extend Appellant's delivery schedule by 8 days due to the lack of GFM jellies. (R4, tab 141). Bilateral Modification P00028 issued on August 27, 1986 extending the delivery schedule 8 days as follows:

Line Item	Quantity	Delivery Date
0001KK	65,000	30 May 86
0001KM	85,000	30 Jun 86
0001KN	80,000	12 Aug 86
0001KR	80,000	10 Sep 86
0001KS	15,304	10 Oct 86
0001KT	64,696	10 Oct 86
0001KU	50,062	12 Nov 86

(R4, tab 144, p. 2, para. a). The modification also increased the limit on PPs as follows: completion and acceptance of 330,000 cs ceiling is $13 million, completion and acceptance of 410,000 cs ceiling is $14 million, completion and acceptance of 490,000 cs ceiling is $15 million, completion and acceptance of 570,000cs ceiling is $15.8 million. Appellant reserved no claims under the modification and in signing the

modification, Appellant specifically acknowledged that it had no claim resulting from the lack of GFM jellies during the period of July 16-28, 1986. (R4, tab 144, p. 2, para. b).

Appellant's Performance Under Modification P00028's Schedule

155. On or about August 26, 1986, Appellant submitted PP request 19 in the amount of $2,136,572. (F 232, subtab PP # 19, p. 3). The cost period for this request was 7/5/86 -8/7/86. (F232, subtab PP #19, p. 4). Although the request was submitted in the amount of $2,136,572, Appellant's cover letter indicated that the maximum eligible was actually for $1,222,585. (F232, subtab PP #19, p. 4). DCAA took exception to prior period costs totaling $1,286,932. DCAA also took exception to $31,165.70, which consisted of personal life insurance $1,306.25, excessive legal and accounting fees of $6,109.25, and capital lease of equipment in the amount of $23,750. (R4, tab 158). The payment of $200,219 represented the balance of 18,052 cases shipped against the 80,000 case delivery requirement due 8/12/86. The calculations were as follows:

$$\frac{18{,}052 \text{ cases}}{80{,}000 \text{ cases}} = .22565\%$$

$1,000,000 (PP increment per Mod. P28) x .22565 = $225,650 maximum amount payable.

(G-95; Tr. 1570). The ACO applied a 95% against the maximum payment and authorized payment of $200,219. (Tr. 1570). A check in that amount was issued on September 8, 1986. (F232,subtab PP # 19, p. 1).

156. On August 26, 1986, Appellant and Bankers leasing met with Dr. Wade, the Assistant Secretary of Defense, and other Government personnel to discuss the number of MRE 7 awards, the guaranteed loan, and Section 8(a) contracts. (See G-46). During the meeting, Dr. Wade advised Bankers that DoD would not support a guaranteed loan. (G-46). Because it later appeared that Appellant did not understand this position, Dr. Wade send Mr. Thomas a letter specifically stating that "As discussed with you ... the Department's policy is not to grant loan guarantees for purposes such as this. Further, we would not support enabling legislation." (G-49)

157. By letter dated September 2, 1986, Appellant requested that the Government eliminate the tie in between PPs and deliveries. (R4, tab 148). Appellant also requested a liquidation rate of 82.6%. (R4, tab 148). Appellant's request was denied by the PCO on September 15, 1986. (R4, tab 146). Throughout the contract period, Appellant had claimed that FI negotiated a liquidation rate 82.6% prior to award. Appellant's claim in this regard is based upon the fact that during the negotiations, FI presented a proposal that sought 82.6% and the Government did not object to this; therefore FI assumed the Government agreed to the rate. (Tr. 187, 189).

158. On or about September 3, 1986, less than a week after submitting PP request 19, Appellant submitted PP request 20 in the amount of $1,936,353. (F232, subtab PP # 20). The cost period for the request was the same as the period for request 19, i.e. 7/5 – 8/7. (F232, subtab PP # 20, p. 3). However, the units shipped were part of a different 80,000 unit increment. Although the contract restricted PP submissions to one every 30 day period, the ACO accepted the request in order to facilitate some payments to Appellant. (Tr. 1571). As the costs were essentially the same as those for PP request 19, no Government reviews were conducted. (G-95). The ACO computed the amount of payment as follows:

33,061 cases shipped out of 80,000 x 4132625% =	$413,262.50
less questioned costs of	$ 31,166.00
maximum amount payable	$382,096.50
x loss ratio factor	.8580
	$327,838.79
x PP rate	95%
Amount Payable	$ 311,477.00

(G-95; Tr. 1572; F-155). A check in the amount of $311,447 was issued on September 23, 1986. (F232, subtab PP # 20, p. 1; Joint Stipulation 65).

159. Less than two weeks after submitting PP request 20, Appellant submitted PP 21, dated September 25, 1986. (F 232, subtab PP # 21, p. 2). Although the request sought $2,399,374, Appellant's cover letter advised that the maximum payable was $1,093,342. (F 232, subtab PP # 21, p. 3). The cost period covered by the request was 7/6 -9/5/86. (F232,

subtab PP # 21). The request was subsequently revised on October 1, 1986 in the amount of $2,165,098. (R4, tab 162, subtab c). Appellant's cover letter indicated that the maximum payable was $1,222,585. (G-95, p. 6). The cost period for the revised claim was 7/5/86 –8/1/86. (See G-95, p. 6). The pricing review was conducted on the original request. (see R4, tab 162).

160. DCAA took exception to $231,157 in costs broken down as follows: lease of equipment in the amount of $423,750, insurance costs of $7,505, excess legal and accounting fees in the amount of $95 and excess over limitation $199,807. (R4, tab 162). The ACO's payment included credit for cases not delivered due to GFM outage. (Tr. 1573). Specifically, Appellant was given credit for an additional 13,600 cases that the PCO determined Appellant might have shipped if there had been no GFM outage. (Tr. 1572-73). The ACO computation is as follows:

467,978 cases accepted as of 10/2/86
+13,600 cases credited for stock outage of GFM items
481,578 total cases

71,576 cases accepted toward 10/10/86 increment = .894725 delivery % factor
80,000 cases due 10/10/86 increment

maximum amt payable = $894,725 ($1,000,000 per Mod 28 x .894725 delivery % factor)
- $172,838 previously paid against PP increment
= $721,887 amount payable.

(G-95; Tr. 1572-1573). The ACO did not reduce the amount by the costs questioned by DCAA. (Tr. 1572). A check in the amount of $721,887 was issued on October9, 1986. (Joint Stipulation 69).

161. By wire dated September 16, 1986, Appellant informed DPSC that it would be out of GFM crackers in ten days. (See R4, tab 156). On September 22, 1986, the PCO advised Appellant that the Government had supplied Appellant with all the crackers necessary for completion of all 620,000 cases, and that no crackers were shipped out as a result of the termination, therefore the Government has fulfilled its commitment. (R4, tab 156). The PCO concluded that assembler damage was the cause and that Appellant would be responsible for the replacing the shortage of crackers. (R4, tab 156).

162. By letter dated September 17, 1986, Appellant advised that it was unable to meet the September delivery increment because of the loss of production days due to the lack of GFM fruit, (5 days) and potato patty (4 days). (R4, tab 153; Tr.). Appellant also claimed reduced production due to the substitution of beans for potato patties, resubstitution of menu 10, USDA's refusal to let Appellant zone in-process cases, and a problem with Appellant pouch folder. (R4, tab 153). The fruit outage had occurred on August 22, 1986. (R4, tab 194, p. 26). As a result of the outage, Appellant was down until August 29, 1986 when it received a shipment of 216,000. (R4, tab 194, p. 26). At the time Appellant ceased assembly, it had approximately 60,000 units of fruit mix in salvage from previously rejected cases, however, Appellant had not taken any action to determine if the units were usable. (R4, tab 194, p. 26)..

163 By letter dated September 29, 1986, Appellant advised of a cash shortfall and informed the PCO that the shortfall would become "virtually unmanageable by the week ending October 10, 1986. (R4, tab 157). Appellant also informed the PCO that it would not be able to complete the contract unless the shortfall is corrected. (R4, tab 157). Appellant's proposed solution was the award of a follow on contract, MRE VII. (R4, tab 157).

164. Bilateral Modification P00029 issued on October 7, 1986 and extended the delivery schedule for one month as follows:

Line Item	Quantity	Delivery Date
0001KR	80,000	15 Oct 86
0001KS	15,304	15 Oct 86
0001KT	64,696	15 Nov 86
0001KU	50,062	5 Dec 86

(R4, tab 159, p. 2, para. A). The parties agreed that:

> In further consideration of the aforesaid extension of delivery schedule, the contractor for itself, it successors and assigns, releases and forever discharges the Government of and from all manner of action, causes of action, suits, proceedings, debts, dues, judgments, damages, claims, and demands whatsoever, in law or equity or under administrative procedures which, against the Government, the contractor ever had, now has, or may have for or by reason of any matter, cause or thing whatsoever arising out of award and performance of the subject contract to date, except claims relating to zyglo testing implemented in modifications P00024 and P00026 or monies due or to become due as payment for product delivered to and accepted by the Government.

R4, tab 159, p. 2, para. C).

165. Modification P00024, issued on May 14, 1986, made changes to specification MIL-P-44073A for Packaging & Thermoprocessing of Foods in Flexible Pouches, i.e. the retort items. (R4, tab 166). In essence, the modification required retorters to perform a visual examination for micro-leaks and a florescein dye (zyglo) test to detect the presence of micro-leaks. (R4, tab 116). On June 27, 1986, Modification P00026 was issued making several changes to the testing requirements set forth in Modification P00024. (R4, tab 127). The tests were conducted at origin – i.e. at the retorter's facility. (Tr 1257). Appellant did not begin its retorting operations until July 22, 1986 with the production of its first article for applesauce. (R4, tab 146, p.1).

Appellant's Shut Down

166. By letter dated October 22, 1986, Appellant advised the PCO that it had not yet received GFM beef slice, diced turkey, ground beef or ham slices. (R4, tab 161; Joint Stipulation # 68).

167. PP Request No. 22, dated October 20, 1986 sought $1,222,585. (F 232, subtab PP 22, p. 2). The following day, on October 23, 1986, Appellant ceased final case assembly and laid off 146 production workers. (F172, p. 1). Appellant advised that these actions were necessary because of severe inventory shortages/outages of CFM (chicken loaf, pouch stands) caused by cash flow problems as a result of the failure of

its financial institution to advance additional funding until it was assured that Appellant could be awarded a contract under MRE VII. (R4, tab 194, p. 35, para. e).

168. On October 24, 1984, the PCO authorized the following GFM substitutions: diced beef for diced turkey, beef stew for diced turkey, chicken ala king for ground beef, frankfurters for ham slices. (G 57 para. 2(c)). The PCO also authorized Appellant to use GFM ground beef for CFM chicken loaf. The PCO advised Appellant that the Government is not responsible for the lack of GFM since substitutions could have been arranged prior to Appellant's shut down. (G-57 para. 3). The substitutions authorized on October 24, 1984 resolved Appellant's GFM shortage problem to the extent that Appellant could assume product. On October 28, 1986, Appellant provided an inventory list of GFM on hand. (G-57, p. 4). The GFM Appellant had as of October 28, 1986, with substitutions, was sufficient to assemble at least 30,000 cases. (Tr. 1277). Appellant however did not start up its assembly lines

169. On October 24, 1986, Appellant advised that an additional 140 production workers had been laid off but noted that most of the laid off employees were expected to be recalled on November 3, 1986 to commence production of 12,000 cases of MRE 6. (F 183, p. 3, para. (g). Appellant gave the ACO the following reasons: (i) completion of rework,

(ii) completion of 505k cases, (iii) start up of MRE 5A, (iv) shortage of GFM (eventually covered by-substitutions), and (v) the need for an MRE VII contract. (F 1, subtab 21). Although Appellant had sufficient GFM to assemble at least 30,000 cases, Appellant did not commence assembly on November 3, 1986. Had Appellant commence production, the Government could have provided additional GFM to keep Appellant going until the contract quantity was completed. (Tr. 1396, 1482-83).

170. Due to the shut down, the ACO advised Appellant that to protect the Government's interest, he had to discuss the release of PPs with the PCO. (F 1, subtab 21, p. 1). Based on acceptance of a total of 500,364 cases, the ACO determined that the maximum amount payable under PP 22 was $208,915. (R4, tab 194, p. 37, para. k). Subsequently, owing to more cases being accepted, (512,462), the maximum amount payable under PP 22 increased to $327,893. (R4, tab 194, p. 38, paras. b, d). Thereafter, on November 5, 1966, the ACO telephonically advised Appellant that he was going to propose the suspension of PPs. (F 1, subtab 21, p. 2).

171. Appellant met with Government personnel on November 7, 1986 to discuss what would be necessary for Appellant to complete the contract. (Tr; R4, tab 185, para. 3). At that time, Appellant informed the Government that it would not be able to complete the contract due to the lack of funds as its financial backer would not provide additional monies

without the guarantee of an add-on MRE VII contract. (R4, tab 185, para. 3).

172 By letter dated January 15, 1987, Appellant advised that it would resume cracker and accessory sub-assemblies so that the assembly line can start producing cases of MREs no later than February 11, 1987. (R4, tab 168). While Appellant did resume limited production on its subassemblies from January 20 to January 27, 1987 it never resumed final assembly or geared up for full production.

174. By letter dated January 26, 1987, the ACO confirmed previous advice given to Appellant concerning the return of PP 22 and the possible suspension of PPs. (R4, tab 169). The ACO proposed suspension of PPs was based on Appellant's inability to:

a. Pay its costs of performance in the ordinary course of business.
b. Repay its of $2,383,322 from Bankers
c. Meet cash in advance requirements imposed by vendors for delivery of ordered materials.

(R4, tab 169). The ACO also noted Appellant's November 7, 1986 shut down and the fact that Appellant only had sufficient CFM on hand to support assembly of 6,000 to 8,000 cases. (R4, tab 169). Suspension of progress payments based on a contractor's failure to pay its bills in the normal course of business is authorized under the PP clause. (Clause 7-104.35(b), para. (c) at Appendix A). Appendix E of the DAR also authorizes suspension based on a contractor's failure to pay its bills where

such failure indicate the existence of an unsatisfactory financial condition which endangers contract performance. (G-1, Section E524.4).

The MRE VII Preaward Resurvey

175. In the November - December 1986 time frame, a resurvey was conducted in connection with Appellant's offer on the MRE VII assembly contract. (R4, tab 165). By letter dated January 30, 1987, Appellant disputed the, Government's negative preaward resurvey findings. (R4, tab 170). By letter dated February 4, 1987, the Small Business Administration declined to issue a Certificate of Competency with respect to the award of an MRE VII contract. (R4, tab 171; F-202). On February 11, 1987, Appellant contacted General Russo, the Director of DLA requesting that he overturn the negative preaward resurvey which conducted in connection with MRE VII. (See R4, tab 173). General Russo assigned an independent fact finding group to review the resurvey issue, as well as, the allegations Appellant raised about the ACO. (See R4, tab 173). The group found no basis to overturn the preaward resurvey recommendation and also found no basis to substantiate the allegations of improper treatment. (See R4, tab 173). The group found that the deportment of the ACO on the MRE V contract was both professional and proper rather than treating Appellant unfairly, the ACO gave Appellant every benefit of doubt in administrating the contract. (R4, tab 173).

The Termination

176. On February 25, 1987, the electrical power was shut off at Appellant's plant due to the non-payment of electrical bills. (See R4, tab 183, tab 185, para. 5.). Due to the concern for the Government property at Appellant's plant, the PCO requested that Appellant perform a physical inventory on all GFM components and to perform a final inventory report as described in paragraph H-5 (E) of the contract on February 27, 1987. (See R4, tabs 185, para. 5, 183 and 175). The request for a complete inventory was confirmed by wire dated March 5, 1987. (See R4, tab 183). In response to this request, Appellant advised that without electricity, it could not access the automated inventory records, see to do a physical inventory or open garage doors to ship out Government property if so desired by the Government. (R4, tab 185, para. 5).

177. On March 12, 1987, the power was turned back on at the Government's expense and the Government became the billing customer. (R4, tab 185, para. 5).

178. On March 3, 1987, the third and final MRE VII award was made to CINPAC. (R4, tab 185, para. 6). By letter dated March 11, 1987, the PCO requested that Appellant provide an acceptable delivery schedule for the contract balance and evidence that Appellant can comply with the schedule. (R4, tab 176;). Appellant responded by letter dated March 23,

1987. (See R4, tab 177). Appellant failed to provide a delivery schedule instead Appellant advised that it would provide a schedule if the Government would:

1. Negotiate a price increase based on delay and disruption
2. Pay Appellant's relocation costs
3 Agree to pay progress payments as long as Appellant is performing.

(R4, tab 177).

183. On March 26, 1987, Appellant telephonically informed the PCO that it would be evicted from its premises as of April 3, 1987. (See R4, tab 183, tab 185, para. 13).

184. Although the Government had turned the electricity back Appellant failed to perform the inventory requested on February 27, 1987. (See R4, tab 183). The Government was concerned with the possibly of theft as there was no security at Appellant's facility. (R4, tab 181). The Government was also concerned that the shelf life of its food components might expire before the Government could use them. (R4, tab 181). Consequently in order to protect and make use of the Government's property, the Government made arrangements to have the facility kept open so that Government personnel could perform Physical inventories. (R4, tab 183). The Government, (Army Veterinary Inspectors), performed the inventory on March 27, 1987 and began transferring the property. (See R4, tabs 183 and 181).

185. By letter dated April 6, 1987, the PCO advised Appellant that the allegations set forth in its March 23, 1987 letter were completely unfounded and its conditions were unacceptable. (R4, tab 177). Appellant was once again requested to provide a delivery schedule and advised that if no schedule was provided within 10 days, the PCO would unilaterally extended schedule. (R4, tab 177). By letter dated April 17, 1987, Appellant advised that in order for it to submit a meaningful schedule, the Government must first make restitution for an alleged breach relating to the payment of certain capital equipment. (R4, tab 179). Appellant again requested that the Government:

1. Negotiate a price increase based on delay and disruption
2. Pay Appellant's relocation costs
3. Agree to paid progress payments as long as Appellant is performing.

(R4, tab 179).

186. Because Appellant failed to provide a delivery schedule, the PCO issued Modification P00030 on April 23, 1987 unilaterally extending the delivery schedule as follows:

Line Item	Quantity	Delivery Date
0001KT	57,780	1-30 Aug 87
0001KU	50,062	1-30 Sep 87

(R4, tab 182; Tr. 4/57).

187. On April 28, 1987, Bankers conducted an auction at Appellant's facility and sold equipment that was necessary for the completion of the contract. (R4. tab 185, para. 14). The PCO attended the auction and found unacceptable Government property conditions. (R4, tab 185, para. 15). The PCO found property that was unaccounted for on any inventory. (R4, tab 185f para. 15). He also observed GFM and CFM components in the salvage area and secondary storage area. (R4, tab 183, P. 2, tab I85f, para. 15). Retort pouch items that had been determined unfit for human consumption and a possible health hazard, and placed on medical hold and for which the PCO had instructed Appellant by wire dated February 26, 1987, to dispose of, by destruction, were still on the premises, unattended and accessible to anyone. (R4, tab 183, tab 185, para. 15).

188. By letter dated May 1, 1987, the PCO advised Appellant that its failure to properly maintain and make available inventory records and to properly handle, administer and store GFM represented a breach of contract and that Appellant's current status and lack of equipment jeopardized the successful completion of the contract. (R4, tab 183). Appellant was further advised that unless it cured these conditions within 10 days and offered evidence that it could comply with the delivery schedule, the Government may terminate for default. (R4, tab 183).

189. By letter dated May 21, 1987, Appellant responded to the Government's cure notice. (R4, tab 184). Appellant did not address the conditions described in the cure notice, rather Appellant advised it may not be able to complete the contract due to the Government's unjust refusal to provide progress payments, and the Government's failure to include substantial start up capital costs in progress payments. (R4, tab 184). Appellant requested that the Government negotiate an equitable adjustment to the contract. (R4, tab 183). Appellant's response was not acceptable to the PCO, consequently, by letter dated June 22, 1987, the PCO terminated Appellant's contract for default for failure to perform inventory control requirements and failure to make progress. (R4, tab 186).

190. On May 1, 1991, Appellant submitted a certified claim in the amount of $21,959,311. (R4, tab 191). The claim was denied in its entirety on October 7, 1991. (R4, tab 192).

ARGUMENT

A. APPELLANT IS NOT ENTITLED TO AN EQUITABLE ADJUSTMENT

1. The Government Did Not Breach Its Duty To Cooperate

The Government took numerous actions to accommodate Appellant and its predecessor. For instance, the PCO authorized the substitution of GFM for CFM through out the contract period, (GPFF 144), granted a waiver and a deviation for Appellant's benefit. (R4, tabs 45, 86,), allowed delivery schedule extensions, (GPFF 80, 108, 122, 143, 154, 164), and allowed an increase to the PP ceiling (GPFF 154). Additionally, after Appellant's November 5, 1986 shut down, the Government forebeared, to its detriment, while Appellant awaited a decision on the MRE 7 awards. Likewise, the ACO took numerous in an effort to accommodate Appellant. For instance, he paid more than recommended by DCAA and the Price Analyst on many PPs. (GPFF 75, 76, 77, 79, 125, 126, 128, 130, 149, 151). He did not apply a loss ratio factor immediately after Appellant fell into a loss position, (GPFF 125), and when he did apply one, he used a modified version of the loss ratio formula which resulted in a higher payment to Appellant. (GPFF 130). Thereafter, at Appellant's request, he utilized a loss factor developed by Appellant wherein Appellant manipulated its costs so that it would receive a larger payment. (GPFF

132). The ACO also accepted and paid multiply PP requests (PP 19, 20, 21) during the same 30 day period.

a. The ACO Properly Withheld Payment of FI's PP 1

Appellant argues that since the ACO knew that FI was a small business, a first time assembler and had no other source of revenue that he should have immediately released payment of PP1. This argument ignores the fact that while the ACO knew all these things about FI, the ACO also knew that FI had financial backing from DDD , which backing was required for FI to qualify for the award. Additionally, the ACO knew that the Government never agreed to expense all FI's start up costs, necessitating FI to have its own resources to cover much of the expenses related to plant rehabilitation and equipment purchases.

Moreover, any claims Appellant may have had with regard to this issue are in the nature of delay claims. By operation of law, Appellant waived these claims in bilateral Modification P00011, and every bilateral delivery schedule issued thereafter. (GPFF 80, 108, 122, 143, 154, 164). Finally, FI's initial PP request 1, its first revised request of PP 1 and its second revised request of PP 1 are all fraudulent submissions. (GPFF 42, 43, 44)

b. The ACO Properly Ordered Audits

The ACO's request for a prepayment audit on FI's PP request 1 was proper given that FI had never have PP prior to the instant contract. Such action was in accordance with the DAR. (GPFF 45). After the audit on FI's PP 1,subsequent audits were requested because the ACO could not place any reliance on FI's submissions. This lack of faith in FI's submissions was due to the fact that FI routinely sought recovery of: (i) costs that were not booked, (ii) costs for which FI was not liable, (iii) costs that were incurred prior to award, (iv) costs that were excessive, (v) costs that should have been capitalized, (vi) costs that were unallowable under the DAR, and (vii) costs that were duplicative. Moreover, Appellant and its predecessor, FI, both routinely failed to pay its bills in the ordinary course of business. (GPFF 45). Under the circumstances, the ACO's actions were justified and proper under DAR Appendix E-521. (GPFF 84).

Moreover, the audits, in and of themselves, did not slow down the payment process. Delay in payments arose from Appellant's actions such as its failure to maintain a sound accounting system and controls, (GFPP 91, 92), its failure to secure and maintain financial capability, (GPFF 63), and its failure to perform in a timely manner. (GPFF 80, 108, 122, 143, 154, 164)

Furthermore, Appellant waived its delay damages in a multitude of bilateral modifications. (GPFF 80, 108, 122, 143, 154, 164)

c. The ACO Properly Suspended PP On February 6, 1985

The ACO's February 6, 1985 suspension of PPs was reasonable and in accordance with the DAR and applicable PP clause. both of which provide that PPs may be suspended Specifically Section E-524.2 of DAR, Appendix E provides:

> If unsatisfactory financial condition, or failure to make progress, endangering contract performance, as described in paragraph (c)(ii) of the clauses in 7-104.35 is found to exist, arrangements reasonably assuring contract completion without loss to the Government will be required in connection with the making of further progress payments and the making of other payments so long as progress payments are unliquidated. Within the meaning of paragraph (c)(ii) of the clauses in 7-104.35, performance of the contract includes full liquidation of progress payments. Further payments will be withheld so long as any progress payments remain unliquidated, only upon full consideration of all pertinent facts, and upon concluding that further payments will serve to increase the probable loss to the Government.

(GPFF 63). The ACO's actions were also justified under DAR Clause 7-104.35(b)(c) which provides:

> The Contracting Officer may reduce or suspend progress payments, ... whenever he finds upon substantial evidence that the contractor ... (ii) has so failed to make progress, or is in such unsatisfactory financial condition, as to endanger performance of this contract

(GPFF 63).

Moreover, Appellant has waived this claim in various bilateral modifications. (GPFF 80, 108, 122, 143, 154, 164).

(i) The ACO Did Not Ignore Preaward Determinations, Nor Did He Interfere With FI's Sources Of Financing

Firstly, the ACO did not ignore preaward determinations in suspending PPs in February 1985. FI was required to be financial capable of performing the contract as a prerequisite to award. Thereafter, FI was required to maintain financial capability at all times. (GPFF 63).

Secondly, the ACO did not interfere with FI's sources of financing. FI had no sources of financing. No financial institution was willing to deal with FI. Broadway Bank, which willing accepted an assignment from H. T. Foods, was not willing to accept a letter of assignment from FI. Bankers Leasing extended credit under the contract to H. T. Foods, but not to FI. (GPFF 59).

Likewise, no supplier or equipment manufacturer was ever willing to extend credit to FI even prior to award. All credit from suppliers and subcontractors was extended to H. T. Foods, not FI. For instance, Gemini Remodeling Corp. extended $500,000.00 credit to H. T. Foods, FI. Similarly, New Ventures Business Services, Inc. extended $2,000,000.00 credit to H. T. Food Products, not FI. Also, New Ventures Personnel Services, Inc. extended $75,000.00 in credit to H. T. Food Products, not FI.. (GPFF 58).

The fact that no company or financial institution would touch FI had nothing to do with the ACO. FI had in excess of $2 million in debt when the contract was awarded. The debt was owed primarily to DDD. On

behalf of FI, H. T. Foods requested that DDD subordinate its UCC 1 filing on accounts receivables so that new financing could be put into place. DDD refused to do this. According to Mr. Thomas, this refusal was detrimental to the refinancing of FI. Hence, FI was unable to get financing from any other financial institution due to DDD's refusal to subordinate, not because of any statements made by the ACO. (GPFF 60)

Thirdly, the four PP requests (FI's PP 1, 2, 3 and H. T. Foods PP 1) submitted prior to the reinstatement were all fraudulent submissions. (GPFF 42, 43, 44, 57, 67, 73)

Fourthly, any damages that Appellant would have incurred as a result of the suspension would be in the nature of delay damages. Appellant waived all delay damages in bilateral Modification P00011 and every bilateral delivery schedule issued thereafter. (GPFF 80, 108, 122, 143, 154, 164)

(ii) The Issue Of Direct vs. Indirect Costs Was Moot At The Time Of The February 6, 1985 Suspension Of PPs

The suspension was based upon FI's lack of financing not the lack of direct costs. (GPFF 63). When PPs were reinstated, indirect costs were paid. (GPFF 74). Moreover, as previously noted, FI had no right to recovery under the PP requests submitted prior to the reinstatement as all those requests were fraudulent. (GPFF 42, 43, 44, 57, 67, 73). Furthermore, Appellant waived all delay damages relative to this

suspension in bilateral Modification P00011 and every bilateral delivery schedule issued thereafter. (GPFF 80, 108, 122, 143, 154, 164)

(iii) The Government Properly Required FI To Demonstrate That It Had The Financial Capacity To Perform The Contract

Appellant's assertion that FI's spreadsheet were incorporated into the contract has no basis in law or fact. During the negotiations, FI was fully aware that the Government was not going to expense all its costs under the contract. FI was also fully aware that it needed outside financing. (GPFF 17). The requirement to have the financial capacity to perform is a continuing requirement. (GFPP 63).

Moreover, Appellant's claims in this regard have been waived. (GPFF 80, 108, 122, 143, 154, 164)

d. The ACO Did Not Require Novation Of The Contract.

Contrary to Appellant's assertion, the Novation was suggested and subsequently prepared by Neil Ruttenburg, FI's attorney. (GPFF 65). Moreover, Appellant's objection to the novation does not reconcile with the fact that FI had entered into commercial assignments which purported to assigned all its rights under the contract to H. T. Foods on at least two occasions prior to the novation. (GPFF 71). While those assignments may have been acceptable in commercial practices, they were not acceptable under the DAR.

In any event, any damages Appellant may have incurred in connection with the novation have been waived. (GPFF 80, 108, 122, 143, 154, 164)

e. FI's Failure To Accept GFM In A Timely Manner Was Due Solely To FI's Actions And Inactions.

Appellant's inability to accept GFM arose from Appellant's failure to gain full access to the facility until April 1985. (GPFF 38). In any event, Appellant waived all its alleged damages in connection with this issue in bialteral Modification P00011 and every bilateral delivery schedule issued thereafter. (GPFF 80, 108, 122, 143, 154, 164).

f. The ACO Did Not Interfere With FI's Equipment Financing

As discussed above the ACO did not interfere with FI's equipment financing as FI had no such financing. (GPFF 58). Moreover, any expectation FI had that the ACO would or should have rubber stamped its "story" regarding how PPs are administered is patently unreasonable, as FI's "story" (R4, tab 22, p. 3) is blatantly imprecise. (Compare FI's story with DAR appendix E and applicable PP clause). Furthermore, according to Mr. Thomas' sworn affidavit, FI never expected to see any PP money until March 1985, (GPFF 36), consequently any financing arrangement that FI made should have taken this into consideration. Likewise, only $333,333 in depreciation for $1.5 million of production equipment was

expensed under the contract, (F 17, Joint Stipulation # 21), consequently any financing arrangement that FI made should have taken this into consideration.

In any event, any damages incurred by Appellant in connection with this issue would be in the nature of delay damages, and Appellant waived all such damages in Modification P00011 and every bilateral delivery schedule issued thereafter. (GPFF 80, 108, 122, 143, 154, 164)

g. The ACO's Decision Not To Pay PP On Capital Equitable Was Proper

The ACO's nonpayment of the capital equipment cost was in accordance with DAR Clause 7-104.35(b) which provides that the contractor's total cost shall not include "costs ordinarily capitalized and subject to depreciation or amortization except for the properly depreciated or amortized portion .." (GPFF 74).

Appellant waived all claims relative to this issue in Modification P00025, (GPFF 142), Modification P00028, Modification P00029. (GPFF 154, 164). Moreover, Appellant has waived any delay damages that it incurred even prior to Modification P00025, by virtue of the bilateral delivery schedules set forth in previous modifications. (GPFF 80, 108, 122).

h. The ACO Properly Considered Suspension Of PPs In August 1985

Under the DAR, Appellant was required to maintain an accounting system and controls that were adequate for the proper administration of PP. (GPFF 92). DCAA properly found that Appellant's accounting system and controls were inadequate, (GPFF 89), and the ACO properly relied upon DCAA's determination in this regard.

Moreover, Appellant waived its claims in connection with this issue in the various bilateral Modifications issued under the contract. (GPFF 80, 108, 122, 143, 154, 164)

i. The Government Properly Required Appellant To Be Financially Capable Of Performance

The Government did not improperly impose additional financial obligations on Appellant. The Government required Appellant to be financially capable of performance in accordance with the DAR. (GPFF 63). Moreover, Appellant waived any claim related to this issue in various bilateral modifications. (GPFF 80, 108, 122, 143, 154, 164)

j. The ACO Made Proper Deductions And Complied Fully With The DAR And PP Clause

Appellant argues that the ACO improperly deducted $400,000 from PP 5.[1] Appellant's argument is unavailing. The $400,000 was a forgiveness of rent that Appellant had not paid to its landlord. Appellant however, had received (via fraud) PP monies for the rent which was forgiven. Moreover, any claim Appellant may have had in connection with this issue was waived in various bilateral modifications. (GPFF 122, 143, 154, 164).

Appellant further argues that the ACO wrongfully withheld payment PP 10 and 11 until Modification 20 was signed and PP 21 until Modification P00029. Appellant's arguments are again without merit. The ACO properly withheld payment until Appellant cured its default. The DAR and DAR Clause 7-104.35(b) allows for the suspension of PPs in the event the contractor fails to make progress as to endanger performance of the contract. Specifically Section E-524.2 of DAR, Appendix E provides:

> If unsatisfactory financial condition, or failure to make progress, endangering contract performance, as described in paragraph (c)(ii) of the clauses in 7-104.35 is found to exist, arrangements reasonably assuring contract completion without loss to the Government will be required in connection with the making of further progress payments ...

(GPFF 63). (GPFF 63). DAR Clause 7-104.35(b)(c) provides:

> The Contracting Officer may reduce or suspend progress payments, ... whenever he finds upon substantial evidence that the

[1] The ACO did not make the deduction until PP 8. (GPFF 103).

> contractor ... (ii) has so failed to make progress, or is in such unsatisfactory financial condition, as to endanger performance of this contract

DLAM 8105.1 at 32.593-8 similarly allows the ACO to stop payment of a PP in the event a contractor's progress is unsatisfactory. (G-4, p. 13).

Moreover, Appellant has waived its claim in connection with this issue in various bilateral modifications. (GPFF 122, 143, 154, 164).

k. DPSC Did Not Divert CFM From Appellant

The PCO did not divert any CFM[2]. (GPFF 123). During the Hearing, the PCO stated that he believes Appellant developed this notion because it did not understand the date of pack requirement in the assembly contracts. (Tr. 1263 –1264). The only conversations the PCO recalled having with Appellant's CFM contractors were a result of the CFM contractors calling him to complain about not getting paid. (Tr. 1263).

In any event, Appellant waived its claim relative to this matter in various modifications issued under the contract. (GPFF 143, 154, 164).

l. The ACO Properly Imposed 100% Liquidation

The applicable PP clause allows an ACO to reduce or suspend or liquidate PP at a higher rate when the contractor has failed to make progress so as to endanger performance, has so failed to make progress that the unliquidated PP exceed the fair value of the work accomplished,

[2] Interestingly, Appellant chose to support its unfounded allegation by relying upon a document that specifically denies any Government action or influence relative to Appellant's subcontractors and their

or is realizing less profit than the established profit. (GPFF 28). In the instant case, all three of these conditions existed at the time the ACO increased the liquidation rate.

2. Appellant Is Not Entitled To Increased Costs Due To Alleged Changes

a. All DD250s Have Been Paid Or Credited To Appellant

Mr. Ljutic, the termination contracting officer ["TCO"], testified that 28 of the disputed 33 payments were in fact made/credited to Appellant. (Tr. 1113-14, G-92; G-93, p. 18-24). In particular, the Government had no record demonstrating that it had paid or credited invoice # FNY0172, (Tr. 1118-20), FNY0245, (Tr. 1123), FNY0297, FNY0298, FNY0339. (Tr. 1126). In all other cases, the Government provided Appellant with the advice of payment for the invoice which showed when the payment was made, and how much was paid. (G-92; Tr. 1118-26).

Out of the 5 unpaid invoices, 4 would have been subject to 100% liquidation based upon the date of the invoices and the payment date of other invoices submitted for payment in that time frame. (G-92, p.2). Only one invoice, FNY0172 in the amount of $63,878.40 would have been liquidated at 95%. (G-92, p.2). Hence under the contract, Appellant would have realized an actual payment of $3,193.92 (5%).

Under the T4C settlement modification, Appellant settled all its disputes with regard to the five invoices which were never paid or never

---

support of Appellant for CFM. (G-31, p. 1, para. 4).

credited. (See Appellant's Exhibit 1, p. 11, copy attached). Since payment of the disputed invoices has been made and the payment issued settled via the T4C modification, Appellant has waived any breach claim it may have had. The only remaining claim relates to interest on the $3,193.40 payment Appellant should have received within 45 days (30 days plus 15 day grace period) of receipt of invoice FNY0172, dated June 20, 1986. Interest is a delay damage. Appellant waived all unreserved delay damages in Modification P00028, dated August 1, 1986 (GPFF 154) and again in Modification P00029, dated October 7, 1986. (GPFF 164).

b. Appellant Is Not Entitled To Delay Damages For Lack Of GFM

Appellant claims that it suffered delay damages through out the entire contract period due to lack of GFM. However, any delays incurred prior to October 7, 1986 have been waived in various bilateral modifications. (GPFF 80, 108, 122, 143, 154, 164). Any lack of GFM after October 7, 1986 was cured in a relatively short period of time (2 days) through substitutions. (GPFF 166, 168). Although Appellant received substitution authority on October 24, 1984, enabling it to assemble at least 30,000 cases, Appellant did not assemble any cases; rather it laid off 140 production workers. (PGFF 169). Appellant's lay off does not make sense, if Appellant did have sufficient CFM to complete the contract as it claims. On October 24, 1986, Appellant advised that it

intended to bring its personnel back to resume final assembly on November 3, 1986. (GPFF 90). Appellant however, did not bring its production people back and final assembly never reconvened. Appellant's actions do not reconcile with Appellant's claims concerning its CFM position, and any delay experienced after October 24, 1986 did not relate to the lack of GFM.

c. Additional Testing Requirements Were Not Improperly Imposed

Appellant claims that the Government changed the agreed to moving lot inspection and did not reinstate it until November 15, 1985. Appellant's contention fails to recognize that the Government has the right to revoke a contractor's "reliable" status under DPSCM 4155.5. In the instant case this occurred on September 3, 1985 in connection with Appellant's cracker production. (See R4, tab 64). In any event, Appellant waived all claims related to this issue in various bilateral modifications. (GPFF 80, 108, 122, 143, 154, 164)

Appellant also claims that it was required to perform zyglo (fluorescent dye) testing for a 6 to 8 month time period. Appellant's claim is without merit. The dye testing test was made a part of the contract via Modification P00024, issued on May 14, 1986. (GPFF 165). The testing requirement was directed toward the retorters, not the assemblers. (GPFF 165). Under the modification, retort items were to be inspected at origin – at the retorters facility. (R4, tab 165). Appellant did not begin its

retort operation until July 22, 1986 with the production of applesauce – first article. (R4, tab 21). The record doesn't indicate whether Appellant ever produced any additional applesauce under the contract. However, to the extent that Appellant did perform zyglo testing on any of its retort items, it has failed to demonstrate this. More correctly, Appellant has failed to allege that it performed zyglo testing on its own product, rather Appellant claims that it spent 6-8 months zyglo testing another retorter's products – Star's. Appellant has offered no explanation of why it would dye test Star's product or why it would conduct an origin inspection at a location other than the product's origin (Star's facility).

In brief, Appellant's claim fails for lack of proof. To the extent that some portion of Appellant's claim relates to the Star product that was on medical hole at Appellant's facility, this claim was waived in Modification P00028, because no more Star pouches were being placed on medical hold after the spring of 1986. (See R4, tab 192, p. 3). Moreover, no records have been produced to substantiate the claim, consequently, that claim fails for lack of proof also.

B. THE ACO'S ACTIONS DO NOT CONSTITUTE A BREACH

Appellant argues that the ACO's malice toward Appellant is apparent based on 1) the fact that the ACO took the actions addressed in section A of this brief, and 2) a statement that the ACO made wherein he indicated that he wouldn't deal with Henry Thomas, as a business man,

knowing what he does now. Appellant's arguments in this regard are wholly without merit. As discussed above, all actions taken by the ACO were justified under the circumstances and proper under the DAR and the applicable PP clause. Moreover, the ACO's expression of his opinion that he would not deal with Henry Thomas in a business setting, doesn't amount to a hill of beans let alone malice.

Appellant also argues that the ACO engaged in a conspiracy to get rid of Appellant. According to Appellant, the ACO was all powerful, and used his power to bring DCAA, the PCO, and DLA under his control so that he could destroy Appellant. This argument is not only meritless, its absurd and doesn't warrant further comment. Appellant's contentions that the ACO's tactics were designedly oppressive and that the ACO specifically intended to injure Appellant are similarly absurd and warrant no comment..

C. THERE IS NO IMPLIED-IN-FACT CONTRACT RELATIVE TO APPELLANT'S PARTICIPATION IN THE IPP PROGRAM

Appellant's Industrial Preparedness Agreement did not impose a requirement upon the Government to enter into a contract with Appellant. This is clearly stated on the first page of the IPP agreement that Appellant signed. (GPFF 2). Moreover, Appellant's participation in the IPP did not impose a continuing obligation on the part of the Government to enter into future Industrial Preparedness Agreements with Appellant. (GPFF 2).

D. MODIFICATIONS P00025 AND P00028 ARE VALID

In its Supplemental Brief, Appellant argues that Modification P00025 is invalid because (i) there was not any consideration, (ii) the Government breached the modification, (iii) the modification is unconscionable because it doesn't recognize the "side agreement" , and (iv) it was induced by fraud. These contentions are discussed in order below.

Modification P00025

Consideration

Contrary to Appellant's allegations the consideration given by the Government in Modification P00025 was not already due Appellant. Appellant had no right to have the terminated cases reinstated. Under Modification P00020, reinstatement was discretionary and conditioned upon Appellant meeting the January through April 1986 delivery increments. (GPFF 122). In the instant case, Appellant failed to meet the April delivery date. (GPFF 133). Hence, the extension in Modification P00025 was consideration.

Similarly, Appellant was not entitled to a delivery schedule extension based solely upon excusable delay. Among other reasons, Appellant had stock outages of CFM. (R4, tab 133).

Likewise, Appellant was not due payment of $399,111 for capital equipment expensed under the contract. Firstly, there was never any

agreement that Appellant would be able to receive PP on these costs. (PGFF 18). Secondly, Appellant was paid this outstanding capital equipment costs at 100%, not the 95% it would have received had it recovered the costs through PP. (PGFF 142).

Also, Appellant was not entitled to reimbursement of its previously paid consideration due to Government caused delay. Modification P00011 was issued due to Appellant's failure to deliver caused by Appellant's lack of financing. Modification P00018 was issued because Appellant failed to meet the delivery schedule due to high rejection rates. (GPFF 110). Contrary to Appellant's assertion, Modification P00025 did not provide for a cash payment of the $200.000. The contract price was adjusted upward to reflect the addition of $200,000.

Breach

The Government did not breach the agreement. The delivery schedule was extended, the terminated cases were reinstated, the contract price was upwardly adjusted to reflect the addition of $200,000 previously paid for by Appellant for extensions, and Appellant was paid $399,111. (GPFF 140, 142, 143).

Side Agreement

Modification P00025 contains no set aside and no one in the Government ever led Appellant to believe that it did. (GPFF 137, 138, 139). Appellant's contention that the Government misrepresented the scope of the modification is contrary to:

1. Both parties have had counsel. Both parties expressly state that the aforesaid recitals are the complete and total terms and conditions of their Agreement and that this Agreement has been entered into free from duress or coercion. (GPFF 144).
2. Appellant's allegations in its mal practice case against its attorney, Mr. Lambert, wherein Appellant claimed that Mr. Lambert, not the Government, led Appellant to believe that the side agreement was included in the modification. (R4, tab 188).

3. Appellant's letter to Mr. Chiesa acknowledging the fact that the alleged side agreement was not part of the modification. (GPFF 146).

4. Appellant's letter to Mr. Gross wherein Appellant states that Mr. Lambert and Mr. Francois failed to represent the true negotiations. (R4, tab 88)

5. Appellant's letter to Mr. Francois wherein Mr. Thomas states that he is presently evaluating the "losses which flow directly from the advice provided by you to sign Modification P00025 and P00029... " (R4, tab 90).

Fraud

Appellant's allegation that Modification P00025 was induced by fraud on the part of the Government is contrary to:

1. Appellant's allegations in its mal practice case against its attorney, Mr. Lambert, wherein Appellant claimed that Mr. Lambert, not the Government, led Appellant to believe that the side agreement was included in the modification. (R4, tab 188).

2. Appellant's letter to Mr. Gross wherein Appellant states that Mr. Lambert and Mr. Francois failed to represent the true negotiations. (R4, tab 88)

3. Appellant's letter to Mr. Francois wherein Mr. Thomas states that he is presently evaluating the "losses which flow directly from the advice provided by you to sign Modification P00025 and P00029... " (R4, tab 90).

Modification P00029

Appellant claims that Modification is invalid because the Government failed to provide GFM, the modifications release does not bar Appellant's claim, the modification lacks consideration, and the modification was entered into under duress. These contentions are addressed in order below.

GFM

On October 24, 1986, the Government authorized substitutions sufficient to allow Appellant to assemble 30,000 cases. Appellant never resume assembly and never used this GFM. (GPFF 168, 169). Moreover, while the Government was responsible for providing GFM under the contract, GFM was not part of the modification's stated consideration.

Release

Appellant's contention that Modification P00029 only contained a general release in inaccurate. The release specifically reserved claims related to the zyglo testing requirements set forth in modifications P00024 and P00026. Hence, Appellant knew the significance of reserving its claims.

Consideration

The delivery schedule extension is proper consideration. The Government only charged Appellant $100 for the extension to cover the administrative costs of issuing the modification.

Duress

Appellant's allegations of duress are of no avail. At the time the modification was issued, Appellant's PP were not suspended. The PP ceiling had been increased, and all Appellant's capital equipment costs had been paid.

E. MR. THOMAS' TESTIMONY SHOULD BE GIVEN NO WEIGHT

The record reflects that Mr. Thomas has committed perjury either in connection with this Hearing or in connection with the civil action involving his landlord. The sworn testimony given in the two actions is grossly contradictory. (See GPFF 33 – 40). It is apparent that Mr. Thomas submitted false testimony in connection with (at least) one of the proceedings.

F. APPELLANT HAS FAILED TO ESTABLISH ENTITLEMENT TO THE DAMAGES CLAIMED

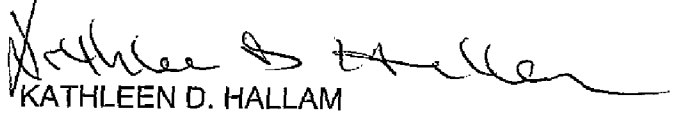
The Government's comments concerning Appellant's damages for the various elements of its claim are address in section A.

CONCLUSION

For the reasons stated above, Appellant's appeal should be denied.

Dated June 11, 2001

Respectfully Submitted



KATHLEEN D. HALLAM
Chief Trial Attorney

EXHIBIT 1

TERMINATION SETTLEMENT DOCUMENT

AMENDMENT OF SOLICITATION/MODIFICATION OF CONTRACT

1. CONTRACT ID CODE	PAGE OF PAGES
J	1 | 3

2. AMENDMENT/MODIFICATION NO.	3. EFFECTIVE DATE	4. REQUISITION/PURCHASE REQ. NO.	5. PROJECT NO. (If applicable)
A00004	See Block 16c	DOCKET L970002NN	

6. ISSUED BY	CODE	7. ADMINISTERED BY (If other than item 6)	CODE
S3310A		S3310A	

DCM NEW YORK
ATTN: DCMDE-GNTE
207 New York Avenue
Staten Island, NY 10305-5013
(718) 390-1300 James Ljutic

DCM NEW YORK
ATTN: DCMDE-GNOD/Attn:Marv Liebman (718) 390-1095
207 New York Ave.
Staten Island, NY 10305-5013

8. NAME AND ADDRESS OF CONTRACTOR (No., street, county, State and Zip Code)	(x)	9A. AMENDMENT OF SOLICITATION NO.
Freedom N.Y. Inc 420 East Martin Luther King Blvd. – Suite 100 Mt. Vernon NY 10550 Attn: Mr. Henry Thomas (914) 235-4811		9B. DATED (SEE ITEM 11)
	√	10A. MODIFICATION OF CONTRACT/ORDER NO. DLA13H-85-C-0591
CODE 7W118 FACILITY CODE		10B. DATED (SEE ITEM 13) November 15, 1984

11. THIS ITEM ONLY APPLIES TO AMENDMENTS OF SOLICITATIONS

☐ The above numbered solicitation is amended as set forth in Item 14. The hour and date specified for receipt of Offers ☐ is extended, ☐ is not extended.

Offer must acknowledge receipt of this amendment prior to the hour and date specified in the solicitation or as amended, by one of the following methods:

(a) By completing items 8 and 15, and returning _____ copies of the amendment; (b) By acknowledging receipt of this amendment on each copy of the offer submitted; or (c) By separate letter or telegram which includes a reference to the solicitation and amendment numbers. FAILURE OF YOUR ACKNOWLEDGMENT TO BE RECEIVED AT THE PLACE DESIGNATED FOR THE RECEIPT OF OFFERS PRIOR TO THE HOUR AND DATE SPECIFIED MAY RESULT IN REJECTION OF YOUR OFFER. If by virtue of this amendment you desire to change an offer already submitted, such change may be made by telegram or letter, provided each telegram or letter makes reference to the solicitation and this amendment, and is received prior to the opening hour and date specified.

12. ACCOUNTING AND APPROPRIATION DATA (If required)

ACRN: SG

13. THIS ITEM APPLIES ONLY TO MODIFICATIONS OF CONTRACT/ORDERS. IT MODIFIES THE CONTRACT/ORDER NO. AS DESCRIBED IN ITEM 14.

(x)	A. THIS CHANGE ORDER IS ISSUED PURSUANT TO: (Specify authority) THE CHANGES SET FORTH IN ITEM 14 ARE MADE IN THE CONTRACT ORDER NO. IN ITEM 10A.
	B. THE ABOVE NUMBERED CONTRACT/ORDER IS MODIFIED TO REFLECT THE ADMINISTRATIVE CHANGES (such as changes in paying office, appropriation date, etc.) SET FORTH IN ITEM 14, PURSUANT TO THE AUTHORITY OF FAR 43.103(b).
√	C. THIS SUPPLEMENTAL AGREEMENT IS ENTERED INTO PURSUANT TO AUTHORITY OF: FAR 52.249-2, Termination for Convenience of the Government (Fixed Price)
	D. OTHER (Specify type of modification and authority)

E. IMPORTANT: Contractor ☐ is not, ☒ is required to sign this document and return the ORIGINAL copy to the issuing office.

14. DESCRIPTION OF AMENDMENT/MODIFICATION (Organized by UCF section headings, including solicitation/contract subject matter where feasible.)

(a) This supplemental agreement settles the settlement proposal resulting from the Notice of Termination dated September 26, 1996, which completely terminated the fixed-price contract shown in block 10A above.

GROSS SETTLEMENT: $16,710,868.24
NET PAYMENT: $799,797.00

Except as provided herein, all terms and conditions of the document referenced in Item 9A or 10A, as heretofore changed, remains unchanged and in full force and effect.

15A. NAME AND TITLE OF SIGNER (Type or print)	16A. NAME AND TITLE OF CONTRACTING OFFICER (Type or print)
Henry Thomas - President	James Ljutic Termination Contracting Officer

15B. CONTRACTOR/OFFEROR	15C. DATE SIGNED	16B. UNITED STATES OF AMERICA	16C. DATE SIGNED
(Signature of person authorized to sign)	12/29/2000	BY (Signature of Contracting Officer)	12/29/00

NSN 7540-01-152-8070
PREVIOUS EDITION IS UNUSABLE

30-105

STANDARD FORM 30 (REV. 10-83)
Prescribed by GSA
FAR (48 CFR) 53.243

Exhibit 1

(b) The parties agree to the following:

(1) The Contractor certifies that all contract termination inventory (including scrap) has been retained or acquired by the Contractor, sold to third parties, returned to suppliers, delivered to or stored for the Government, or otherwise properly accounted for, and that all proceeds and retention credits have been used in arriving at this agreement.

(2) The Contractor certifies that each immediate subcontractor, whose settlement proposal is included in the proposal settled by this agreement, has furnished the Contractor a certificate stating (i) that all subcontract termination inventory (including scrap) has been retained or acquired by the subcontractor, sold to third parties, returned to suppliers, delivered to or stored for the Government, or otherwise properly accounted for, and that all proceeds and retention credits were used in arriving at the settlement of the subcontract, and (ii) that the subcontractor has received a similar certificate from each immediate subcontractor whose proposal was included in its proposal.

(3) The Contractor certifies that all items of termination inventory, the costs of which were used in arriving at the amount of this settlement or the settlement of any subcontract settlement proposal included in this settlement, (i) are properly allocable to the terminated portion of the contract, (ii) do not exceed the reasonable quantitative requirements of the terminated portion of the contract, and (iii) do not include any items reasonably usable without loss to the Contractor on its other work. The Contractor further certifies that the Contracting officer has been informed of any substantial change in the status of the items between the dates of the termination inventory schedules and the date of this agreement.

(4) The Contractor transfers, conveys, and assigns to the Government all the right, title, and interest, if any, that the Contractor has received, or is entitled to receive, in and to subcontract termination inventory not otherwise properly accounted for.

(5) The Contractor shall, within 10 days after receipt of the payment specified in this agreement, pay to each of its immediate subcontractors (or their respective assignees) the amounts to which they are entitled, after deducting any prior payments and, if the Contractor so elects, any amounts due and payable to the contractor by those subcontractors.

(6) (i) The Contractor has received $15,910,921.24 for work and services performed, or items delivered, under the completed portion of the contract. This total amount includes unliquidated progress payments in the amount of $1,634,082.99. The Government confirms the right of the Contractor, subject to paragraph (7) below, to retain this sum and agrees that it constitutes a portion of the total amount to which the Contractor is entitled in complete and final settlement of the contract.

(ii) Further, the Government agrees to pay to the Contractor or its assignee, upon presentation of a proper invoice or voucher, the sum of $799,947.00 arrived at by deducting from gross settlement of $16,710,868.24 (A) the amount of $1,634,082.99 for all unliquidated partial or progress payments previously made to the Contractor or its assignee and all unliquidated advance payments (with any interest), and (B) the amount of $0.00 for all applicable property disposal credits, and (C) the amount of $14,276,838.25 for all other previous payments made by the Government under this Contract, except as provided in paragraph (7) below.

(iii) The net payment of $799,947.00 in subdivision (ii) above, together with sums previously paid, constitutes payment in full and complete settlement of the amount due the Contractor for the complete termination of the contract and all other demands and liabilities of the Contractor and the Government under the contract, except as provided in paragraph (7) below.

(7) Regardless of any other provision of this agreement, the following rights and liabilities of the parties under the contract are reserved:

(i) All rights and liabilities, if any, of the parties, as to matters covered by any renegotiation authority.

(ii) All rights of the Government to take the benefit of agreements or judgments affecting royalties paid or payable in connection with the performance of the contract.

(iii) All rights and liabilities, if any, of the parties under those clauses inserted in the contract because of the requirements of Acts of Congress and Executive Orders, including, without limitation, any applicable clauses relating to: labor law, contingent fees, domestic articles, employment of aliens, and "officials not to benefit."

(iv) All rights and liabilities of the parties arising under the contract and relating to reproduction rights, patent infringements, inventions, or applications for patents, including rights to assignments, invention reports, licenses, covenants of indemnity against patent risks, and bonds for patent indemnity obligations, together with all rights and liabilities under the bonds.

(v) All rights and liabilities of the parties arising under the contract or otherwise, and concerning defects, guarantees, or warranties relating to any articles or component parts furnished to the Government by the Contractor under the contract or this agreement.

(vi) All rights and liabilities of the parties under the contract relating to any contract termination inventory stored for the Government.

(vii) All rights and liabilities of the parties under agreements relating to the future care and disposition by the Contractor of Government-owned property remaining in the Contractor's custody.

(viii) All rights and liabilities of the parties relating to Government property furnished to the Contractor for the performance of this contract.

(ix) All rights and liabilities of the parties under the contract relating to options (except options to continue or increase the work under the contract), covenants not to compete and covenants of indemnity.

(x) All rights and liabilities, if any, of the parties under those clauses of the contract relating to price reductions for defective cost or pricing data.

With respect to the paragraph at 7(i), a reservation is hereby incorporated for a re-negotiation and/or a re-computation of the loss ratio utilized in the agreement herein. Based upon the outcome of the contractor's ASBCA case # 43965 it is possible that the contract price may be adjusted upward. If the Request for Equitable Adjustment of the contract price results in an increase of the contract price, and the increase is properly quantified as being an increase resulting from Government caused cost overruns, this settlement will be adjusted in accordance with a revised loss ratio. A re-computation of the loss ratio may result in an additional net payment to Freedom.

The attached settlement memorandum signed by both parties clarifies the basis on which the settlement was agreed to and provides detailed loss computations as to how the settlement was agreed to. That memorandum is hereby incorporated as part of this modification.

MEMORANDUM OF AGREEMENT

Between Freedom NY Inc. and the United States of America (US Government)

This agreement settles the revised Total Cost Basis Settlement Proposal Dated January 18, 1999, as revised through October 31,2000 under Contract DLA13H-85-C-0591.

The contract was terminated for default on June 22, 1987 by Modification P00031. Freedom appealed the default to the Armed Services Board of Contract Appeals (hereinafter the "ASBCA" or the "Board"). The Board, by decision dated May 7, 1996 (ASBCA No. 35671) sustained the appeal and ordered the default converted to a termination for the convenience of the Government. On September 27, 1996, Modification P00032 was issued to effect the Board's conversion of the default termination to one for the convenience of the Government.

After receiving several extensions, Freedom submitted its Final Termination Settlement Proposal on December 18, 1997 on a total cost basis. The proposal presented total incurred costs plus profit and settlement expenses in the amount of $25,594,066.00, and sought a net payment of $9,688,464.00 after consideration of amounts previously paid.

A revised Final Termination Settlement Proposal was submitted by Freedom on January 18, 1999, which represented increased incurred costs, profit, and settlement expense. The total requested applicable credit towards unliquidated progress payments was also revised upwards by the contractor. The amount of $25,594,066.00 was revised to $25,906,426.00. The total net payment requested after considering previous payments was raised to $10,668,279.00 from $9,688,464.00.

At the time of negotiations and after the submission of the final termination settlement proposal, Freedom introduced new costs in the amount of $275,000 which were sought as compensation for property which the Government seized in 1987 prior to the original termination for default. Additionally a final negotiated agreement between Freedom and a subcontractor (Cadillac Products) in the amount of $64,318 was submitted after the submission of the final proposal. Freedom also sought payment of 5 unpaid invoices in the total amount of $246,947 as well as interest on those invoices in the total amount of $250,000. Lastly Freedom sought a credit of $116,527 (which the PCO had made provisions for) and an increase of $387,455 to that credit for seized contractor furnished material (CFM) which was sold to a 3rd party. All of these revisions to the proposal were introduced after submission of the final proposal. Thus at the time of negotiations the total proposed net payment was $11,641,071.

1. The Government agrees to pay to Freedom, upon presentation of a proper invoice, the sum of $799,947.00 arrived at by deducting from the total negotiated amount of $16,710,868.24, the amount of $14,276,838.25 for previous payments and the amount of $1,634,082.99 for unliquidated progress payments.

2. Freedom and the Government agree that the negotiated settlement finalizes the Contractor's entitlement for the following termination costs in the amounts set forth below as adjusted for loss in accordance with FAR 49.203 plus settlement expenses and credit adjustments.

	Proposed	Negotiated	Notes
Direct material	7,445,754	7,445,754	
Direct Labor	2,526,746	2,526,746	
Indirect Factory expense	7,032,904	7,032,904	
Other costs	862,316	862,316	
Gen. and Admin. Costs	4,679,213	3,593,672	1
Settlement with Subcontractor	64,318	64,318	2
Total costs	22,611,251	21,525,710	
Profit	3,359,493	0	3
Estimate to complete	1,499,489	1,435,171	4
Est. cost at completion	24,110,740	22,960,881	
Less Contract price		-17,197,818	
Loss		5,763,063	
Loss ratio 5,763,043/22,960,881 = .251			5
Recovery rate = 1-.251= .749			
Recovery rate X costs incurred	(.749) 21,525,710 = $16,122,756		
Line 9 of SF 1436 (incl. profit/ktr and adjusted for loss/Government	25,970,744	16,122,756	
Less previously invoiced	14,208,009		6
Less previously disbursed		14,315,451	6
		(38,612)	6
Total (line 11)	11,762,735	1,845,917	
Settlement expenses	300,000	226,113	7
Total	12,062,735	2,072,030	
Less unliquidated PP	1,310,138	1,634,083	8
Net payment	10,752,597	437,947	
Inventory disposal credit	116,527	116,527	9
Credit for seized progress payment inventory	275,000	151,614	10
Subtotal payment	11,144,124	706,088	
Payment of 5 invoices	246,947	246,947	6
Interest on the above 5 invoices	250,000	0	6
Credits to Government:	0	146,088	11
		7,000	12
Total net payment	11,641,071	799,947	

Explanatory notes:

1. General and Administrative expenses have been agreed to and settled by the parties in total for the amount of $3,593,672 with the two exceptions as noted below (see a.).

6

a. The two exceptions to the agreement on total General and Administrative costs are as follows: (1) The auditor questioned Freedom's claimed cost of $400,000 related to Freedom's relinquishment of a lease option. This issue is before the Board as part of Freedom's pending claim in ASBCA N0. 43965. Freedom intends to continue to pursue the matter before the Board. The termination settlement does not include any resolution of this issue; (2) The auditor also questioned Freedom's claim for interest cost in the amount of $484,890 as unallowable under DAR. Of that amount, Freedom is pursuing a claim before the Board in the amount of $313,236 for additional interest incurred by Freedom which Freedom alleges is due to the Government's failure to provide progress payment financing. This termination settlement does not provide a resolution of that $313,236 portion of the interest expense and that matter remains open at the Board for final determination. The Government does not believe that the interest related to the option was incurred or that the interest claimed is allowable and therefore believes that Freedom has no entitlement thereto regardless of the forum in which such costs are pursued. Freedom disagrees. The issues remain open at the Board for final determination.

The contractor's proposed G&A expense included legal costs totaling $338,471 for the firms of Quinn, Racusin, Ruttenberg; Alberi and Alberi; Barnett and Alagia; Neil Ruttenberg; and Saul, Ewing, and Remick. The negotiated agreement on the G&A, notwithstanding the reservation in a.(above), includes the compensation for all above legal expenses which were negotiated and finalized at $281,973. The agreement, notwithstanding the reservation in a.(above), on the amount of reimbursable G&A expense constitutes $1,085,541 in costs which the Government disallowed. Of that amount $1,039,043 was questioned by DCAA, and $46,498 was additionally negotiated between Freedom and the TCO (per contractor letter dated August 2, 2000). Total negotiated disallowed costs consist of $484,890 in interest charges, a $400,000 credit related to a lease option relinquishment, $7,200 in charitable contributions, $136,450 in unexplained costs, and a total of $57,000 in legal expense. The $57,000 in legal expense disallowance agreed to consists of $10,501 which the DCAA took exception to and $46,498 which was a negotiated decrement between the TCO and Freedom.

2. The subcontractor settlement with Cadillac Products Inc. was approved by the TCO as submitted by the contractor, despite its submission being over 2 years late and despite the contractor having failed to request an extension for its submission.

3. The contract is in a loss position. The profit is $0 and the incurred costs are compensated in accordance with a loss ratio formula as set forth in this memorandum.

4. The estimate to complete was previously negotiated and finalized. The subcontractor settlement with Cadillac Products Inc. has been deducted from the amount of $1,499,489 since it was included in the estimate to complete as material costs yet to be incurred. This resulted in a revised estimate to complete of $1,435,171.

5. Loss adjustment computations

6. Based upon the proposal, the total amount of $14,208,009 was invoiced by contractor for shipped product under the non-terminated portion of the contract. The 10 September 1999 DCAA Audit of all DD-250 invoices reflects only $14,178,870 in shipments and invoices. Failure of exact agreement on the amount of previous shipments notwithstanding, the contractor per law and regulation is being reimbursed on the basis of all his costs incurred, less previous payments, subject to the compromises and loss adjustment herein. Based upon the audit and reconciliation which was completed in May of 1999, by DFAS, Ohio, the total actual payments from contract funds after consideration is given to all recouped progress payments are $15,949,533.64. Of this amount $38,612.40 represented direct Government payments to 3rd parties (Con Edison, Mohawk Movers, and Wittek Development Corp.) These Government payments were related to the shutdown of Freedoms facility. As such, Freedom had received total compensation of $15,910,921.24 prior to the termination for Default in 1987. Freedom's internal records reconcile with the total amount received.

Freedom however has claimed that 33 invoices for shipments made were never paid during the contract's active life. That claim is pending at the ASBCA. The TCO maintains that the Government has a record of liquidation of progress payments covering 28 of the 33 invoices, 4 of which were recouped at 95% and 24 of which were recouped at 100%. The records were provided to Freedom twice in 1999 by the TCO. Furthermore the records were submitted as evidence to the ASBCA. Freedom contends the timing of payments, and therefore the liquidations, are critical to possible liability for prompt payment interest. The Government maintains that liquidations of progress payments were effected during the active life of the contract and has submitted dated records of the liquidations and payments to validate this. The Government further maintains that the Contractor had received funds in excess of shipments approximating $1.7 million and therefore whether or not a specific invoice was paid, liquidated against progress payments, or misplaced, that Freedom already had funds well in excess of amount of all invoices for shipped product. The Government maintains since the liquidation of 5 unpaid invoices would have been effected at 95% for one invoice and 100% for the other 4 invoices, Freedom would have received only $3,163 on account of the 5 invoices, and the balance would have been applied to unliquidated progress payments at the time of payment. Freedom maintains that for all intents and purposes the invoices were never paid in that the liquidation was effected only recently for the purposes of this settlement. The parties also disagree as to the Government's right to liquidate at 100% when Freedom was not in default.

This settlement incorporates payment of the remaining 5 invoices for which the Government can not locate a record of either payment or liquidation against outstanding progress payments. As such this settlement adds an amount of $246,947 to cover payment of invoices FNY 0172, FNY 0244, FNY 0247, FNY 0298, and FNY 0339. As consideration for the payment of the unpaid DD-250's within the net payment of $799,947 Freedom agrees to withdraw its pursuit of the principal amount of these DD-250's, from its appeal at the ASBCA. Freedom and the Government consider the demand for payment of the principal amount of these outstanding balances of DD-250's to be satisfied. This agreement does not affect Freedom's right to pursue its claim before the Board on account of delay and disruption, or any other impact on or entitlement under the contract, specifically including but not limited to the right to recover interest, which Freedom claims resulted from the late payment of invoices, including progress payment requests, or the recoupment of unliquidated

progress payments by the Government. The agreement not to include interest as part of the recovery under this termination settlement does not negate Freedom's right to pursue interest in another forum, nor does it affect the Government's right to deny it.

7. This negotiated agreement reflects total settlement expenses of $226,113. These expenses are the result of the termination, do not constitute proceeds of the contract and therefore are not subject to assignment under the assignment of claims provision of the contract.

8. In its original submission Freedom proposed the unliquidated progress payment amount of $1,697,593. In a revised proposal submission the contractor re-proposed the amount of unliquidated progress payments as $1,310,138. An additional credit of $387,455 was sought by Freedom as compensation for contractor furnished materials, which the contractor alleges the Government seized. The credit is in addition to a $116,527 credit to be applied by the Government related to the sale and disposal of contractor furnished assets (see note 9). The contractor claimed a total of $503,982 in CFM (contractor furnished materials) were seized; yet that the applied disposal credit was designated to be only $116,527.00. Thus the contractor sought the difference of $387,455 as an additional credit to unliquidated progress payments. The DCAA Auditor rejected the proposed adjustment to the unliquidated progress payments by Freedom. In an effort to provide a mutually agreeable compromise on an apparently otherwise irreconcilable issue, and in the interest of reaching a bi-lateral agreement, the contractor has agreed to utilize the unliquidated progress payment amount based upon the DFAS Audit and reconciliation performed in 1999 and dated May 18, 1999. That amount of $1,634,083 has been agreed to by the parties and is supported by the official Government record. The TCO confirmed the amount via a double check and revalidation by DFAS on October 20, 2000 in writing. Additionally, Freedom's proposed amount ($387,455) of compensation for alleged seized contractor furnished materials is hereby settled and agreed to in an amount of $193,727, representing ½ the proposed amount. The parties have agreed this credit is to be applied for the contractor's benefit as a credit towards what the Government believes are unsupported continuing vendor liabilities (see item #11). The agreement settles that issue of seized contractor furnished material by the Government.

9. A letter in the Government's file dated October 30, 1990 by Trial Attorney James D, Mirynowski indicates that the application of a $116,527.41 disposal credit was to be applied as a credit to the Contractor's unliquidated progress payments. As such the credit is applied here to the contractor's benefit. This is in accordance with the PCO's intention by letters dated 10 July 1987 and 26 October 1987.

10. At some time in 1987 it became clear to the ACO and PCO that performance on the contract had stopped and that the contractor had ceased operations and shipments. While the contractor alleges that the stoppage was Government caused, that issue has not yet been decided upon and is before the ASBCA as part of a Breach of Contract Claim against the Government. It is not an issue under a termination for convenience settlement. Based upon the facts of the case and certain ambiguous documentation, it is evident that the Government paid for certain inventory in the form of progress payments and that the contractor used certain progress payment money to purchase various equipment, tooling, and to make

facility adjustments. It is also clear that at the time of performance stoppage the contractor had not yet liquidated a balance of $1,634,082.99 in progress payments the Government had disbursed. In order to protect the Government's interest to the extent it could, the Government seized all Government furnished property to which it had clear title and ownership. In addition to seizing property to which the Government had title, the Government assumed title under the progress payment clause to the remaining contractor furnished inventory such as the food items sold to Sopako. The seizure of the contractor furnished inventory which was sold to Sopako and/or otherwise been disposed of has been resolved via a credit of $116,527 to the bottom line settlement (note 9) and a credit of $193,727 to continuing ongoing vendor liabilities considered doubtful by the Government. The parties have thus compromised on their respective positions regarding seizure of property and accounts payable (notes 8 and 11).

The Government and the contractor have furthermore negotiated and agreed to a bottom line credit of $151,614 as consideration for seized progress payment inventory. Thus the matter of credits arising out of property seized by the Government has been resolved via this settlement.

11. The auditor qualified his acceptance of the contractor's proposed costs, noting that $3,305,526 of vendor costs included in the contractor's proposal still had not been paid to the vendors by Freedom some 14 years after the incidence of the expense. Furthermore the contractor has not paid a substantial amount of Federal and State payroll withholding taxes ($526,048.00). The contractor included his "vendor accounts payable and unpaid taxes" as incurred costs in the Termination for Convenience proposal and seeks reimbursement for these incurred costs. This settlement includes all previously paid taxes by Freedom and $526,048.00 in unpaid taxes on account of Freedom tax liability. Disagreement between the TCO and Freedom regarding the validity of vendor accounts payable is resolved through concessions given by both parties in order to obviate the necessity of litigating an issue for which differing legal opinions exist. The issue has been negotiated and resolved by a credit to the Government in the amount of $146,088. While this agreement provides for the allowance of the costs incurred for taxes previously paid and currently owed, the total amount of allowable costs and, thus, the current net payment has been reduced by the adjustment for loss factor. There has been no attempt by Freedom to recover either additional penalties and interest that taxing authorities might impose, since such interest or penalties are not now determinable. Additionally it can not be determined here whether additional interest or penalties that might be imposed can properly be attributed to Government causes. The Government assumes no responsibility for such further potential liability regarding interest and penalties on unpaid taxes unless it can be shown that such additional liability was the fault of the Government. This matter is pending before the ASBCA in docket No. 43965. Additionally, in the event that Freedom is able to negotiate a reduced amount of tax liability which is less than the $526,048 of unpaid taxes allowed herein, the Government would have the right under FAR 31.205-41 to a refund of excess taxes specifically allowed herein, as adjusted by the loss ratio used to compute them herein. Accordingly, it is agreed that the payment made herein does not reach those issues and either party is free to pursue such issues at their discretion.

12. Credit per PCO letter dated October 5, 1986 for additional inspection costs incurred by the Government, which constitutes an unadjusted contractual change hereby agreed to and resolved.

3. The net payment in the amount of $799,947.00 in paragraph 1 above, together with sums previously paid, constitutes payment in full and complete settlement of the amount due the contractor for the complete termination of the contract and all other demands and liabilities of the Contractor and the Government under the contract for termination costs and settlement expenses. The concept of full and complete settlement does not negate the rights of the parties, as specifically reserved herein, to pursue their various positions in ASBCA No. 43965 or in any appeal from a decision therein.

4. This settlement includes a reservation of Freedom's right to a possible upward adjustment related to the re-computation of the loss ratio. Such a re-computation and upward adjustment of the termination settlement amount is dependent upon the Board finding that the contractor is entitled to an upward adjustment in contract price. The quantification of such an adjustment in contract price is to be determined by the Board and is related strictly to those increased contract costs experienced, or additional profits earned, by Freedom on account of Government causes entitling Freedom to an upward adjustment in contract price. Any possible or potential compensation by the ASBCA for damages, interest, or penalties is not part of an Equitable Adjustment of the Contract Price and is not to be considered in computing a revised loss or profit.

The items and elements settled here are explicitly compensated via the termination settlement. The intent of the parties is to avoid duplicate compensation under ASBCA docket 43965, for costs and elements of the settlement which have been settled under the termination for convenience as directed by ASBCA docket # 35671. Nothing in this agreement is to be a bar to the ASBCA in compensating or giving relief to Freedom for other matters not compensated herein, or for impacts on the contract not considered herein, if it determined that Freedom deserves such relief.

Freedom NY Inc.

Henry Thomas
President – Freedom NY Inc.
Date: _____

United States of America

James Ljutic
Termination Contracting Officer
Date: 12/29/00