

ARMED SERVICES BOARD OF CONTRACT APPEALS

Appeal of -- )  
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Motorola, Inc. ) ASBCA No. 51789  
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Under Contract No. DAAK20-84-C-0879 )

APPEARANCE FOR THE APPELLANT: Peter B. Jones, Esq.  
Jones & Donovan  
Newport Beach, CA

APPEARANCES FOR THE GOVERNMENT: COL Michael R. Neds, JA  
Chief Trial Attorney  
MAJ Karl W. Kuhn, JA  
MAJ Robert B. Neill, JA  
Trial Attorneys

OPINION BY ADMINISTRATIVE JUDGE JAMES  
UNDER BOARD RULE 11

After our decision on defective pricing liability in *Motorola, Inc.*, ASBCA No. 48841, 96-2 BCA ¶ 28,465, *aff'd*, *Motorola, Inc. v. West*, 125 F.3d 1470 (Fed. Cir. 1997), and remand, the parties failed to agree on the amount of damages. This appeal arises from the contracting officer's (CO) final decision demanding a \$888,995 reduction in the price of the captioned contract and denying appellant's alleged offset. We have jurisdiction of this appeal under the Contract Disputes Act (CDA) of 1978, 41 U.S.C. § 607. The parties agreed to submit the appeal on the record pursuant to Board Rule 11. The record consists of the "Consolidated Rule 4 File," derived from the Rule 4 files under ASBCA Nos. 46785, 48841, and 51789 and the hearing transcripts and exhibits G-1, G-2, G-6, G-7 and G-8 in ASBCA No. 48841.

FINDINGS OF FACT

1. Contract No. DAAK20-84-C-0879 (contract 879) is a fixed-price incentive contract that was executed by appellant, Motorola, Inc., and respondent, U.S. Army Communications & Electronics Command (CECOM) on 10 August 1984, with an effective date of 1 May 1984 (R4, tab 1, "BASIC" at 1).

2. Contract 879 incorporated, *inter alia*, DAR clauses: 7-104.29(a) PRICE REDUCTION FOR DEFECTIVE COST OR PRICING DATA (1970 JAN), which provided:

If any price, including profit or fee, negotiated in connection with this contract, or any cost reimbursable under this contract was increased by any significant sums because:

....

(ii) a subcontractor, pursuant to the clause of this contract entitled "Subcontractor Cost or Pricing Data" . . . or any subcontract clause therein required, furnished cost or pricing data which were not complete, accurate and current as certified in the subcontractor's Certificate of Current Cost or Pricing Data;

....

the price or cost shall be reduced accordingly and the contract shall be modified in writing as may be necessary to reflect such reduction . . . .

7-104.42(a) SUBCONTRACTOR COST OR PRICING DATA (1982 DEC), which required the prime contractor to require its subcontractors, prior to award of any subcontract exceeding \$500,000, to certify "that to the best of their knowledge and belief, the cost or pricing data submitted . . . is accurate, complete, and current as of the date of agreement on the negotiated price of the subcontract"; 7-104.39 INTEREST (1983 FEB), which required payment of "simple interest" at the CDA rate on any amounts payable to the Government from "the date due," defined as the earliest of four dates, including "the date of the first written demand for payment, consistent with this contract," until paid, and 7-108.1 INCENTIVE PRICE REVISION (FIRM TARGET) (1980 FEB) (R4, tab 1, "BASIC" at 186, 191).

3. CECOM sought to modify contract 879 to add raster display subsystems that were to be provided by Aydin Computer Systems Division (Aydin), an operating unit of the Aydin Corporation (R4, tab 1 at P00031; tr. 2/35-37).

4. In Aydin's 8 November 1985 Cost Proposal No. Q9510 for \$6,708,219 to Motorola for 13 avionic displays, general and administrative (G&A) costs were 45% of Aydin's proposed direct and overhead costs (R4, tabs 3, 5 at 6, 8; tr. 1/156-57).

5. In February 1986, the Defense Contract Audit Agency (DCAA) audited Aydin's November 1985 Q9510 Cost Proposal and its general ledger and January 1986 "Statement of Operations" containing its "Corporate G&A" cost (tr. 1/179-81). DCAA's 17 March 1986 audit report on the Q9510 proposal recommended accepting Aydin's proposed 45% G&A rate (R4, tab 5). DCAA first discovered the charge in Aydin's G&A costs called "cost of facilities" (COF) in early 1988 (tr. 1/31). Aydin's G&A costs included COF charges,

Account No. 5624, for each month in 1985 and 1986 (R4, tab 96 at A, C, C-1 to C-77, D to D-3-1).

6. In late 1985, Grumman Corp. awarded Aydin a major subcontract, which, according to Aydin's president, accounted for about 60% of Aydin's sales at that time and "sucked up" most of its engineering resources performing research and development (R&D) (part of G&A), with the effect of shifting R&D costs to the G&A direct and overhead cost base and lowering the G&A rate (R4, tab 116 at 4; tr. 2/232-34).

7. Aydin's comptroller believed that Aydin's bid and incurred G&A rates were "significantly out of whack" in about July 1986, so he issued a memorandum changing the bid G&A rate from 45% to about 30-35% (tr. 2/179, 181). Aydin's president had that memorandum withdrawn, on the belief that he could move employees from contract work to R&D and bring Aydin's G&A rate up to 45% (tr. 2/181-85, 224, 234-36).

8. In August-September 1986, Grumman terminated the Aydin subcontract for convenience, so that Aydin's engineers could again be applied to R&D (R4, tab 116 at 4; tr. 2/232-34).

9. On 24 September 1986, CECOM and Motorola agreed to a \$18,066,530 target price for Modification No. P00031 (P00031) to contract 879, including \$6,511,898 for the Aydin subcontract. The parties executed P00031 on 30 September 1986. (R4, tab 1, P00031 at 1, 11; tab 14 at 1).

10. Aydin Corporation's 30 September 1986 memorandum to its divisions stated that the corporation would charge a "Cost of Facilities" to its divisions, whose divisional G&A was to include the "Cost of Facilities" for all programs bid "except for the U.S. Government" (ex. G-6).

11. On 29 October 1986, Motorola awarded subcontract No. C-064 to Aydin for the raster display, the subject of P00031, for the "not to exceed" price of \$6,090,397, subject to downward negotiations (R4, tab 84 at P-1). On 24 November 1986, Aydin reduced its proposed price to Motorola for 13 display generators to \$6,089,095 due to CECOM scope changes (R4, tabs 69, 74).

12. To evaluate Aydin's November 1986 C-064 subcontract proposal, during the week of 27 February 1987 CECOM advised Motorola of Aydin's 45% G&A rate (tr. 2/60-61). Motorola accepted that 45% rate and used it during negotiations in March-April 1987, as did Aydin (R4, tab 79 at 2, 4-5; tr. 2/66-68).

13. Aydin's G&A rate was the ratio of its G&A costs to its "total factory cost incurred" (direct labor, manufacturing overhead, direct material, and the like) (R4, tab 29). As of 31 December 1986, Aydin's year to date (YTD) G&A costs were \$3,791,000, including \$897,200 for Aydin Corporation's COF, and Aydin's "total factory cost incurred"

was \$12,514,000, producing the 30.3% G&A rate ( $\$3,791,000 \div \$12,514,000 = .3029$ ) stated in Aydin's December 1986 Statement of Operations (R4, tab 29 at 13; tab 78 at 14; tab 139 at 4). If one deducts the \$879,200 COF from those G&A costs, the December 1986 YTD G&A rate was 23.1% ( $\$3,791,000 - \$879,200 \div \$12,514,000 = .2312$ ), 7.2% less than the 30.3% G&A rate set forth in Aydin's December 1986 Statement of Operations.

14. On 3 April 1987, Aydin and Motorola agreed upon the price of \$5,222,863 for subcontract No. C-064 (R4, tab 80 at 1, 6). At the agreed-upon 45% G&A rate, G&A costs were \$1,391,490 of the \$5,222,863 subcontract price (R4, tab 84 at K1, tab 93 at 5). Aydin signed a certificate of current cost or pricing data for the raster display quote Q9510 on 9 April 1987, stating that such data were accurate, complete and current as of 3 April 1987 (R4, tab 81).

15. We find that multiplying the 7.2% G&A rate element attributable to COF (finding 13) by Aydin's \$3,092,201 cost base for subcontract No. C-064, produces \$222,638, times the 13.77% negotiated profit rate (R4, tab 84 at K1) yields \$30,657 profit, for a \$253,295 increase caused by inclusion of COF in Aydin's G&A.

16. DCAA's 8 June 1993 memorandum to CECOM stated that the "appropriate baseline date" was 3 April 1987, when Motorola and Aydin agreed to subcontract No. C-064, and DCAA calculated a \$297,006 price reduction due to the undisclosed COF, including profit, by applying to total cost inputs the 8.5% difference between the 36.5% 1985 G&A rate excluding COF and the 45% rate including COF (R4, tab 24).

17. The CO's 5 August 1993 final decision demanded \$297,006 plus interest, *inter alia*, as a price reduction on P00031 under contract 879, due to inclusion of the "unallowable" COF in the price of Aydin's subcontract C-064 (R4, tab 25 at 2, 9). Motorola's appeal from that decision was docketed as ASBCA No. 46785.

18. DCAA's 9 December 1993 Audit Report No. 3791-92D42097009-S1 stated that its previous G&A rate adjustment included only Aydin subcontract costs. DCAA revised its calculations to include Motorola's mark-up costs negotiated for contract 879, and derived a \$452,486 price adjustment for the unallowable COF charge. (R4, tab 27)

19. On 10 April 1995, the CO issued a final decision which stated that defective cost or pricing data had been submitted in connection with P00031, and the Government was entitled to a \$798,504 reduction in the price of contract 879, due to both the COF charge and an allegedly overstated G&A rate (R4, tab 100).

20. Motorola appealed from that final decision to the Board, which was docketed as ASBCA No. 48841. The Board dismissed ASBCA No. 46785 as superseded. On 25 July 1996, the Board sustained the appeal in No. 48841 with respect to the actual G&A rate, and

denied it with respect to the COF charge. *Motorola, Inc.*, ASBCA No. 48841, 96-2 BCA ¶ 28,465, *aff'd*, *Motorola, Inc. v. West*, 125 F.3d 1470 (Fed. Cir. 1997).

21. The *Motorola* appeal was remanded to the parties, who were unable to agree upon the amount of the price reduction (R4, tabs 104-06, 109-10, 112-13, 116).

22. Appellant's 18 December 1996 letter to the CO alleged an offset with regard to the Grumman contract termination (R4, tab 106). In June 1998, Aydin contended to CECOM that "[i]f the unusual effect of the Grumman contract is removed from ACS's 1986 actuals, to account for the effect of the contract termination," the result would be to transfer \$642,000 from Aydin's 1986 cost base to its G&A pool, thereby increasing Aydin's 1986 G&A rate from 30.3 to 37.3%, and off-setting the overcharge. Aydin argued that the "existence and termination of the Grumman subcontract were facts existing as of the time that Aydin and Motorola agreed to the subcontract price"; that "Aydin's 30.3% G&A rate and its constituents were cost or pricing data [as] were the Grumman subcontract circumstances"; and that "[a]pplying those circumstances to the other data results in an increase in Aydin's G&A rate of 7%." (R4, tab 116 at 4) Such \$642,000 figure is not substantiated by any 1986 documents in the record.

23. On 2 September 1998, the CO issued a final decision in which he demanded a \$888,995 contract price reduction (\$452,486 principal, plus \$436,509 interest) due to inclusion of the COF, and denied Motorola's alleged offset (R4, tab 118). This timely appeal in ASBCA No. 51789 resulted (R4, tab 120).

24. The present record contains no evidence that Aydin's 1986 G&A rate of 30.3% did not encompass and reflect performance of the Grumman subcontract until August 1986 and the termination thereof in September 1986.

## DECISION

### I.

Regarding its defective pricing claim, respondent argues that: (1) the presumed natural and probable consequence of Aydin's undisclosed COF charge was an overstated subcontract C-064 price; (2) to determine the downward price adjustment for undisclosed cost or pricing data, "the critical comparison . . . is between the lower cost figures that the contractor failed to disclose and the higher figures upon which the government relied in agreeing to the contract price," *Unisys Corp. v. United States*, 888 F.2d 841, 845 (Fed. Cir. 1989); (3) there was an 8.5% difference between the 45% G&A rate used to price subcontract C-064 and a recalculated 36.5% 1985 G&A rate excluding COF; and (4) such 8.5% factor results in a \$452,486 overstatement in contract 879's price.

Appellant contends that: (1) the only defective pricing found in ASBCA No. 48841 was the undisclosed COF included in Aydin's actual 1986 G&A rate of 30.3%; (2) a price

reduction cannot be based on Aydin's proposed 45% G&A rate because that rate was not cost or pricing data, but only Aydin's "estimate"; (3) Aydin's 31 December 1986 G&A rate could not affect the prime contract price because such rate was not known until months after Motorola certified the cost or pricing data for P00031, on whose price Motorola and the Government agreed on 24 September 1986; and (4) the remedy for defective subcontract pricing arising under a fixed price, incentive fee type contract, like contract 879, subsequent to certification of the prime contract cost or pricing data, is to disallow the defective subcontract cost with a concomitant reduction to the final price.

In *Motorola, Inc.*, ASBCA No. 48841, 96-2 BCA ¶ 28,465, we held that Aydin's COF charge was cost or pricing data, the G&A cost information disclosed to DCAA was not understandable without explanation of how the COF charge was derived, and respondent relied on such information to its detriment. 96-2 BCA at 142,171. To determine the amount of defective pricing caused by such COF charge, we apply the "critical comparison" set forth in *Unisys Corp.*, *supra*.

The cause of defective pricing was the undisclosed COF charge, which was included in each of Aydin's G&A costs for each month in 1985 and 1986 (finding 5). In negotiating and agreeing upon subcontract C-064's price, Motorola accepted Aydin's proposed 45% G&A rate (finding 12) to compute the G&A costs negotiated for, and included in, subcontract C-064. Neither the \$5,222,863 subcontract price nor the negotiated G&A cost element therein was cost or pricing data, but both must be analyzed to arrive at the monetary effects of the defective COF cost or pricing data. Thus, we must analyze the extent to which the G&A costs and hence the price of subcontract C-064 were overstated because the undisclosed COF cost or pricing data were included in the negotiated G&A rate.

Our analysis of the 7.2% G&A rate differential, derived by comparing the reported December 1986 30.3% G&A rate including COF costs with our reconstructed G&A rate of 23.1% excluding COF costs, indicates that subcontract C-064's price was increased by \$253,295 (findings 13, 15). Since the defective pricing as of 3 April 1987 did not affect the original price of Modification No. P00031 negotiated on 24 September 1986, we do not apply prime contract mark-ups to the disallowed cost. *See* DAR 3-807.10(d)(3) or FAR 15.804-7(f)(2).

We hold that respondent has the right to disallow the \$253,295 cost element of contract 879 pursuant to its DAR 7-104.29(a) clause. We express no view on the effect of such disallowance upon the mechanics of determining the "total final price" of contract 879 pursuant to the DAR 7-108.1 clause.

## II.

The pertinent case-law precedents hold that a contractor may properly offset unintended errors in understating the original price against overstatements made in negotiations. *See Cutler-Hammer, Inc. v. United States*, 416 F.2d 1306, 1309-13, 189

Ct. Cl. 76 (1969); *TGS International, Inc.*, ASBCA No. 31120, 87-2 BCA ¶ 19,683 at 99,630 (contractor inadvertently failed to identify one elements of cost of re-warehousing to be performed by someone other than the named prospective subcontractor). However, when a contractor intends to understate a cost element of its cost or pricing data, and such element is not known by or disclosed to the Government before the parties agree on price, the contractor is not entitled to offset such intentionally understated data. See *United Technologies Corp.*, ASBCA No. 43645, 98-1 BCA ¶ 29,577 at 146,633, *aff'd in part, rev'd in part on other grounds, and remanded, United Technologies Corp./Pratt & Whitney v. Peters*, 215 F.3d 1343 (Fed. Cir. 1999) (table), see 1999 U.S. App. LEXIS 15490; *AM General Corp.*, ASBCA Nos. 48476, 51107, 99-1 BCA ¶ 30,130 at 149,049-50 (intentional understatements by amortizing non-recurring costs over increased projected sales base were “errors of judgment”).

In 1998, Aydin contended that if the “unusual effect of the Grumman contract” were removed from its actual 1986 costs, then \$642,000 would be transferred from Aydin’s 1986 direct and overhead cost base to its G&A pool, thereby increasing Aydin’s 1986 G&A rate from 30.3 to 37.3%, and off-setting the overcharge (finding 22). Appellant argues that Aydin failed to account for the effects of the Grumman subcontract in its final 1986 G&A rate, and hence appellant is entitled to offset a 7% G&A rate understatement against any overstated G&A cost arising from the undisclosed COF charge.

In ASBCA No. 48841, we found that the “auditor’s workpapers show the G&A rate for all of 1986 was recorded by Aydin as 30.3%” (finding 10), and held that “the Government has failed to prove the non-disclosure of Aydin’s data on its actual 1986 G&A rate.” 96-2 BCA at 142,171. Since Aydin disclosed its actual 1986 G&A data and rates to the DCAA, what then are the noncurrent, incomplete, or inaccurate cost or pricing data which Aydin failed to disclose, that form the basis for its alleged offset? Aydin argues that the “existence and termination of the Grumman subcontract were facts existing as of the time that Aydin and Motorola agreed to the subcontract price”; that “Aydin’s 30.3% G&A rate and its constituents were cost or pricing data [as] were the Grumman subcontract circumstances”; and that “[a]pplying those circumstances to the other data results in an increase in Aydin’s G&A rate of 7%.” (Finding 22)

But this argument is plainly fallacious. “Applying” the factual circumstances of the “existence and termination of the Grumman subcontract” to Aydin’s actual 1986 30.3% G&A rate can make no difference whatever, because the record contains no evidence that such 30.3% G&A rate did not reflect those “facts” of the existence and termination of the Grumman subcontract (finding 24). What Aydin appears to argue, then, is that to “apply” the Grumman subcontract circumstances means to hypothesize that the Grumman contract was neither awarded nor terminated. But such hypothetical “circumstances” are not factual, since the Grumman contract assuredly was awarded and terminated. Nor did such circumstances produce an unintended error of Aydin in compiling its actual 1986 G&A costs and rate, since such rate was current, complete and accurate, except for the overstated COF cost element. If any “error” occurred in the “circumstances” of the Grumman contract

award and termination, it was the error of Aydin's President to believe that "he could move employees from contract work to R&D and bring Aydin's G&A rate up to 45%" (finding 7). Such an erroneous management belief was not defective cost or pricing data, but rather was a judgment that cannot offset overstated cost or pricing data. *See United Technologies, AM General, supra*. Moreover, the \$642,000 cost effect on Aydin's actual 1986 G&A rate alleged in Aydin's offset hypothesis was not substantiated by any 1986 documents in the record (finding 22).

We hold that appellant is not entitled to off-set any underpricing of subcontract C-064.

### III.

In late 1999 respondent moved, and appellant cross-moved, for partial summary judgment regarding the period for which interest is payable for overpayments due to the submission of defective cost or pricing data under contract 879. Respondent argued that it was entitled to interest on the amount of defective pricing calculated in accordance with Pub. L. 99-145, § 934(a), which provided for interest on any overpayment due to defective cost or pricing data with respect to contracts entered into after 7 November 1985. Appellant argued that Pub. L. 99-145 did not apply retroactively to this August 1984 contract, and only interest under contract 879's DAR 7-104.39 INTEREST (1983 FEB) clause was applicable.

In December 2000, the Board granted appellant's motion, and denied respondent's motion for partial summary judgment, holding that any interest for overpayments arising from defective cost or pricing data under contract 879 must be charged in accordance with the DAR 7-104.39 INTEREST (1983 FEB) clause. *Motorola, Inc.*, ASBCA No. 51789, 01-1 BCA ¶ 31,233 at 154,154.

The DAR 7-104.39 INTEREST (1983 FEB) clause requires Motorola to pay "simple interest" at the semi-annual CDA rate on any amount payable to the Government. Such interest starts to run from the earliest of four specified dates, the second of which is pertinent to the facts of this appeal: "the date of the first written demand for payment, consistent with this contract." (Finding 2) *See Electronics & Space Corp.*, ASBCA No. 47539, 95-2 BCA ¶ 27,768 at 138,447 (unless a contract fixes the date for payment of an amount, recovery of interest under DAR 7-104.39 requires proof that "the Government made a written demand for payment of the amount of its claim, which established the 'date due' for the claim and started interest running under the definition of 'due' in paragraph (b)(2) of the [DAR] Interest clause").

On 5 August 1993, the CO first demanded payment of an amount alleged to be defective pricing due to inclusion of the COF in the price of Aydin's subcontract C-064 (finding 17). Appellant argues that that decision was "superseded and vacated" and cannot provide a basis for commencing interest liability. We disagree. In *Motorola, Inc.*, ASBCA

No. 46785, 95-2 BCA ¶ 27,645, we granted appellant's motion to exclude the issue of respondent's allegedly undisclosed G&A rate data because that issue was not included in the CO's 5 August 1993 decision, and so we lacked CDA jurisdiction to decide such issue. That decision did not supersede or vacate the CO's 5 August 1993 decision, or hold that such CO's decision could not trigger the running of interest under the DAR 7-104.39 INTEREST (1983 FEB) clause.

We hold that appellant shall pay interest, in accordance with the DAR 7-104.39 INTEREST (1983 FEB) clause, commencing 5 August 1993 on the principal amount of the cost disallowance of \$253,295.

We deny the appeal with respect to such \$253,295, and DAR 7-104.39 interest thereon, and sustain the balance thereof.

Dated: 11 October 2002

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DAVID W. JAMES, JR.  
Administrative Judge  
Armed Services Board  
of Contract Appeals

(Signatures continued)

I concur

I concur

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MARK N. STEMLER  
Administrative Judge  
Acting Chairman  
Armed Services Board  
of Contract Appeals

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EUNICE W. THOMAS  
Administrative Judge  
Vice Chairman  
Armed Services Board  
of Contract Appeals

I certify that the foregoing is a true copy of the Opinion and Decision of the Armed Services Board of Contract Appeals in ASBCA No. 51789, Appeal of Motorola, Inc., rendered in conformance with the Board's Charter.

Dated:

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EDWARD S. ADAMKEWICZ  
Recorder, Armed Services  
Board of Contract Appeals