

ARMED SERVICES BOARD OF CONTRACT APPEALS

Appeal of --)
)
Kelly-Ryan, Inc.) ASBCA No. 57168
)
Under Contract No. W911KB-05-C-0016)

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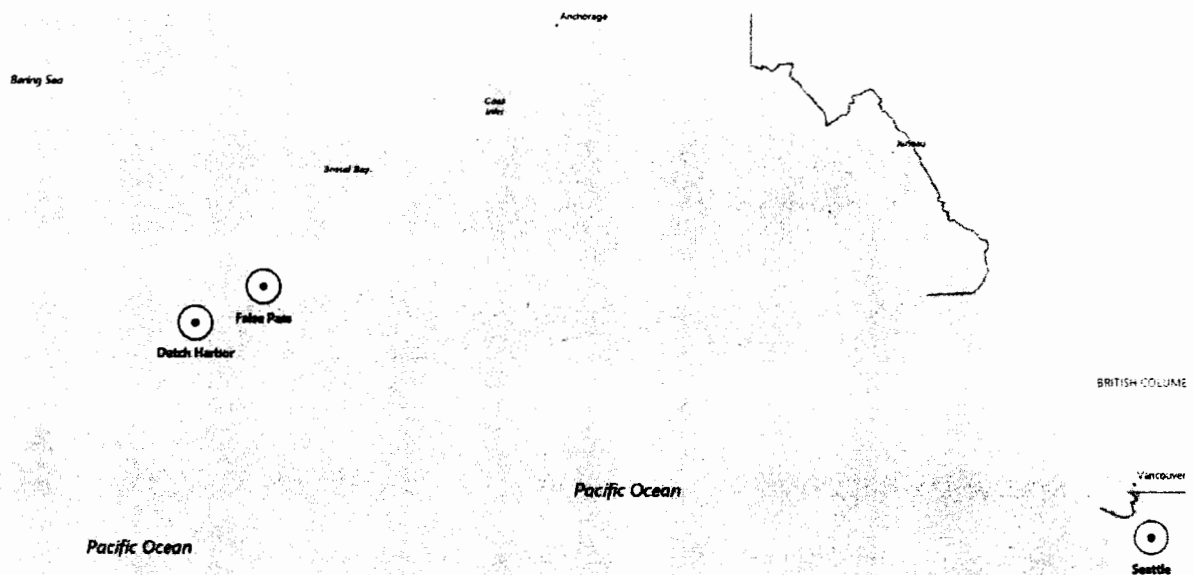
OPINION BY ADMINISTRATIVE JUDGE DICKINSON

This appeal arises from a contract awarded by the Army Corps of Engineers (government or Corps), to Kelly-Ryan, Inc. (appellant or KRI) to construct harbor improvements at False Pass, Alaska, in the Aleutian Islands. Both entitlement and quantum are before us for decision.

FINDINGS OF FACT

A. Background and Pre-Contract Matters

1. False Pass, Alaska, is located on Unimak Island in the Aleutian Islands. It occupies a remote, but strategic, location on the west side of the Isanotski Strait, the shortest transit route between the Gulf of Alaska and the Bering Sea. False Pass is 670 miles southwest of Anchorage, Alaska, and approximately 2000 miles from Seattle, Washington, the location of KRI's business office. (Compl. ¶ 70; tr. 9/10; finding 3)



False Pass was so remote that all crew, materials and equipment had to be brought in by barge. It took two-three weeks for a sea-going barge to make the trip from Seattle to False Pass. As a result of the remote location and time to transport items required to perform contract work, it was necessary to prepare “months instead of weeks” in advance. (Tr. 9/10)

[O]ne of the reasons it was such a big deal on this job is in Alaska generally and remote Alaska in particular, you’re way out in the Aleutians.... They’re very difficult and expensive to get to.

They have extreme winters, and the logistics of it required very careful planning because the Corps’ intent, and I think the contractor[’]s, in bidding on these, are trying t[o] do the jobs in as few...seasons as possible, because the mob[ilization] and demob[ilization] alone are so expensive.

(Tr. 7/49-51) Because False Pass was so far north, the work was seasonal, essentially six months of work followed by six months of winter:

[T]he Aleutians...[are] a different world.... [This is] the case with respect to the geography and sheer distances involved, regarding how weather is a daily concern, how unforgiving that part of the world is on equipment, vessels and people, and where getting to the nearest store can be akin to driving all the way across Texas for a package of batteries or a few groceries....

Contractors have to “hit the beach” with virtually everything they need and might need, [to] get the work done, and retreat at the onset of winter....

[C]ontractors face the...enemies of high winds, extreme tides, protracted periods of cold and wet weather, remoteness, and just plain tough dangerous conditions.... The television series *The Deadliest Catch* is filmed just north and west of False Pass.

(Stipulated Rule 4¹ (hereinafter “SR4”), tab 19 at 1185-86; *see also* tr. 6/151, 7/207)

[I]f your time overruns, it’s not like if you’re on a non-seasonal job, say down on the lower 48. [In the lower 48] you have a 12 month job. If it overruns a month or two, it’s not the end of the world. Here, if you overrun on any seasonal job,...you’re into another whole year.

And as far as the impact on a construction company,...it’s big in terms of dollars and cents, but it’s also big in terms of if you lose a season, you’ve lost the ability to find other work the next season. You’ve tied up your bonding capacity. You’ve tied up...overhead.... [W]hen you have seasonal work, it’s just not the same as non-seasonal work.

(Tr. 9/10-11) Because of the remote location and short construction season, advance planning was particularly important:

You have to make extensive and very thorough advance planning and arrangements. It’s a short season, and contractors that work in Alaska want to be gainfully employed. So if you want to hire a subcontractor to do a specialty task like dredging, you need to get that contractor – you need to be able to commit to that contractor with a specific time frame, so that that contractor will be available.

Because if they don’t sign up with you, they’re looking for business some place else, because they’ve got – again, they’ve got a short construction season, just like everybody else, and they want to be fully booked for the year.

¹ (Tr. 1/84)

So there's a lot of advance planning that's necessary, and over the winter is the time to repair equipment, to line up barges. It gives the contractor an opportunity to tweak its operation. It may decide that one barge is too big or too small and maybe we can swap this barge out for that barge, and all of those things take time and planning.

You want to make sure that your crews are going to be available for the next season, and any long lead materials like the materials for the bridge and dock, it all has to be ordered, fabricated, delivered, containerized and ready to load on that barge when the time comes, because there's no hardware stores in False Pass, and you've got to take it with you or you're bringing it in on a four-seater aircraft, or you have to wait for the next barge.

....

[I]t takes time and it takes funding, because you can't make commitments without knowing that you're funded. When you make a commitment to a dredging subcontractor to perform dredging, and they pass up on other work because they know they have a good contract at False Pass, you've got to have the money, the funding available to pay them.

(Tr. 6/152-53, 155-56, 162-64, 7/223)

2. The Corps had been working for ten years to move forward with two harbor projects in Alaska: one at Sand Point and one at False Pass, which is the subject of this appeal (SR4, tab 106; tr. 7/102-03).

3. KRI is a small business (tr. 2/165) started by brothers Kelly Pleas, president, and Ryan Pleas, vice president, in 1979, specializing in marine construction at remote sites in Alaska primarily for the Corps and the Navy, including several earlier projects at False Pass. KRI was familiar with the continuing contracts funding clause, CCC-5001 (*see* finding 9), as all of KRI's previous contracts with the Corps had included it.² KRI's home office is in Seattle, Washington, and the company usually performs one large project at a time. (Tr. 1/57-60, 2/182-83, 5/71, 7/160-71) We find

² CO Williams testified that "most of your civil works contractors are very familiar with the clause" (tr. 13/42).

that the False Pass project was the only large project performed by KRI after April 2006 (*see* finding 34).

KRI's experience with Alaska Marine Construction was extensive. Among the major projects it had constructed prior to False Pass, the two most recent were St. Paul I and St. Paul II [*see* finding 6]. These were Corps projects which required substantially the same type of construction as was called for on the breakwater and dredging at False Pass; rubble mound type (EM-1110-2-1100, Chapter VI). Design of the rock structures on those projects was similar. The rock placement specification was identical.

(SR4, tab 19 at 1200; *see also* tr. 6/173)

4. In February-April 2005 the Corps was aware of pending legislation that would affect the funding of continuing contracts and was also aware that no funds for the False Pass project were in the FY 2006 budget. David Lau, Pacific Ocean Division, provided the following analysis to Corps Headquarters (HQUSACE) on 4 April 2005 in his request for approval to advertise and award the False Pass project:

Sufficient funds are available to award a continuing contract [for the 2005] Fiscal Year. The project has received Congressional Add appropriations of \$4,442,000 in Fiscal Year 2005. There are no funds for this project included in the Corps of Engineers' Fiscal Year 2006 budget request because the project is still under review by the Administration. We are expressing a Fiscal Year 2006 capability of \$7,416,000 for this project.

....

The following alternate contracting options were evaluated.

Fully Funded Contract- A fully funded contract requires that all funds be available at the time of contract award. We currently do not have all required funding to award a fully funded contract.

Multiple Fully Funded Contracts- Multiple fully funded contracts involve separating the construction of the project into smaller contracts to meet anticipated funding stream.

Construction [of] this project could...be potentially broken into two smaller contracts one for construction of the breakwater and one for dredging. Because of the project's remote location, it is estimated that this could result in increased cost of approximately \$1.3 million dollars more due to the potential of having to pay added mobilization costs associated with two contracts. Because of the added costs...of multiple contracts, this option is not recommended.

Extended Duration Contracts- Extended duration contracts involve adjusting and extending the construction schedule to meet anticipated funding stream in conjunction. The current schedule is based on a 36-month construction period. Because of the short summer construction season in Alaska, it is estimated that extending the construction would result in increased costs of approximately \$1 million dollars per year. Because of the added costs to extend the project, this option is not recommended.

"Standard" Continuing Contract Clause- The "Standard" Continuing Contract Clause is contained in EFARS S52.232-5001^[3] and used for multi-year, incrementally funded construction contracts in connection with projects that have been specifically adopted by Congress in authorizing legislation and appropriations are sought from Congress annually to cover contract payments to be made during the year. **Because the project is still under review by the Administration and the project is not included in the Corps Fiscal Year 2006 budget request, use of the Standard Continuing Contract clause is not recommended for this project.** [Emphasis added]

"Alternate" Continuing Contract Clause- The "Alternate" Continuing Contract Clause is similar to the "standard" clause. However, unlike the "standard" clause, the liability of the Government for payments beyond the funds reserved under the alternate clause is contingent on the reservation of additional funds. The "alternate" clause is contained in EFARS S52.232-5002^[4] and is used in

³ Referred to in this decision as "CCC-5001" (finding 9).

⁴ Hereafter referred to as "IFC-5002."

incrementally funded civil works contracts when contract authority does not exist to obligate the entire contract price in advance of appropriations. **We recommend use of the “alternate” clause for award of this project. This would allow us to award the contract with currently available funding, while limiting the liability of the Government for payment beyond funds reserved.** [Emphasis added]

We are currently scheduled to advertise this project for construction in April 2005 and award a contract in June 2005. Subject to availability of funds, construction completion is scheduled in Fiscal Year 2007.

(SR4, tab 106) Mr. Lau further explained his recommendation to advertise the False Pass project with the “Alternate” Continuing Contract clause:

[B]ecause the Alternate clause specifically states that “Funds are not available at the inception of this contract to cover the entire contract price” and...“The liability of the United States for payments beyond the funds reserved for this contract is contingent on the reservation of additional funds.” Although the project has Congressional authorization, this project has not yet been cleared by the Administration, thus, we cannot include funding for this project in the President’s budget. Continued funding will depend on future Congressional Adds.

(SR4, tab 106 at 1-2) Contrary to his own recommendation, on 6 April 2005, after coordination with HQUSACE, Mr. Lau agreed with the HQUSACE “strategy” to advertise the False Pass project with the “‘Standard’ Continuing Contract Clause” (*id.* at 1). The Solicitation contained EFARS 52.232-5001, CONTINUING CONTRACTS (MAR 1995) [CCC-5001] with no mention of the EFARS 52.232-5002, CONTINUING CONTRACTS (ALTERNATE) (MAR 1995) clause [IFC-5002] (SR4, tab 14 at 356-57, 388).

5. KRI’s project manager (PM) at all times relevant to this appeal was James Swantz. Mr. Swantz, together with Kelly Pleas, did the estimating and scheduling for KRI projects (tr. 4/45-46, 140-41, 7/172). In the course of KRI’s bid preparation Mr. Swantz and Kelly Pleas conducted site visits at several quarries on Dutch Harbor that included Northern Mechanical’s (Dutch Harbor) and Western Marine’s (Sand Point) quarries. They also visited the load out facility at Sand Point. (Tr. 4/46-47, 82-86, 7/177-79)

6. KRI completed work at St. Paul Island under two fixed-price contracts awarded by the Corps. The CCC-5001 funding clause was incorporated by reference in both of those contracts (SR4, tab 27 at 325; tr. 2/183-87, 3/10-13, 46, 4/65). St. Paul Island is one of the Pribilof Islands in the middle of the Bering Sea and is considered one of the most remote villages in Alaska. The first St. Paul Island contract (St. Paul I) required KRI to build a set of three 1,200 foot by 300 foot underwater reefs in front of the St. Paul Island breakwater, one of the tallest breakwaters in the world, and to replace some of the large armor stones in the breakwater. The second St. Paul Island contract (St. Paul II), completed in 2005 just prior to award of the False Pass contract now at issue, required KRI to build a jetty, dredge and install “a ladder of small reefs perpendicular to the breakwater” between the breakwater and the three reefs installed in the first contract. (SR4, tab 134; tr. 1/60-62, 3/46-50, 7/164-72) KRI’s Swantz was the project engineer on St. Paul I and was the project manager on St. Paul II (tr. 4/43-44, 52-54, 61-62). The Corps’ contracting officer (CO) with whom KRI worked on the St. Paul II contract was CO Davidson (tr. 2/102-04, 13/54). The False Pass project was attractive to KRI, in part, because:

We were in the area. We were coming off of St. Paul, and that was an advantage. We had a crew and a Corps administrative staff that was ideal. I mean we – they took care of our requests quickly. When we would have any concerns or communications with them, they would get back to us immediately, and...I wanted to continue that. It seemed like things were working well.

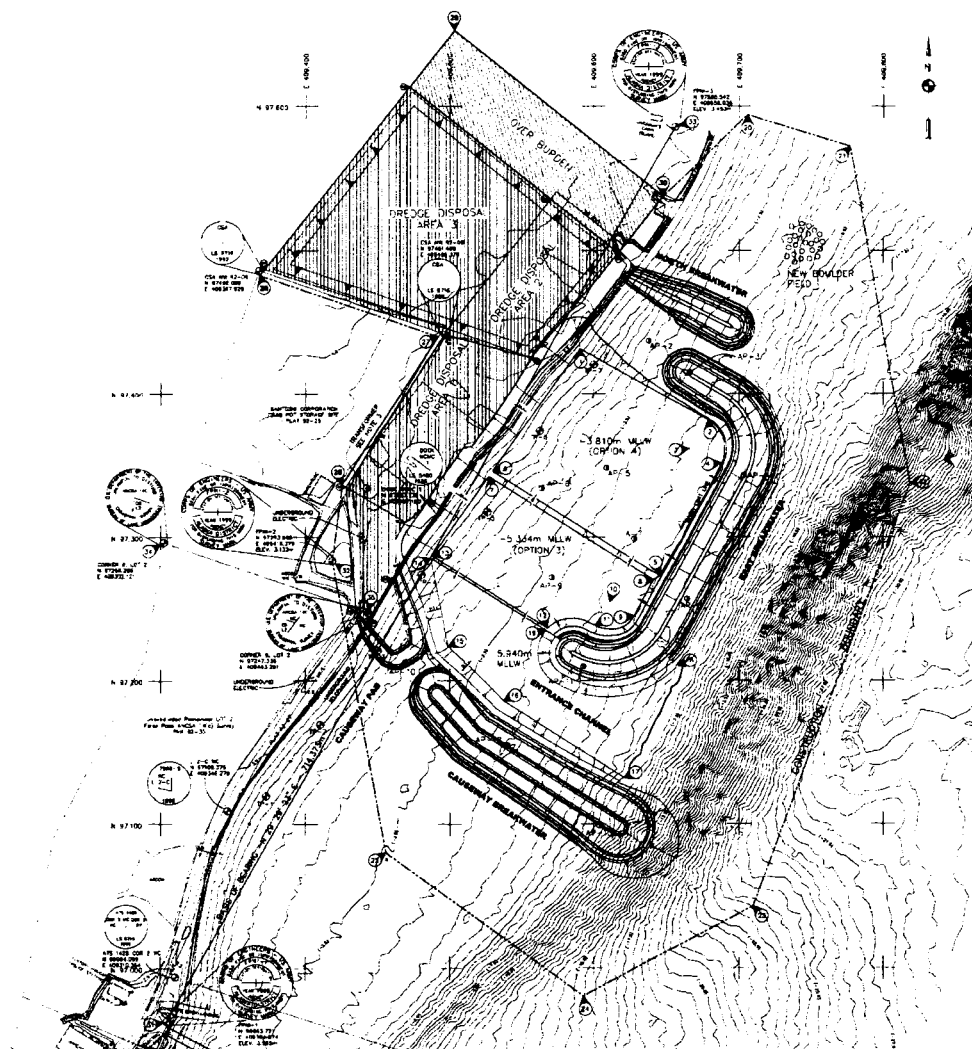
(Tr. 7/182)

7. The bid opening took place on 21 June 2005 (SR4, tab 14 at 86-90). KRI’s bid, including the options for dredging and the dock and bridge, was for \$19,729,300. The Corps’ estimate, including profit, was \$20,076,812. KRI verified its bid on 28 June 2005. (SR4, tabs 6, 14 at 66-67, tab 19 at 704; tr. 1/65-71, 3/57-59) Further analysis of both KRI’s bid and the Corps’ estimate revealed that KRI’s bid included \$13.8 million dollars of direct costs compared to the Corps’ estimate that included \$13 million dollars of direct costs (tr. 9/23-24). The DCAA audit report of KRI’s claim opined that KRI’s bid was unreasonable, however, after careful consideration of the complete record before us, including our examination of the DCAA audit (finding 104), we find KRI’s bid to be reasonable.

B. Contract

8. On 11 July 2005 Contract No. W911KB-05-C-0016 in the fixed-price amount of \$15,981,000 was awarded to KRI for the construction of three rock breakwaters (the options for dredging and the dock and bridge were not exercised at

the time of contract award) to be constructed at the False Pass, Alaska, harbor (SR4, tabs 7, 14 at 1015-17) as shown below:



(SR4, tab 36 at 2 (the Causeway Breakwater is usually referred to throughout the record as the South Breakwater)) The contractual completion date was 890 days after KRI received the Notice to Proceed (NTP) (SR4, tab 14 at 87). The contract performance period included two construction seasons (2006 and 2007) (SR4, tab 19 at 819, 822). The NTP was received by KRI on 28 July 2005 (SR4, tab 8), making the contractual completion date 4 January 2008. The contract specified that no in-water work was permitted to be performed between 1 October and 30 March of any year (SR4, tab 11 at 33, tab 14 at 403, 1090). CO Davidson (*see* finding 6), then the branch chief, signed the contract (SR4, tabs 7, 14 at 1015-17; tr. 12/191, 13/22-23). The contract, as awarded, included a lump sum of \$2,540,050 for “Mobilization/Demobilization, complete” (SR4, tab 14 at 1019).

9. The Continuing Contract Clause, EFARS 52.232-5001 [CCC-5001] contained in the solicitation (finding 4) and the contract as awarded provided:

(a) This is a continuing contract, as authorized by Section 10 of the River and Harbor Act of September 22, 1922 (33 U.S. Code 621). The payment of some portion of the contract price is dependent upon reservations of funds from future appropriations, and from future contribution to the project having one or more non-federal project sponsors. The responsibilities of the Government are limited by this clause notwithstanding any contrary provision of the "Payments to Contractor" clause or any other clause of this contract.

(b) The sum of \$100,000.00⁵ has been reserved for this contract and is available for payments to the contractor during the current fiscal year. It is expected that Congress will make appropriations for future fiscal years from which additional funds together with funds provided by one or more non-federal project sponsors will be reserved for this contract.

(c) Failure to make payments in excess of the amount currently reserved, or that may be reserved from time to time, shall not entitle the contractor to a price adjustment under the terms of this contract except as specifically provided in paragraphs (f) and (i) below. No such failure shall constitute a breach of this contract, except that this provision shall not bar a breach-of-contract action if an amount finally determined to be due as a termination allowance remains unpaid for one year due solely to a failure to reserve sufficient additional funds therefore.

(d) The Government may at any time reserve additional funds for payments under the contract if there are funds available for such purpose. The contracting officer will promptly notify the contractor of any additional funds reserved for the contract by issuing an administrative modification to the contract.

⁵ (See also SR4, tab 142 at 2; tr. 3/47, 14/165)

(e) If earnings will be such that funds reserved for the contract will be exhausted before the end of any fiscal year, the contractor shall give written notice to the contracting officer of the estimated date of exhaustion and the amount of additional funds which will be needed to meet payments due or to become due under the contract during that fiscal year. This notice shall be given not less than 45 nor more than 60 days prior to the estimated date of exhaustion.

(f) No payments will be made after exhaustion of funds except to the extent that additional funds are reserved for the contract. The contractor shall be entitled to simple interest on any payment that the contracting officer determines was actually earned under the terms of the contract and would have been made except for exhaustion of funds. Interest shall be computed from the time such payment would otherwise have been made until actually or constructively made, and shall be at the rate established by the Secretary of the Treasury pursuant to Public Law 92-41, 85 STAT 97, as in effect on the first day of the delay in such payment.

(g) Any suspension, delay, or interruption of work arising from exhaustion or anticipated exhaustion of funds shall not constitute a breach of this contract and shall not entitle the contractor to any price adjustment under the "Suspension of Work" clause or in any other manner under this contract.

(h) An equitable adjustment in performance time shall be made for any increase in the time required for performance of any part of the work arising from exhaustion of funds or the reasonable anticipation of exhaustion of funds.

(i) If, upon the expiration of sixty (60) days after the beginning of the fiscal year following an exhaustion of funds, the Government has failed to reserve sufficient additional funds to cover payments otherwise due, the contractor, by written notice delivered to the contracting officer at any time before such additional funds are reserved, may elect to treat his right to proceed with the

work as having been terminated. Such a termination shall be considered a termination for the convenience of the Government.

(j) If at any time it becomes apparent that the funds reserved for any fiscal year are in excess of the funds required to meet all payments due or to become due the contractor because of work performed and to be performed W911KB-05-B-0009 under the contract during the fiscal year, the Government reserves the right, after notice to the contractor, to reduce said reservation by the amount of such excess.

(SR4, tab 14 at 356-57, 1075)

10. FAR 43.103, Types of contract modifications, provides:

Contract modifications are of the following type:

(a) *Bilateral*. A bilateral modification (supplemental agreement) is a contract modification that is signed by the contractor and the contracting officer.

Bilateral modifications are used to—

- (1) Make negotiated equitable adjustments resulting from the issuance of a change order;
- (2) Definitize letter contracts; and
- (3) Reflect other agreements of the parties modifying the terms of contracts.

(b) *Unilateral*. A unilateral modification is a contract modification that is signed only by the contracting officer. Unilateral modifications are used for example, to—

- (1) Make administrative changes;
- (2) Issue change orders;
- (3) Make changes authorized by clauses other than a changes clause (*e.g.*, Property clause, Options clause, or Suspension of Work clause); and
- (4) Issue termination notices.

An “Administrative change” is defined in FAR 43.101 as:

[A] unilateral (see 43.103(b)) contract change, in writing, that does not affect the substantive rights of the parties

(e.g., a change in the paying office or the appropriation data).

11. FAR, Subpart 43.2—Change Orders, provides:

(a) Generally, Government contracts contain a changes clause that permits the contracting officer to make unilateral changes, in designated areas, within the general scope of the contract.

(FAR 43.201) The Changes clause incorporated into the contract by reference (FAR 52.243-4) provided that the CO “may...make changes in the work within the general scope of the contract” and that the CO “shall make an equitable adjustment and modify the contract in writing” if any such change “causes an increase or decrease in the Contractor’s cost of, or the time required for, the performance of any part of the work under this contract, whether or not changed by any such order” (SR4, tab 15 at 21-22). CO Williams testified as to his understanding that “the Changes clause protects the contractor’s rights “because they can go ahead and submit an REA claim, if they don’t agree with the unilateral mod that’s been given to them” (tr. 12/198-200).

12. FAR 33.204 provides that:

The Government’s policy is to try to resolve all contractual issues in controversy by mutual agreement at the contracting officer’s level. Reasonable efforts should be made to resolve controversies prior to the submission of a claim.

Consistent with that policy, contracting officers “*shall* negotiate equitable adjustments resulting from change orders in the shortest practicable time,” taking into account an appropriate cost analysis. FAR 43.204(b)(1), (b)(4) (emphasis added).

13. The contract incorporated by reference: FAR 52.248-3, VALUE ENGINEERING-CONSTRUCTION (FEB 2000) (SR4, tab 14 at 337, tab 15 at 26-27); and, FAR 52.249-2, TERMINATION FOR CONVENIENCE OF THE GOVERNMENT (FIXED-PRICE) (MAY 2004) (SR4, tab 14 at 337), which enumerated multiple potential sources of termination settlement costs (SR4, tab 15 at 31-35).

14. The contract specifications included Section 01016, “SPECIAL ITEMS (CIVIL WORKS),” which included:

1.17 PARTNERING

- a. The Government intends to encourage the foundation of a cohesive partnership with the Contractor and its subcontractors. This partnership will be structured to draw on the strengths of each organization to identify and achieve reciprocal goals. The objectives are effective and efficient contract performance, intended to achieve completion within budget, on schedule, and in accordance with plans and specifications.
- b. This partnership will be bilateral in makeup, and participation will be totally voluntary. Implementation of this initiative will be a topic of discussion at the Preconstruction Conference. Other recurring or special purpose meetings, as agreed between the Government and the Contractor, will be held as necessary to resolve contentious issues and maintain the partnering spirit.

(SR4, tab 14 at 1081, 1086)

15. The three different types of rock required to be used in the False Pass project were described as:

Core rock is basically the core, the center of the breakwater, and it's usually the largest quantity that's involved in the rock supply. The second layer outside of that is B rock.

....

...There's a spec [SR4, tab 14 at 1527-28]. In the spec there's a gradation clause, and the gradation clause determines what the core rock is made up of.... [C]ore rock can be anything from, I mean sand and gravel and dirt to quality, well-graded stone. In False Pass' case, that core rock was the best grade of core rock I've ever seen.

There's no sand, there's no small chunks in it.... I believe the smallest rock was 20-25 pounds that you could use, and they would allow up to 160 pounds, I think. It seemed to me the size of a small basketball maybe.... So

that rock actually had to be processed, to get all the fines out of it.

....

...B rock. That is the next size up, and now you're into a fairly good sized stone. I'm not going to remember exactly what False Pass was, but it seemed to me that the largest B rock was around a 1,000 pounds, and that was a fairly tight spec, and I was very concerned about it. But as it turns out, you put the B rock into the big jaw that Northern Mechanical had.

If you opened it up as big as it would go and you powered the B rock into it, it would crunch away and it would come out almost perfect. It was almost right on spec.... Then the armor stone, it's more selective. I mean it's – a guy on a backhoe picking up a stone and setting it aside and putting it in a pile and then you can handle it with a front-end loader.

(Tr. 7/187-88)

16. The total amount of funds reserved to the contract, by date, were as follows:

Source	Date	Total Funds on Contract	
Contract Award	7/11/2005	\$100,000	(findings 8, 9)
P00003	1/9/2006	\$5,900,000	Unilateral (finding 24)
P00004	4/27/2006	\$8,350,000	Unilateral (finding 39)
P00005	7/17/2006	\$8,350,000	Unilateral (finding 42) (Deleted CCC-5001, added IFC-5004) Stated to be (\$10,500,000 reserved to contract) but no funds added by the modification.
---	8/23/2006	\$8,350,000	Email (no modification) (finding 54) (\$13,500,000 stated to be reserved to contract but no modification)

P00006	9/19/2006	\$10,450,000	Unilateral (finding 58)
P00007	3/1/2007	\$13,450,000	Unilateral (finding 65) (\$3 million from DOT)
P00008	3/19/2007	\$19,729,300	Unilateral (finding 66) (Deleted IFC-5004, added CCC-5001)

(See also SR4, tab 30 at 3, tab 142; tr. 14/165-72, 174-80)

C. Contract Performance, Claim and Appeal

17. KRI's PM Swantz managed the project from KRI's office in Seattle and was in communication with the jobsite at least once or twice every workday (tr. 4/44, 71-72). He described his responsibilities and duties:

I manage the flow of information to and from the site. I track the daily progress. I take care of scheduling, pay estimates, pretty much everything involved with the project. As issues come up that need to be escalated, [to] Kelly or Ryan, I make them aware of it.

I keep them up to date on accounting, financial information. I am the liaison with the owner. So I work with Lynn Meyers primarily...the [Corps'] Project Engineer for this False Pass, actually St. Paul and False Pass Projects.^[6]

....

Generally the day to day operations, little stuff like that I took care of through Lynn. As you see Ryan [Pleas] on some of the more important issues, dealt with [CO Williams] directly too.

....

⁶ Project Engineer Meyers managed the Corps' onsite quality assurance representatives (QARs), was the "eyes and ears" of the ACO and the "primary interface" between KRI and the Corps. He was assigned to the False Pass project for its entirety. (Tr. 13/10, 86-87) The QARs were onsite at False Pass for the entire construction season each year (tr. 13/14).

[I visit the job from time to time. The people at the jobsite] send in daily reports⁷ by email or depending on how long ago, faxes. And then once Kelly and Ryan, and I have reviewed those, we would then call the field and follow up on any issues and discuss the progress made or concerns identified in those daily reports.

(Tr. 4/44-45)

18. In the late fall of 2005 KRI began mobilizing equipment from St. Paul Island in the Bering Sea to an embarkation point near the False Pass jobsite (*see* finding 6; tr. 4/50). KRI used several barges that had been modified for the St. Paul project to meet American Bureau of Shipping (ABS) requirements and to stand up to the wear and tear of hauling rock:

The hardest service on a barge is hauling rock. No, the hardest service is hauling armor stone.

But all rock service is heavy, and it really increases your maintenance cost, and you have an extra component that you need to add heavy duty fences down both sides, and some type of a wear deck that goes across the floor of the barge, so that as you load and unload and your activity on the barge, it fends off the wear and tear, and you don't get into the steel [of] the barge deck....

...Once that steel wear gets below the amount that's allowed by ABS, basically the value of your barge just drops in half or less.

So when we looked at basically St. Paul to start with, we took a few barges, I believe it was three, and made those conversions to the deck, so that we could haul the armor stone for them. Then there are a couple of other barges that are in the Northwest that have the ABS load lines that you need to cross the ocean, and the wear decks.

(Tr. 7/167-68)

19. The equipment selected by KRI to perform the False Pass project work:

[W]as well suited for its intended use [and a list of that equipment was included in KRI's daily reports to the

⁷ Both the Corps' QAR daily reports and KRI's daily reports are in the record at Stipulated Rule 4, tab 17.

Corps onsite personnel].... The fleet varied from year to year, depending upon the type of work being done. A brief perusal [of the list] reveals an impressive fleet; KRI was well equipped....

(SR4, tab 19 at 1200; *see also* tr. 6/173) Much of the equipment utilized by KRI in performance of the contract was rental equipment:

[T]he big barges are rental, the tug is rental. The cranes, the big cranes are rental. So [when we demobilize] we need to get those back, so that they come off rent and we don't sit with them all year.

....

Seattle [is home for that equipment], and so we demobed all of that back to the home base, and then basically the other parts of the job are to winterize the equipment, move stuff....

...So we would take selective pieces back to Dutch Harbor, where they were secure in the quarry, and we had a mechanic's shop.

(Tr. 7/205) All of the non-rental equipment was normally left onsite or at Dutch Harbor over the winters between construction seasons, but the non-rental equipment would also have to be demobilized back to Seattle by barge if the contract were terminated for lack of funds (tr. 7/205-06).

20. The Energy and Water Development Appropriations Act of 2006 (E&WDA), Pub. Law No. 109-103, was passed on 19 November 2005 (SR4, tabs 23, 143).

The [E&WDA] includes new legal limitations that severely constrain many of the Corps existing processes and procedures used in the execution of the Civil Works program.

(SR4, tab 110 at 1) The E&WDA was described by Mr. Loew, CECW-I, as "a big deal" and "a sea change in Corps of Engineers' business practices for civil works projects" (tr. 7/88-93). Mr Loew was responsible, at the HQUSACE level, for:

[T]he development of the [Corps'] Civil Works budget, which is a compilation of all of the budgets of the districts

and divisions, all the field offices, to negotiate that inside the Corps through our Chief of Engineers, and then present it to the Assistant Secretary of the Army for Civil Works.

(Tr. 7/80) He had decades of program management and fund management experience. After passage of the E&WDA, it was the responsibility of his office to prepare the Corps' guidance to its program management community, the EC 11-2-189 (*see* finding 23). He also coordinated on the Corps' guidance to its contracting community (*see* findings 23, 30). (Tr. 7/79-86, 107-08, 117-22, 133)

21. On 2 December 2005 contract Modification No. P00001 exercised the contract line item numbers (CLINs) 0015 and 0016 options that added the dredging of the entrance channel to the harbor, as well as the harbor basin. The contract completion date of 4 January 2008 remained unchanged and the contract price was increased by \$1,132,300 from \$15,981,000 to \$17,113,300. (SR4, tab 14 at 2047-48, tab 19 at 822)

22. On 19 December 2005 Contract Modification No. P00002 exercised CLINs 0013 and 0014 options that added the construction of a bridge and dock as components of the causeway breakwater. Again, the contract completion date of 4 January 2008 remained unchanged and the contract price was increased by \$2,616,000 from \$17,113,300 to \$19,729,300. (SR4, tab 14 at 2035-36).

23. On 31 December 2005 HQUSACE published Circular EC 11-2-189, its statement of Corps policy for implementation of the E&WDA (finding 20), as well as budgeting and programming instructions, which was distributed to all Corps civil Divisions and Districts (SR4, tab 110). Circular EC 11-2-189, published as guidance to the Corps program management community (tr. 7/133, 13/119-21), provided:

This Circular provides [Corps] program and project management policies and practices to ensure that execution of the [FY 2006] annual appropriations is conducted in accordance with the statute [P.L. 109-103], direction and intent of the Administration and Congress.... It documents changes in Corps processes that must be incorporated into FY2006 execution plans and acquisition strategies to ensure that implementation of programs, projects, and activities (PPA) in FY2006 complies with the new legal restrictions and commitments made to the Congress....

2. Applicability. This Circular applies to all HQUSACE elements, major subordinate commands and district commands having Civil Works responsibilities. It is applicable to all [Corps] Civil Works programs, projects,

and activities (PPA) in all Civil Works Appropriations upon publication of this Circular. This guidance is effective immediately, and supersedes all other reprogramming guidance including ER 11-2-201. District and Division offices shall inform CECW-I [see finding 20] of any problems with the implementation of this guidance.

....

c. **Actions on Existing Continuing Contracts. With respect to existing continuing contracts, the Corps has a bilateral agreement with contractors based on the true continuing contract clause [EFARS 52.232-5001]. The Corps, therefore, cannot unilaterally modify existing contracts to require the contractor to work within funds reserved in compliance with the new limitations contained in P.L. 109-103.** HQUSACE will develop a standard memorandum for use by Contracting Officers to notify all contractors working under an existing continuing contract that they cannot rely on reprogramming to add funds to their contract, and if funds are exhausted, the Corps may have to consider terminating their contract.... [T]he following steps **must** be taken (**in the order provided below**) to ensure existing continuing contracts are in compliance with provisions of P.L. 109-103:

(1) **Negotiate with the contractor and reach agreement to modify the contract to limit the Government's liability to funds currently available in FY2006.** This action could require the contractor to develop and prosecute a schedule based on funding levels that are less than optimum. This option could include items such as the contractor agreeing to not charging the Government for any suspension or demobilization/mobilization costs. **Realize that limiting the Government's liability increases the contractor's risk and, therefore, is likely to increase the cost of the contract.**

(2) **Seek approval to reprogram** and add additional funds to the project, if and when the contractor notifies the Corps that it expects to exhaust available funding. Reprogramming of funds into the project will be

limited by Section 101 of P.L. 109-103 as described in paragraph 10 of this Circular.

(3) Terminate the contract, and reprocure as a fully funded contract. Since funds are required to terminate the contract and to reprocure as a fully funded contract, the termination and reprocurement may need to occur in different fiscal years.

All of the options listed above could have **significant cost implications** from a contractual perspective. The actual impacts will depend on **factors unique to each contract and project.**

(SR4, tab 110; tr. 7/119-29) (Emphasis added) Mr. Loew testified that “[t]his is a directive. It’s not a choice.” (Tr. 7/95)

So in short it says get with the contractor. Bilaterally negotiate a mod. It also says in the instruction to this we expect, we expect that that will cause problems in some contracts, and it could be schedule problems or cost (problems).

So you work those out with your contractor, and if you can solve the problem, like I say it takes a little more money, do a reprogramming, solve the problem and put the clause in, so that the costs of this year are covered.

It says if you can’t solve the funding problem, then terminate the contract. Those instructions are absolutely clear.

(Tr. 7/98-99) Further detailed instructions by HQUSACE were later distributed throughout the Corps, as guidance to the Corps contracting community (tr. 7/133, 13/120-21), in the “PARC⁸ Instruction Letter (PIL), Continuing Contracts and Incrementally Funded Contracts for Fiscal Year 2006,” dated 22 March 2006 (*see* finding 30).

24. Contract Modification No. P00003, dated 9 January 2006, added funds to the contract in the amount of \$5,800,000, making the total funds on the contract \$5,900,000 (SR4, tab 14 at 2029-30; tr. 13/6-9, 57-58, 62-63, 96-104, 123-27)

⁸ Principal Assistant Responsible for Contracting, CEPR (EFARS 1.201-100) (tr. 7/129-130), the Corps’ headquarters for the contracting field (tr. 13/36).

25. A Pre-Construction Meeting was held on 26 January 2006 during which KRI submitted value engineering documents (VE or VECP) proposing an open cell design for the bridge and dock (tr. 13/15-16). The minutes of the meeting do not contain any mention by the Corps to KRI of the impending change in funding policy. (SR4, tab 11 at 28-42; tr. 1/94-98) KRI's inquiry about being paid for rock stored at Dutch Harbor near the rock source was discussed (SR4, tab 11 at 41-42; tr. 3/129-130, 4/56-57, 13/29-32). The appropriate clause permitting such payment was incorporated by reference into the contract as awarded as "SCR-33, PAYMENT FOR MATERIALS DELIVERED OFF-SITE (MAR 1995) (EFARS 52.232-5000): SEE SECTION 00700: CONTRACT CLAUSES." Nevertheless, the Corps maintained that it would not pay for stored materials until the full text of the clause was added by modification; we find no evidence that such a modification was ever issued. (SR4, tab 14 at 336-57, 1074; tr. 3/54-57, 107-09, 130-31)

26. KRI's original construction schedule/work plan and cash flow estimate dated 16 December 2005 (SR4, tab 11 at 3-8, tab 18 at 75-76; tr. 3/89-99, 4/53-54, 9/59-60) was updated to include the dredging, dock and bridge that were added by Modification Nos. P00001 and P00002 (findings 21-22; tr. 4/53-54). The updated schedule was submitted to the Corps with a data date of 1 February 2006 and showed mobilization to the jobsite by 30 May 2006 and demobilization from the jobsite at the end of the construction season from 30 August 2006 – 6 September 2006. The 1 February 2006 schedule also showed its plan to mobilize to the jobsite 11-31 May 2007 for the 2007 construction season and demobilize from the jobsite at the end of the 2007 construction season from 28-30 August 2007. KRI's schedule planned that the work performed would earn payment of \$10,065,300 in the 2006 construction season and the balance of the contract amount, \$9,664,000, in the 2007 construction season. (SR4, tab 11 at 7-8, tab 18 at 12-18, 67-73; tr. 3/92-104, 109-12) KRI's 1 February 2006 work plan for the 2006 construction season called for two barges to haul rock between Dutch Harbor and the jobsite, as well as completion of the North Breakwater in 2006. The length of the East Breakwater was planned to be partially constructed, through armor stone placement, in 2006. The remaining work on the East Breakwater and construction of the South Breakwater were planned to be completed in 2007. The dock and bridge were tied into the South Breakwater and KRI planned to perform the dock and bridge work concurrent with placement of the South Breakwater rock. (Tr. 7/192-93) Per specifications, the dredging was not to commence until all three of the breakwaters had been constructed to a minimum height of 1.25 meters. Accordingly, KRI's plan anticipated that the dredging subcontractor would mobilize to perform its work commencing in June of 2007. Dredging in the east channel had to follow construction of the bridge and dock. The critical path throughout contract performance was through rock placement. (SR4, tab 19 at 241-43, 248; tr. 2/107-08, 9/52, 116). After consideration of the extensive record before us, we find that KRI's 1 February 2006 construction schedule was reasonable and further find that, had the

work been performed as planned, the contract would have been completed on time (*see also* SR4, tab 19 at 248).

27. On 5 January 2006 KRI entered into a \$6,100,000 contract with its primary source of the rock to be utilized on the project, Northern Mechanical at the Ugadaga Quarry at Dutch Harbor, Alaska. The contract specified that all of the rock needed for the False Pass project was required to be produced by 15 November 2006 and Northern Mechanical started producing rock for the project over the 2005/2006 winter before its subcontract with KRI was executed. The rock was planned to be transported between the Dutch Harbor and the False Pass jobsite using two barges (*see* finding 26). KRI also made preliminary arrangements with a supplemental/alternate rock supplier, Western Marine⁹ at its Sand Point Quarry, to be used if Northern Mechanical was unable to deliver the sizes and/or quantities of rock required to meet KRI's production schedule. (SR4, tab 19 at 756, 1194, tab 20 at 2; tr. 3/74-85, 4/50-51, 68-71, 7/175-82, 185-86, 16/8-9, 25-26) As bid and planned by KRI, the cost of the rock was the largest item of project cost to KRI, followed by the bridge and dock and then dredging (tr. 4/51). In a separate agreement KRI offered to Northern Mechanical the use of some of KRI's equipment from the St. Paul Island project to lower the price of rock (SR4, tab 19 at 1200; tr. 4/50-51, 68-69, 5/10-14, 7/181, 185). Northern Mechanical produced rock for False Pass through 31 May 2007 (SR4, tab 24 at 179-90; tr. 10/138-40) and there was work at the quarry in June 2007 but no rock production (SR4, tab 24 at 191; tr. 10/140).

28. The process of rock production was described as:

[T]he mining operation is done on the face of the quarry, and the blast, come down. They set in front with very large machines and pulled the rock apart, and the initial sort is there. It gets pulled back with front end loaders, and in the case of core rock, they run it through a large jaw and then a screen or actually a grizzly that separates the core rock into the pay item, and the reject, and the reject on that material is the stuff that was too small.

Then the reject on the upper end would go to a B rock sorting area. The armor stone, the way the Corps handles their armor stone process, is they want you to paint a rock that is on the large side of the armor size, and then they want you to paint a rock that's on the small size. You have those two rocks that oppose each other.

⁹ Western Marine was also the contractor with whom the Corps contracted for performance of the Sand Point harbor project (*see* findings 2, 5, 29, 44).

The operator[]s in the front end loaders can look at those as they're sorting it out, and they can basically tell what an armor stone is, and then they stockpile those armor stones.

(Tr. 7/183; *see also* 4/70-71, 7/179)

29. CO Williams was the contracting officer and PM Wierzbicki was the project manager for both the False Pass and Sand Point¹⁰ projects (SR4, tab 14 at 167; tr. 13/43, 138-39). As project manager, Wierzbicki was responsible for project funding and funding related decisions, while contracting officers made contracting decisions (tr. 12/193, 13/58; *see also* finding 24). By email dated 20 March 2006, PM Wierzbicki notified CO Williams and CO Davidson¹¹ of the following:

Continuing Contracts

All existing contracts MUST be re-negotiated immediately (if not already) to include new clause where contractors agree NOT TO EXCEED amount available for the project (carry over plus amount appropriated for project this FY). Congressional intent is for Contractors to stay within amount available for project and keeping Congressional control of the amount allocated for the project.

HQ has not sent this letter instructing us to do this as yet. Waiting for the guidance to be signed.

In anticipation of the Guidance, we have negotiated with Western Marine for the on-going Sand Point harbor contract. The contract completion was extended [one work season] to 1 October 2007.... This funding policy will be discussed at the False Pass harbor partnering meeting on 3 April with [KRI]. From now on, no more contracts will be awarded as continuing contracts under the Construction, General appropriation without a waiver from Assistant Secretary of the Army (Civil Works).

(SR4, tab 14 at 1999-2000; tr. 13/132; *see also* SR4, tab 145) The Corps recognized that the change in funding policy would possibly affect KRI's construction schedule such that KRI would need an extension of the contract performance period, just as the

¹⁰ (See findings 2, 5)

¹¹ (See findings 6, 8)

Corps had granted one to Western Marine (SR4, tab 3 at 169). The bilateral modification negotiated by the Corps with Western Marine for the Sand Point project replaced the CCC-5001 with “52.232-5003 Special Continuing Contract Clause”¹² and extended the performance period by 247 days. The Sand Point project was the only then-existing continuing contract in the Alaska district, other than the False Pass project, which was over \$10,000,000. CO Davidson signed the Western Marine modification. (SR4, tab 14 at 78, 144, 1999-2000, 2306-07, tab 145; tr. 13/139-45)

30. The 22 March 2006 PIL (*see* finding 23) contained the Corps’ express requirements for the implementation of the E&WDA:

1. References:

- a. Section 10, River and Harbor Act of 1922 (Public Law 67-362); 33 U.S.C. §621.
- b. Energy and Water Development Appropriations Act of 2006 (Public Law 109-103).
- c. Engineering Circular 11-2-189 “Execution of the Annual Civil Works Program” (2006).
- d. EFARS Subparts 32.7 and 52.2
- e. CECW-I Letter “Existing Continuing Contracts Notification Letter,” (February 13, 2006).

2. Background:

a. The [E&WDA] included provisions that restricted the Corps authority to reprogram funds and award continuing contracts in fiscal year 2006.... Section 108 of the 06 E&WDA prohibits the Corps from awarding or modifying an existing continuing contract when doing so would commit an amount in excess of the amount appropriated for that project pursuant to the 06 E&WDA, plus any amounts available from carryover or reprogramming. Section 101 of that act restricted the Corps reprogramming authority.

b. In light of the legal restrictions on continuing contracts, the Corps must change its implementation of

¹² Hereafter referred to as “IFC-5003.” This is a different incremental funding clause than the IFC-5004 unilaterally modified into KRI’s contract because Sand Point was in the President’s budget for 2007 and False Pass was not.

existing continuing contracts, as well as the terms it uses to award new multi-year contracts that are not fully funded.

3. Purpose:

a. The existing continuing contract clause (EFARS 52.232-5001) permits the contractor to work beyond the amount reserved to the contract for a fiscal year. Doing so, creates a legal liability to pay the contractor for such costs, even though – under the existing continuing contract clause – we do not have to make the payments until the next fiscal year. Accordingly, because the clause permits contractors to commit the government in excess of the amount appropriated for that project plus available carryover and reprogramming, use of this clause runs a high risk of violating Section 108 of the 06 E&WDA. **Therefore, the existing continuing contract clause should not be used in new or existing solicitations, unless specifically authorized by CECW-I [see finding 20] and ASA(CW) or his delegatee.**

b. In order to implement the Corps Civil Works program under the new continuing contract restrictions, the Corps has chosen to draft two new clauses.... The second clause – found at Attachment B [IFC-5004] – is an incremental funding clause. It also does not permit the contractor to work beyond the amount reserved and expressly requires the contractor to stop working when funds are exhausted. **Note that since both clauses limit the amount payable to the contractor and require the contractor to stop work, contractors' estimates will likely increase their prices in order to account for this increase in risk. The difference between these two clauses is that under the incremental funding clause, the government's liability for termination costs is limited to the amount reserved on the contract. In contrast, under the clause at Attachment A, the government is responsible for all costs pursuant to the termination for convenience clause regardless of the amount reserved on the contract.** This memorandum provides guidance on when to use the clause at Attachment A and when to use the clause at Attachment B.

4. Existing Continuing Contracts:

a. This section applies to all contracts that have been awarded with the so-called “True” Continuing Contract Clause (EFARS 52[.]232-5001) that have not been completed. For those contracts, the Engineering Circular governing Fiscal Year 2006 operations requires limiting the Government’s liability through one of the following (in order of precedence):

(1) **Negotiate** with the contractor and reach agreement to modify the contract to limit the Government’s liability to funds currently available in FY 2006. This action could require the contractor to develop and prosecute a schedule based on funding levels that are less than optimum. This option could include items such as the contractor agreeing not to charge the Government for any suspension or demobilization / mobilization costs. Realize that limiting the Government’s liability increases the contractor’s risk and, therefore, is likely to increase the cost of the contract.

(2) Seek approval to **reprogram** and add additional funds to the project, if and when the contractor notifies the Corps that it expects to exhaust available funding. Reprogramming of funds into the project will be limited by Section 101 of P.L. 109-103 as described in paragraph 10 of Engineering Circular [EC] 11-2-189.

(3) **Terminate** the contract, and reprocure as a fully funded contract. Since funds are required to terminate the contract and to reprocure as a fully funded contract, the termination and reprocurement may need to occur in different fiscal years....

b. We recommend using the model letter developed by CECW-I to explain the change in law to those contractors working under an existing continuing contract. See Ref. 1e....^[13]

¹³ The only copy of the referenced model letter we have found in the extensive record before us is a 3 February 2006 draft of the letter (SR4, tab 105). We have found no evidence that CO Williams actually used the recommended model

c. For all contracts awarded with the continuing contract clause at EFARS Part 52.232-5001, unless you have approval to continue the contract as a continuing contract pursuant to paragraph 5c of the EC, you must delete the continuing contract clause from the contract.... For those continuing contracts that do not have funding in the budget for the out years, replace the continuing contract clause with the Incremental Funding clause found in Attachment B.... The incremental funding clause in Attachment B limits the government's total liability – including termination costs – to the amount reserved and, therefore, should be used when future year funding is less certain.

d. The 52.232-5001 clause must be replaced through a bilateral modification; a unilateral modification is not sufficient.^[14] So long as the contractor anticipated meeting its schedule this fiscal year using only the funds reserved to the contract, modifying the contract using the clause in Attachment A could be at no cost. However, **we expect most contractors will attempt to justify an equitable adjustment due to the increased costs or risks associated with these new clauses.** Your office should use its discretion to ensure that any required equitable adjustment is both a result of increased costs directly attributable to a funding shortfall and also is reasonable. A contractor may have expected to work beyond the amount reserved for the contract this fiscal year. In such a case, work with the contractor to

letter, nor have we found even a reference to the model letter by CO Williams or any other Alaska District Corps personnel.

¹⁴ Mr. Loew, CECW-I (*see* finding 20), testified:

[T]he contract is a bilateral agreement. We put out a set of plans and specifications. The contractor bid on that. So we have arrived at a bilateral document, and a change like this, which could impact cost or schedule, we do not have the option of doing this without discussing it with the contractor, and reaching a mutual solution.

(Tr. 7/151)

develop a new execution schedule that starts later in the year or only requires earnings equal to the amount reserved in this fiscal year. We recognize that changing the schedule may also prompt the contractor to request an equitable adjustment. Again, work with contractor to ensure any equitable adjustment is a result of increased costs directly attributable to a funding shortfall and is reasonable.

....

6. Incrementally Funded Contracts:

a. The PARC office has received several requests for guidance on incrementally funded contracts. Because of the new legal restriction on continuing contracts for this fiscal year, the EC directs contracting officers to consider acquisition alternatives such as incrementally funded contracts. An incrementally funded contract is one in which the agency enters into a multi-year contract without obligating the entire amount of the contract at the time of award; the agency only obligates the amount needed each year of the contract, and the Government's liability under the contract at any given time is limited to the amount reserved for the contract at that time. Such contracts are generally prohibited unless authorized by statute. See 41 U.S.C. §11. The Corps is authorized to use incrementally funded contracts by the same statute that authorizes us to use continuing contracts – 33 U.S.C. [§]621. Therefore, incremental funding is available only for those contracts that could have used continuing contracts under the guidance at EFARS Part 32.705-100(a).

b. No approval is needed from either the ASA(CW) or CECW-I to solicit or award an incrementally funded contract. Although the clause at Attachment B [IFC-5004] limits the Government's termination liability to the amount reserved in the contract, any termination carries a high administrative cost to the Corps that may include litigation and reprocurement. Therefore, to avoid unnecessary terminations contracting officers should have a reasonable expectation that the project will receive funding in future years. **When work can be segmented into discrete and**

viable work segments, contracting officers should consider awarding a fully funded base contract with options as an alternative.

....

8. Commanders and Directors should disseminate this PIL widely, to include all acquisition personnel at your respective activities.

(SR4, tab 22; tr. 7/99, 129-47) (Emphasis added, footnotes omitted) Mr. Loew, CECW-I (finding 20) testified:

You have to negotiate with the contractor first, to determine if there's any cost associated with the IFC, and if there is, you should include that, the solution to that cost or schedule problem in the modification.

....

They're...to sit down with the contractor and see if that clause is going to have an impact on your cost or schedule or risk that we have to deal with, and to figure out what that is, then the modification would take care of that.

....

...The law says that the Corps of Engineers can no longer have an existing, continuing contract underway that has planned expenditures in excess of the amount available in that contract. That's a change. That's a huge change for us.

So the guidance basically says this is how you deal with that problem. You now figure out if your contract price for this year is still adequate, and if it's not, take these steps to either make it adequate or, if you can't do that, terminate it. The law does not allow us to continue with that contract if there's not enough funds in it to cover that year's cost.

....

[The guidance was followed on] hundreds and probably thousands of contracts.

(Tr. 7/143-45; *see also* tr. 7/146-57) CO Williams testified that the PIL did not tell him what to do if the contractor refused to sign a bilateral modification (tr. 13/122-23, 25, 14/22), but we find the PIL to be very clear in its direction that if you don't, or can't, negotiate a bilateral modification (option 1) and you don't or can't reprogram funds (option 2), the only other option (option 3) is to terminate the contract for convenience (*see* tr. 13/207-13).

31. The PIL's Attachment B [IFC-5004] incremental funding clause was a new clause (*see* finding 30) that was not in existence at the time of the solicitation or the contract as awarded to KRI. IFC-5004 provided:

Attachment B

52.232-5004 Incremental Funding Clause

(a) Funds are not available at the inception of this contract to cover the entire contract price. The liability of the Government is limited by this clause notwithstanding any contrary provision of the "Payments to Contractor" clause or any other clause of this contract. The sum of \$ _____ has been reserved for this contract and is available for payment to the contractor during the current fiscal year. It is expected that Congress will make appropriations for future fiscal years from which additional funds, together with funds provided by one or more non-federal project sponsors, will be reserved for this contract.

(b) Failure to make payments in excess of the amount currently reserved, or that may be reserved from time to time, shall not be considered a breach of this contract, and shall not entitle the contractor to a price adjustment under the terms of this contract.

(c) The Government may at any time reserve additional funds for payments under the contract if there are funds available for such purpose. The contracting officer will promptly notify the contractor of any additional funds reserved for the contract by issuing an administrative modification to the contract.

(d) If earnings will be such that funds reserved for the contract will be exhausted before the end of any fiscal year, the contractor shall give written notice to the contracting officer of the estimated date of exhaustion and the amount of additional funds which will be needed to meet payments due or to become due under this contract during that fiscal year. This notice shall be given not less than 120 days prior to the estimated date of exhaustion. Unless informed in writing by the contracting officer that additional funds have been reserved for payments under the contract, the contractor shall stop work upon [] the exhaustion of funds.

....

(f) Any suspension, delay, or interruption of work arising from exhaustion or anticipated exhaustion of funds shall not constitute a breach of this contract and shall not entitle the contractor to any price adjustment under a "Suspension of Work" or similar clause or in any other manner under this contract.

(g) An equitable adjustment in performance time shall be made for any increase in the time required for performance of any part of the work arising from exhaustion of funds or the reasonable anticipation of exhaustion of funds.

(h) If, upon the expiration of one-hundred (100) days after the beginning of the fiscal year following an exhaustion of funds, the Government has failed to reserve additional funds for this contract sufficient to cover the Government's estimate of funding required for the first quarter of that fiscal year, the contractor, by written notice delivered to the contracting officer at any time before such additional funds are reserved, may elect to treat his right to proceed with the work as having been terminated. The Government will not be obligated in any event to reimburse the contractor for any costs incurred after the exhaustion of funds regardless of anything to the contrary in the clause entitled "Termination for Convenience of the Government."

....

(j) The term “Reservation” means monies that have been set aside and made available for payments under this contract. Reservations of funds shall be made in writing via an administrative modification issued by the contracting officer.

(SR4, tab 22 at 7)

32. In an email dated 31 March 2006, in response to KRI’s inquiry about topics for discussion at the first Partnering Meeting set for 3 April 2006, Corps project engineer Meyers responded:

Sorry it took me so long to get back to you. The only thing we want to discuss is the following:

Funding of contract vs. contractor’s schedule
Possible time extension needed by KRI because of
the above issue.

(SR4, tab 3 at 9, 169) This was the first indication KRI had that funding or schedule were potentially an issue.

33. The first two Partnering Meetings (*see* finding 14) utilized a facilitator as “a way of cutting through a lot of the paperwork and getting to the heart of matters and getting to the meat of matters quickly without a bunch of letter writing.” The facilitator, Lane Tucker, prepared and distributed the minutes of the Partnering Meetings held in April and May 2006. (Tr. 1/98-99, 7/42-48, 54, 58-65, 69-73, 13/55-56)

34. The first Partnering Meeting took place in Anchorage, Alaska, on 3 April 2006 prior to the commencement of jobsite work during the first construction season (*see* finding 26). In attendance were representatives of the Corps, KRI and the Aleutians East Borough (the end user of the project, referred to in the record as either the sponsor, the customer or AEB). (SR4, tab 111; tr. 7/76-77) The meeting minutes began with a statement of seven (7) Project Goals to include:

- 3) Producing a quality project that conforms to the plans and specifications and addresses the needs and priorities in the feasibility study. The harbor is the first priority; the dock is second; and then the bridge.

- 4) Working as a team with open and prompt communication[.]
-
- 6) Protecting the environment, and being aware of the window for work: no in-water work between November 15 and March 31; no piles until after April 15.^{15]}
- 7) Realizing savings through the Value Engineering proposals[.]

(SR4, tab 112) Specifically, with respect to communications, the minutes stated that:

All parties agree that open and prompt communication is critical to the success of the project. To facilitate this process, it was agreed that a joint teleconference will be held once a week on Wednesdays at 9 a.m. beginning June 7, 2006.

The parties recognize that the timely submission of proposals and reviews is important to the successful completion of the project. The Corps advised that meeting its review times has generally not been a problem.

(SR4, tab 112 at 2; tr. 1/100-01) Facilitator Tucker's meeting minutes further contain the following record of issues discussed pertinent to the matters now before us:

A. Funding

[After handing out a copy of the PIL (tr. 3/123, 4/162-163, 7/53),] [t]he Corps explained that Congress has recently passed legislation restricting its ability to reprogram funds. Hence, the Corps will need to execute a bilateral modification with KRI to incorporate [an

¹⁵ The contract, as awarded and at the time of the 3 April 2006 meeting, prohibited in-water work from 1 October thru 30 March (finding 8). The contract was not modified to extend in-water work through 14 November until Modification No. P00010 dated 13 November 2007 (findings 78, 83).

incremental funding clause] into the contract.^[16] The Corps will officially notify KRI of funding issues by letter [see n.13 *infra*].

The Corps' interpretation of the effect of this change is that \$8.5 million^[17] is available for work on this contract through September 30, 2006 (Fiscal Year 2006). ALL COSTS, including requests for equitable adjustment, termination for convenience costs, demobilization, etc., MUST come from this \$8.5 million. The Corps will not be certain that additional funds are available for contract work until Congress passes the next appropriation bill.

KRI had budgeted [to earn] approximately \$10.5 million for work during FY 06. Hence, the bilateral modification will have to address changes in the scope of work that can be undertaken during FY 06, and the costs of those changes due to the new funding mandate.

In order to address this issue, the Corps will send KRI a letter on or before April 14, 2006, setting forth its preference for the scope of work undertaken in FY 06. KRI will respond on or before May 3, 2006. On May 5, 2006, appropriate representatives from the Corps, KRI, and False Pass will conduct a partnering meeting to discuss viable options and respective cost impacts.

B. Off-Site Material Storage

... KRI explained that it proposed to handle the storage of material on this job much the same as it handled material storage on the St. Paul [Island] job [see findings 6, 25]....

In the meeting, KRI advised the Corps that this issue needed to be resolved in order to address the changes

¹⁶ There was agreement among witnesses that the discussion referred to three different funding clauses in general as continuing contract clauses but that the subject of an incremental funding clause to be modified into the contract was the primary topic of discussion (tr. 3/123, 7/66-68).

¹⁷ The amount on the contract as of Modification No. P00004, issued 27 April 2006, was \$8,350,000 (finding 16).

that would be required by the new contract funding clause to be incorporated with the bilateral mod, and that it is time-sensitive because the quarry operator is currently producing rock under contract to KRI. KRI also advised the Corps that renegotiating the rock contract would almost certainly result in additional contract costs.

C. Value Engineering Proposals

KRI has submitted two value engineering proposals [for the bridge and dock].

....

D. Method of Work Questions^[18]

General: The rock will be quarried, and KRI has leased and permitted an area for loading. Rock will be barged to False Pass and deposited with a G.P.S. survey system. KRI is finalizing the barge and mobilizing; there will be two barges to start and three later. KRI expects departure around April 11 or 12, 2006. Activity will start after the high water mark shows. KRI expects the first load of rock to arrive in False Pass during the first part of June. The transit time is approximately 26 hours; the unloading times will vary.

Rock Schedule:

Rock will be quarried throughout the summer; completed in August.

Building of Breakwater:

....

¹⁸ We find that the work plan detailed in these minutes is the 1 February 2006 work plan submitted by KRI after the bridge and dock were added to the contract but before the Corps notified KRI of the funding clause change (*see* finding 26).

- The B rock will be placed at various levels, and after confirmation the A rock will be placed. Armor stone will probably be alternated on the second barge.
- Under the current work plan, the north breakwater will be completed first, and it will be used to set up the system on the rest of the job. The long [East¹⁹] breakwater will then be built.
- KRI intends to use a progressive sequence, rather than placing all core rock, then all B rock, then all A rock. For pay purposes, KRI will use its construction control survey gear.

....

E. Miscellaneous

- All of the bridge and dockwork will be postponed²⁰ to save money; the city and borough are okay with this.

(SR4, tab 13 at 3-6, tabs 111-12; tr. 4/58-61, 7/48-54, 7/193-96, 13/170-75) Facilitator Tucker testified:

What the Corps wanted to talk about was how can you reprogram or resequence this job? What can you do for the amount currently funded on the contract, particularly given that you have [to] conserve a certain amount of money prior to being done. Here, the ice is out and the season is usually in a typical year, June to the end of August.

They can go perhaps late May to early September, but it's a very short season that you have available to get to these locations and then get back to your staging area, which is typically Seattle for Alaska projects.

¹⁹ (See finding 8)

²⁰ "Postpone[ment of] the dock and bridge to save money, even if looked at alone, constituted a serious impact to the project" (SR4, tab 19 at 1317).

....

The sequencing of work, the means and methods, the scope of work that was going to be performed during that first season had to be adjusted. So I think the issue with respect to that was the Corps was to send a letter telling KRI what it would like to see accomplished for the amount of money it was going to spend, in the event that it didn't get anymore money, and KRI was going to respond, and then we were going to have a second partnering meeting.

(Tr. 7/51, 53-54, 56) With respect to the funding issues discussed at the meeting, the notes of KRI's Ryan Pleas state:

[PM] Wierzbicki f[ro]m the Corps stated that they only have \$8.5 million for the False Pass Project this year. Next year[']s budget has not been finalized by Congress. Corps will send KRI letter regarding funding. KRI can not spend more than \$8.5 million including complete demob costs and termination costs. Corps will send KRI a bilateral modification for the contract which will insert a new clause (see handout²¹). KRI [is] entitled to recoup any termination costs or extra costs due to the need to change means and methods to accommodate the funding issues. KRI also entitled to extended time to complete project. If contract is extended the [C]orps will need to extend the real estate agreements. In no case should KRI plan on spending more than \$8.5 million this year. If they go over this amount they do so at their own risk of not getting paid for the amount above \$8.5 million.

(SR4, 190 at 1; tr. 1/101-03, 109-22) After the Partnering Meeting and related discussions that day with Corps personnel, it was Ryan Pleas's understanding that:

So, in other words, if you had eight and a half million dollars, you have to figure out...how much it would cost or how much you should reserve....

²¹ Ryan Pleas testified that the handout he received during the Partnering Meeting was a pamphlet, identified by the Corps as the PIL (tr. 1/101). KRI's Swantz agreed (tr. 4/59-60).

You take how much the termination costs are, you subtract that from the total amount of funding that's available and you end up with an amount that you can actually use to do the work.

....

[I]f we went through and spent—say we had an eight-and-a-half-million-dollar cash flow schedule...and we just went ahead and did the eight and a half million [of work] and at the end of the season they terminated our contract, we would get nothing in termination reimbursement. There would be no money left.

....

Well, it was obvious to everybody that this was going to impact our work plan. So, we were talking about we needed to adjust our work plan in order to be able to leave enough money for a possible termination.

And at this meeting,...they're telling us there is no guarantee, you know. They're hopeful they're going to get more money, but there is no guarantee.... I've never come into a contract like this with the Corps where they're right up front telling us they got a funding problem....

Of this magnitude, I mean,...it's like they're telling us that they got to put this clause in our contract and no guarantee that Congress is going to come up with any more money. So, you guys need to make sure you stay within that funding cap, including you need to leave yourself room for termination costs.

So we talked about in the meeting some options..., what we could do to tailor back our plan.

....

Well, one of them was—and it was actually the Corps' suggestion, was to postpone the dock and bridge.

Later on we had discussions I know Kelly [Pleas] and I had discussions specifically with [PM Wierzbicki]. I know it's not in the minutes, but during break we were batting around different ideas. And one of them was the

[PIL]—right in the [PIL] they'd say talk to the—work with the contractor, talk to them about starting later.

And so, we asked that question and, you know, he didn't show any objection to it.... [O]ne of the questions we asked him was what would be your preference? Do you want us to show up early, hit it hard and then go home early, or do you want us to be there longer...so that you have a chance to get the funding?

And his preference was for us to stay there longer. And so, that was his advice is I would stay there longer and do what you got to do because...the funding may not come for a while. I can't tell you when it's going to come, but, anyway, those were the kind of discussions we had.

....

We talked about starting later. We talked about cutting back to one barge. What we were trying to do is come up with a way that we could stay out there and end up at the end of the season building something that...would stand up over the winter. But also if they had terminated the contract, would be in a condition or in a state that would be easy to come back and finish whether it be on our contract or somebody else's....

....

[W]e talked about that we were going to...have some cost impacts and that we would have to sit down and figure that out and come up with a way to get reimbursed for it.

....

My recollection [with respect to the Corps promise to send a letter by 14 April 2006 indicating their preferences for work to be done in the first work season] is the Corps agreed that they would huddle amongst themselves and figure out a plan of how they wanted us to proceed or how they wanted the work left [at the end of the season]....

...Once we got their preferences, we would sit down and come up with some options and figure out—well, we'd

have another meeting with them. The next partnering meeting we would sit down and figure out a plan of action to go forward.

....

Well, one thing we knew is that we didn't want to get caught without enough funding to cover our termination costs because it was pretty much drilled in our head in this meeting that funding was definitely not a for sure thing and they still had to deal with Congress on it. But at the same time, they were hopeful that maybe they'd get some other money into the contract.

So, anyway, our thought coming away from the meeting was that we've got to make sure that we plan this so we leave enough reserve so that, if they do terminate the contract, that we end up not having to come out of our own pocket to fund the project.

....

[W]e knew...we were going to have to slow the job down. We wouldn't be able to perform as much work based on the current, the funding level that they had established at the meeting.

....

...I came away from the meeting that they basically were telling us you better start planning your work for this funding cap because it's coming, it's definitely coming, and we might as well be all on the same page and start adjusting your plan right now. I mean, that's what we were talking about in the meeting. I mean, we talked about changing our plan in order to accommodate this funding cap. [There was no discussion that KRI should wait until the contract was actually modified to include the Incremental Funding Clause.]

(Tr. 1/103-07, 112-14, 122-25; *see also* tr. 2/35-36, 57-58, 3/121-26, 4/60-67, 90-91, 8/145-47 ("It was communicated to us that termination was a possibility."))
CO Williams agreed that, at the time of the 3 April 2006 Partnering Meeting, the Corps was not certain of additional funds beyond the \$8,350,000 the PM already had

and which were not actually reserved to the contract until 26 April 2006 (*see* finding 39; tr. 13/56-58).

35. KRI's Ryan Pleas expressed his primary concern about the Corps' post-award change of the funding clause in the contract:

I just don't see how somebody can – or a contracting officer can just – they make a change to something so fundamental and important to the contract.

In other words, I mean, if...that project had that IFC clause in it before we bid it, I could have assessed the risk and I might have said, "You know what? I don't know if I want to bid this job." I can't take that kind of risk, or if I bid it, I'm going to put a bunch of money on it because the IFC clause, especially in a contract that's remote in Alaska, is a whole different duck.

Under the continuing contracts clause, we don't have to – we're not worried about the funding stream.

(Tr. 5/154)

36. KRI's planned cash flow (i.e., revenue) schedule was based on KRI's planned performance of contract work shown in its construction schedule. The construction schedule included only items of work required by the contract. As a result, the cash flow schedule based upon KRI's work plan did not include anything for possible termination for convenience costs or REAs/claims. (Tr. 1/103-04)

37. The Corps never sent KRI the letter it promised by 14 April 2006 (finding 34) expressing its preferences for the work to be completed in the 2006 construction season. There were also no meetings between the 3 April and 5 May (finding 40) Partnering Meetings in which there was discussion with KRI on the subjects of amendments to KRI's work plan or the amount of funds then reserved to the contract that KRI believed it necessary to set aside for possible termination, changes and/or claims. (Tr. 13/187-89; *see also* tr. 1/137, 6/145-46) In the absence of the promised input from the Corps as to what work it preferred be performed in the 2006 construction season, KRI proceeded on its own to develop an alternative work plan for FY 2006, taking into account that all costs including requests for equitable adjustment and termination for convenience costs had to come from the \$8,350,000 reserved to the contract for FY 2006 (SR4, tab 11 at 125; tr. 5/63-65).

Forecasting the necessity of reserving an allowance of approximately \$3.8 million to \$4.5 million for reserves in order to cover demobilization, equitable adjustments and

termination expenses, KRI scaled back the amount of construction that it could perform in 2006 in order to stay within the mandated funding restriction.

(SR4, tab 5 at 16-17; tr. 1/125-34 (details of reserve; always kept \$4 million in mind), 152-55, 3/121-22, 138-46, 154-63, 4/97-98, 167-69, 175-94, 7/207-08)

So the schedule that we had prepared and turned in,...didn't apply anymore. But the problem is...that if you change the schedule you don't get paid because you have to have an approved change or a mod to the contract to make a change to the completion date.^[22]

So we would make our schedules up showing the original January [2008 completion] schedule, as far as a two-year schedule, 2006 and 2007. And then part of the scheduling process is every month or every time you turn it in for a pay request is that you update the as-built portion. So the schedule reflected what was actually going on accurately in the field, but it was showing the original \$19.7 million contract over a two-year period.

So the issue we had was I don't know if we're getting funding tomorrow. I don't know if we're going to be terminated. I don't – you know, we're not sure how to change the schedule until we've come to an agreement with the Corps what the plan is going forward.

So, anyway, that 2006 period was...a period of time where we basically had to live with the original schedule [for purposes of payment].

....

We didn't know or we didn't have any word on funding, so we didn't – again, we still don't know what we

²² In order to be paid for the work it was doing KRI had to submit schedules that showed the original contract completion date (CCD) because the Corps would reject any schedule that showed a later projected contract completion date as a result of the Corps' request for a later start and the change in planned work due to the possibility of a termination for convenience if Congress did not appropriate more funds for the project beyond what was then already on the contract. As a result, KRI continued to submit schedules showing the original CCD as required by the Corps but included a note on each stating that they were inaccurate and why that was the case. (SR4, tab 14 at 2203; tr. 8/72-80, 91-94)

have. We don't know if we're getting terminated. We don't know if we're going to end up with a funny contract. We're just kind of in limbo land.

(Tr. 1/155-57; *see also* 3/164-65, 176-77, 4/97-98, 7/196-97; *see also* finding 68)

38. At the time of the 3 April 2006 Partnering Meeting, rock was being stockpiled by Northern Mechanical at the quarry at Dutch Harbor. KRI was concerned about having enough funds on the contract to pay its rock supplier, given the change of funding clause in the contract and the resultant changes in KRI's construction schedule which then forced changes in its cash flow schedule. (SR4, tab 20; tr. 1/115-16, 153-54, 3/74-85).

39. On 27 April 2006 the Corps issued unilateral Modification No. P00004 which added \$2,450,000 to the contract, bringing the total funds reserved to the contract to \$8,350,000 (SR4, tab 14 at 2018-19). As of 18 July 2006, KRI had not received a copy of Modification No. P00004 even though it had been asking CO Williams for a copy since at least 14 June 2006 (SR4, tab 34 at 1-7). Due to the funding limitations imposed by the Incremental Funding clause, it was important to KRI to have copies of the actual modifications showing the funds on the contract:

When you get closer to the end of the season and they're telling you they got \$3 million and we're running up to the stop amount where we have to stop, I want to see the piece of paper, because I don't want to overshoot and end up having a shortfall if they cancel the project.

I like to see the piece of paper. You know, early on in the season, you know, you expect that the mod will come in in enough time that you don't have to again slow down even more.

(Tr. 3/184) More important than KRI's preference for a formal contract modification to memorialize the addition of funds to the contract, the IFC-5004 which was unilaterally added to the contract by the Corps, required that the only valid notification of additional funds reserved to the contract that a contractor was entitled to rely upon was a formal contract modification (*see* finding 31).

40. The second Partnering Meeting took place on 5 May 2006 as previously scheduled. The scant two pages of meeting minutes are as follows:

- (1) **Funding Increase/Continuing Contracts Clause:**
The Corps indicated that contract funds are now available in the amount of \$10.5 million, and that this amount includes all changes and any

termination costs.^[23] The Corps also stated that it expected another \$5 million to be available on October 1, 2006. KRI advised that its cost of \$10.5 million for work this season does not include demobilization or termination costs. The Aleutians East Borough (“AEB”) advised that they will have an additional \$4 million in sponsor money available. The Corps indicated that they could send KRI a letter advising it that this additional sponsor money was available. KRI stated that they needed to receive that letter by August, 2006. The Corps indicated that the “continuing contracts clause” modification was not ready to be issued. There was discussion concerning whether that mod would be issued as a unilateral mod or whether the Corps would attempt to negotiate a bilateral mod.^[24] Given the current status of funding, it was not necessary to resolve that issue at this meeting.

....

- (3) **VE Proposal:** The Corps indicated that it could not accept the VE proposal based upon the information it had been provided to date. After some discussion, it was concluded that the Corps wanted a VE proposal that complied with FAR 52.248-3. Garth Howlett and Alan Christopherson from the engineering firm PND^[25] joined the meeting to

²³ This statement is contrary to the evidence. As of 5 May 2006 there was \$8,350,000 in funds on the contract. Additional funds were not put on the contract until Modification No. P00006 brought the total funded amount to \$10,450,000 on 19 September 2006 (findings 16, 58)

²⁴ Ryan Pleas testified that the “discussion” was actually an argument between CO Williams and PM Wierzbicki (tr. 1/143, 146-147). The record before us shows that it was PM Wierzbicki’s position that a bilateral modification was required (*see* finding 29) and that CO Williams chose to believe otherwise (*see* findings 30, 43-46).

²⁵ PND Engineering was the owner of the patent on the open cell dock which used “so much less steel” than the Corps’ design in the contract as awarded. However, the Corps was familiar with PND’s patented method of design and required additional assurance of safety factors before the design could be approved. (SR4, tab 10 at 80-81; tr. 4/54-57, 161, 14/213-17). KRI engaged the PND

present information concerning the VE proposal. PND indicated that it could provide the requested package within four to five weeks, and that it would also provide to the Corps its previously negotiated patent language. The Corps indicated that it needed one week to review the VE package. KRI indicated that it would provide a hard dollar number for the VE proposal savings.

- (4) **Dock Plan:** The AEB indicated that the plan for the dock was acceptable to the customer, and a meeting was scheduled for Friday, May 12, 2006, to see if additional moorage could be added on the south side.

....

- (6) Other:
KRI plans on putting rock in the water starting June 15-21 through early September, 2006.

(SR4, tab 13 at 7-8, tab 14 at 2391-92, tabs 115, 190 at 3-4; tr. 1/137-48, 4/64-68, 90, 7/59-61, 7/196-97 (PM Wierzbicki said if the Corps didn't get more funding, the contract would be terminated))

41. KRI commenced project work in accordance with its amended work plan, starting work in July 2006 instead of the 15-21 June start discussed at the 5 May 2006 Partnering Meeting, and with a "scaled down" operation to allow it to continue working for as long as possible in the 2006 construction season. We find no record of any contemporaneous objection from the Corps as to KRI's amended planned start date or its actual start date. KRI concentrated its efforts in the 2006 construction season on installation of the core rock for all three of the breakwater structures. (SR4, tab 19 at 250; tr. 3/126, 4/92-95, 5/45-57; *see also* SR4, tab 16 at 37, 39, 92-93, 210, 212, 7/197-202) The Corps' schedule expert Mr. Ockman opined in his expert report that KRI's "late start" in 2006 was caused by KRI's "failure to gear up at the site." He further opined that, as a result, KRI was responsible for 29 days of delay. (SR4, tab 19

engineers on a time and material basis because KRI wanted to keep the VECF design "alive" but KRI could not be sure, until additional funds were appropriated by Congress and added to the contract by the Corps, that the False Pass contract would not be terminated for convenience (tr. 1/157-58, 4/78-79).

at 250) In his testimony, however, he found KRI's July 2006 start to be "ambitious, but reasonable" (finding 49). We find that KRI's start of work at the jobsite in 2006 to be due to the Corps' unilaterally-imposed funding changes to the contract and to be in accordance with the expressed preference and agreement of PM Wierzbicki (*see* findings 26, 34, 40). It was Mr. Ockman's opinion that "[t]his one delay, alone, would have pushed [KRI] into a third construction season" (SR4, tab 19 at 283).

42. After the 5 May 2006 Partnering Meeting, there was no communication from CO Williams to KRI about contract funding until a 9 July 2006 email (tr. 4/80) to which, without any additional discussion or negotiation since the Partnering Meeting, was attached a draft bilateral Modification No. P00005:

As we discussed in our last meeting, attached is the modification which deletes the old Continuing Contracts clause and replaces it with the new Incremental funding clause. This mod also serves as documentation showing the amount of funding currently available on the contract. The project manager is continuing to search for more funding, but as we discussed in the Partnering Sessions, additional funding will have to be added by congress. We do not have a timeline on the availability of additional funding, but it could be as late as early next Fiscal Year (mid October 2006). If you have any questions, please let me know. Please let me know if Kelly-Ryan is willing to sign the modification. If Kelly-Ryan is unwilling to sign the modification, I will have to issue the modification unilaterally. This mod does not remove your rights to submit a Request for Equitable adjustment and/or claim. In accordance with the clause, \$10.5 million is all the funding we currently have which includes any termination or claim costs. If you have any questions, let me know. I will be on leave starting Wed, July 19, 2006, and would like an answer either way before then.

(SR4, tab 14 at 2342-47, tab 34 at 6-8, tab 155 at 11) KRI declined to sign Modification No. P00005 because it did not include or acknowledge any monetary or schedule impact as a result of the clause (SR4, tab 14 at 2124, 2126, 2325; tr. 1/158-64, 2/28-32, 3/180-82, 4/82, 13/49).

There was never any option. It was this is the mod, here, sign it. There was never any negotiation, never a discussion about it other than here it is, sign it. No time, no money. Just sign it.

(Tr. 3/180-181) One week later, on 17 July 2006, again without discussion or negotiation, Modification No. P00005 was issued unilaterally by CO Williams (SR4, tab 34 at 6-7, tab 14 at 2339, 2126).

43. CO Williams was aware of EC 11-2-189 and the PIL, as well as specific direction within the Corps, that he was required to either negotiate a bilateral modification or terminate the contract for convenience (*see* findings 23, 29-30, 44). Nevertheless, he admitted in testimony and documentary evidence that he did not respond to requests for funding modification information from KRI and that he had no contact or discussion with KRI between the 5 May 2006 Partnering Meeting and his 9 July 2006 email forwarding the draft bilateral modification. CO Williams admitted that the entire extent of his “negotiation” with KRI on the subject of a bilateral modification to change the funding clauses consisted of his 9 July 2006 email statement, “Please let me know if [KRI] is willing to sign the modification.” If KRI declined to do so, he believed he had no choice but to replace the Continuing Contracts clause with the Incremental Funding clause by unilateral modification. (SR4, tab 14 at 2124-28, 2284-85, 2289, 2339, 2348; tr. 13/194-219, 221-26, 14/21-22)

44. By email dated 28 July 2006 Corps attorney, Michael Gilbert, notified Christopher Tew, Alaska District Chief of Construction, that:

The issue concerning unilateral modifications for continuing contracts was raised during yesterday's PRB. The two contracts involved are False Pass and Sand Point. Our office was not consulted, and did not coordinate, on the False Pass modification. We do not know if the Sand Point modification has been accomplished. We believe the False Pass contract was incorrectly modified on 17 Jul 06 by Dave Williams of your office. Accordingly, based upon PARC guidance, you should cancel the unilateral modification and either negotiate a bilateral modification or terminate the contract and reprocure as a fully-funded contract. Please advise us of what corrective action you decide to take and if we can assist you in this matter.

Attached is our 23 Mar 06 legal opinion, which was based upon a 22 Mar 06 PARC memo, that responded to a query from RM with courtesy copies to PM and CT. I also have attached a 21 Mar 06 e-mail that suggests [CO Williams] was aware of the prohibition before the modification was made. What personnel action you take, if any, is at your discretion, but I suggest you look into this apparent violation of failure to comply with law and policy

guidance. I also send you this information for you to discuss with your staff and address with on-going contracts.

If we can assist, please let us know....

(SR4, tab 14 at 1989, tab 166 at 30)

45. On 8 August 2006 CO Williams told Mr. Tew and CO Davidson that “[a] possible solution to this would be to rescind the unilateral modification. Since I know the contractor will not sign the bilateral modification [without an equitable adjustment including time and/or money], we could continue to ‘negotiate’ the bilateral mod.” (SR4, tab 14 at 2279; tr. 14/29-30, 33 (he couldn’t explain why he put “negotiate” in quotes)). Mr. Tew responded: “At the end of the day, if the contractor won’t sign a bilateral action, then we have 2 choices – terminate or seek a waiver per the PIL” (SR4, tab 14 at 2279; tr. 14/33-34). CO Williams ignored both choices and did nothing to rescind the unilateral modification or to otherwise follow the Corps’ guidance/direction (tr. 13/53-54).

46. In addition, contrary to all express guidance and direction otherwise, after he specifically elected not to negotiate a bilateral modification, CO Williams also made the conscious decision not to consider a termination for convenience:

At the time I sent [P00005], I decided not to pursue a [termination for convenience] until we were sure we would not receive funding for FY07. During the period of July 17, 2006 when the unilateral modification was issued until the full funding was added March 19, 2007 I was in continuous contact with the [Corps] PM in regards to funding for FY07 and we were assured by congressional staffers that full funding would be provided for this contract. Unfortunately, we could not pass this information along to the contractor until the funding bill was signed. In an email from [Corps Office of Counsel on 28 July 2006] it was recommended that I rescind the unilateral modification. In consultation with the PDT²⁶, I made the decision to not change the funding clause or start a Termination for Convenience process until we knew the funding status for FY07.

(SR4, tab 14 at 2124, 2126; tr. 13/225)

²⁶ District/Center Project Delivery Team (PDT). EFARS 1.170-100(d).

[B]ut in my mind we have failed if we terminate a contract. Now we no longer have a project. Our sponsors, Aleutians East Borough, is not getting a harbor, and who knows when they will get a harbor?

So, in my mind, I never really considered terminating the contract at this point in time.

....

...[T]erminating a contract at this point in time is a very high likelihood that the contract will not get refunded and be completed.

(Tr. 13/44-45, 209, 220) The Corps had been trying to get the False Pass project funded for ten years (finding 2).

47. Mr. Loew, CECW-I (finding 20), described the process to be used if a Corps district needed help applying the new funding policy:

The process would have been for them, let's just say they needed reprogramming support, would have been to look inside the district to see if they had funds available, and then if they didn't[,] seek their division's help and if division couldn't do it, then they would come to my office for help.

I am not aware of any cases where districts came forward and needed the help that they didn't get it.... In the first partnering meeting minutes, which I read, I thought that the district was on target at that point.

They had read the guidance. They said they were going to work through a bilateral modification. They recognized that the contractor had additional costs, and it just appeared to be a matter of time, and in fact I think they were setting that to be resolved at the next partnering meeting, which took place in early May.

Then things went south 180 degrees, in my opinion. They never got with the contractor. I mean this was serious enough on this contract, and I say on this contract, because as has been explained, there are tremendous logistical problems associated with work in the Aleutians, to get your equipment out.

You had to do early planning and you have to have stuff on site at the beginning of the construction season,

ready to go to take advantage of that construction season. So I guess I'm trying to point out that the contractor not only needed the money, but he needed [it] well [in] advance of the place he was going – at the point in time he was going to place it.

For instance, he needed the money to order the steel for a year before that steel was going to be on site. So he had to commit, and this clause clearly created funding uncertainty. What should have happened, in my opinion, and they would be typical program project management practices that everybody does all the time.

The district should have gotten with that contractor, and when I say the district, I mean the project development team, which includes the project manager, in this case Contracting, in this case Construction, Engineering. They should have sat down with that contractor and say well okay, you're projecting that there's going to be a funding deficit in the middle of the first construction season. How much money is that? What is your deficit?

They should have entered into a negotiation at that time. They should have nailed down the amount of money, which at that time, my reading, was very small. Somewhere between one million and four million dollars they could have solved that problem that day.

They didn't do that, and I mean it's not understandable why they didn't, but they never got with the contractor. They never put a number that they could work with to handle the reprogramming or anything else, and so then it just, you know, continued to go south in my opinion.

(Tr. 7/100-02)

48. In the period from 13 July 2006 to at least 19 September 2006, termination of the contract for convenience was a possibility due to no additional funds from Congress (SR4, tab 14 at 2127, tab 118; tr. 14/68-73).

49. The first schedule KRI submitted (with Pay Estimate #2) after Modification No. P00005 had a data date of 30 July 2006 (SR4, tab 16 at 21-72, tab 19 at 301-02). The cash flow estimate showed earnings from placing core rock beginning in July 2006 and contained the following note prominently displayed on both pages:

The above cash flow is based on the current billable projections and DO NOT include liabilities associated with modification P000[0]5.

(SR4, tab 16 at 48-49) KRI decided to use one rock transport barge, instead of the two originally planned, and to place only core rock for all three breakwaters in the 2006 construction season (SR4, tab 5 at 18-19; tr. 1/149-51, 3/126, 4/67-68, 72-74, 93, 6/149-53, 7/206, 220-21). KRI planned to place as many lineal feet of core rock as possible in 2006 in order to have the project in the best possible position for breakwater completion and dredging in the 2007 work season, assuming funding was received for FY 2007. KRI's alternative schedule "left options open in the event the Corps added more money to the contract in 2006." (SR4, tab 19 at 1186-87) The Corps' schedule expert, Mr. Ockman, testified that this alternative work plan schedule was "ambitious, but it was reasonable" and "very similar to their original plan" except that they started one month later (tr. 12/88, 93-96).

50. The Corps elected not to provide input to KRI to assist it in making decisions about preferred work for FY 2006 (finding 37; SR4, tab 11 at 374; tr. 1/152, 4/64), and we have found no evidence that the Corps, either its onsite or offsite personnel, ever objected during the 2006 construction season to KRI's amended work plan or the work it accomplished (*see* SR4, tab 19 at 1188; tr. 6/153). Not until one month *after* KRI had demobilized from the jobsite at the end of the 2006 construction season did the Corps mention a concern about leaving only core rock in the breakwaters over the winter (finding 61).

51. KRI was told repeatedly by the Corps to be sure to set aside from the funds reserved to the contract an amount that KRI estimated would cover any termination for convenience costs and potential claims (*see* findings 34-35, 37, 40).

[KRI was] told...in the meeting that it was up to us to figure out how much we needed to reserve and just make sure that you watch, you know, watch your ass because it's on us. I mean, if we run over, I mean, if they shot the job down, it was made very clear by [PM Wierzbicki] that if they shut the job down, if you don't have enough left in your contract to cover termination, you're not going to get reimbursed. He made that very clear.

And so, you know, he didn't really care how we did it. He wasn't asking to be involved in the calculation. He just said you guys need to understand that the Corps is doing business differently now, and we can't do it the way we used to with this new [Incremental Funding] clause. So

we took him seriously, and we came up with our own idea of what we thought and then planned accordingly.

(Tr. 1/133-34) We have found no evidence in the record that the Corps ever required KRI to provide, nor even asked KRI, for the amount of reserve it had calculated, even though CO Williams testified that such information would have been "very important" (tr. 1/135, 13/68-69, 14/49). CO Williams testified:

Well, we never discussed dollar amounts that he would have to hold back. I mean we made it clear that all the costs he thought he would need for termination would need to be part of this reserved amount that was indicated in these minutes.

....

Potentially [the contractor had the risk if he made the number too low], but..., I would expect that a heavy civil contractor doing this type of business for many years should have a pretty good estimating system. So, one would think he could do a pretty good job estimating his costs, especially since [t]he demob costs were already priced in the contract.

....

...There's never any obligation for the contractor to spend up to the amount of money on the contract that we've reserved. And he can earn up to that amount, but if he decides on his own to prosecute the progress differently to where his earnings don't go up [to] that level, there's no requirement on the government's part for them to earn up to that point....

Obviously, when the contract is completed, he will bill for the full contract amount as funded. But we're not going back to say, "You're spending too little. Spend more."

Q And obviously, if he feels it is good business for him to save a cushion so that he doesn't overspend the funded amount, that's okay too, isn't it?

A Yes.

Q That's his prerogative, correct?

A Yes.

Q And that's because he's got the financial risk, doesn't he?

A Yes.

....

...I will say [the contractor] has to account for his [potential] termination costs if he feels he's going to incur them and keep that amount of money set aside in the unfortunate event that we might have to terminate the contract.

(Tr. 13/178, 184-85)

52. The amount of available funds reserved by KRI at the Corps' direction to cover possible termination for convenience and claims (*see* finding 37) complicated the requirement in both the CCC and IFC for contractor notification to the Corps prior to exhaustion of funds.

[Y]ou don't actually exhaust the funds. That is why I say you have to take into consideration the reserve for the termination cost.

So, it is a little confusing because yes, they have \$10.5 million for the job but we can't use all of it for construction. You have to hold some in reserve for termination. So, I guess it depends on how you define exhaustion, whether maybe you have to include the termination for convenience, money that you may have to draw on if they terminate the contract. You have to anticipate that might happen. So, that is kind of the way I looked at it. I thought we had to look at it that way.

....

We would not use all of the funds for construction in 2006. We would have to hold or not draw some of those funds and leave them there for a possible termination.

Q So, still looking at paragraph D of the incremental funding clause attached to Mod 5, how did you handle the 120-day notice provision?

A Well, at this point, this was issued in July, there wasn't 120 days left in the fiscal year. So, I think there was I don't know, 70 something days left. So, we

couldn't comply with the 120 days. We did send a letter shortly after this was issued explaining that it wasn't possible to give them the 120 days' notice.

....

...[T]he fiscal year is September 30, the year-end. And it was about mid-July when this was issued. So, there wasn't 120 days. When this was issued, there wasn't 120 days before the fiscal year-end. There was no way to comply.

(Tr. 2/32-34) KRI notified the Corps of this complication by letter dated 3 August 2006 (SR4, tab 11 at 19, 121, 125; tr. 2/36-45, 3/188-90, 5/62-63, 14/52-58).

[W]e wanted to know if the Corps had any preferences on how they wanted the work site left, you know what state they would like us to leave it in. We thought that it would be prudent for them to have input into that since we are not sure whether we are coming back next year.... We [also] didn't want to have our [rock] supplier end up making rock that we couldn't pay them for, basically.... We don't want to get into a situation where we end up having to pay out-of-pocket if this job gets terminated.

(Tr. 2/45-47) CO Williams acknowledged KRI's letter and agreed a meeting was warranted, however, despite KRI's numerous attempts to schedule such a meeting, no meeting on this subject was ever held (SR4, tab 120; tr. 2/41-42, 47-48, 5/59-62).

53. As early as the April and May Partnering Meetings, and in numerous phone calls and letters, KRI had advised the Corps that additional funds would have to be committed to the project by August 2006 or the project would have to be shut down two months earlier than planned (SR4, tab 11 at 121-22, 125, tab 14 at 2391; tr. 1/140-41, 2/42-45, 4/90-92).

54. On 23 August 2006 KRI again requested input from the Corps:

We would like to request that a conference call take place Thursday of this week as was suggested yesterday. It is important that we get into the details with the Corps because our figures indicate that funding will be exhausted within the next couple of weeks. We want to discuss how

to handle the shutdown of the work. Our view is that the Corps should have input, and our course of action necessarily will be influenced by how the Corps assesses the potential future of this contract.

We had a lengthy conference yesterday with our rock supplier. He also will be affected by the shutdown, and mentioned unamortized front-end costs and the added cost of a demobilization. You can appreciate our concern that allowing him to continue producing rock, at this point, rapidly exhausts the limited remaining funds.

We see the objective of tomorrow's call as reaching an understanding upon a course of action that serves the interest of all parties. At the same time, that course of action has to assure that the \$10.5 million of available funds will not be exceeded. We are proceeding in accordance with the unilateral modification, treating it as a directive that under no circumstance should there be any costs incurred on or in connection with the project that exceeds the \$10.5 million funding cap.

We obviously will respond to any questions or concerns you have and will be prepared to deal with any form of expanded agenda you may think is appropriate.

(SR4, tab 11 at 125; tr. 3/147-49) Later that same day, CO Williams advised by email that "we are in the process of receiving \$3.0 million from the Department of Transportation" (*see* finding 55) and that "for planning purposes, the current contract funding is \$13.5 million" (SR4, tab 24 at 165; tr. 13/45-46, 61-62, 14/65-68, 73-74). However, the contract's IFC clause specifically required that the only valid notification of additional funds on the contract was a formal contract modification²⁷ (finding 31) and KRI conducted itself accordingly (*see* finding 39). We find that, as of 23 August 2006, the contract was actually funded in the amount of \$8,350,000 (finding 16).

55. In early-September 2006, the Corps was in contact with the Department of Transportation (DOT) regarding \$3,000,000 in DOT funds for the False Pass project (SR4, tab 14 at 2262, tab 165). The record shows that DOT was prepared to send the funds to the Corps in early-September 2006, however, the Corps advised DOT that they could not complete all the paperwork to obligate the funds to the contract before the close of the fiscal year and requested that DOT "[w]ait until next fiscal year and send it when you can" (SR4, tab 34 at 8, tab 165 at 24). The DOT funds were not added to the contract by the Corps until 1 March 2007 (finding 65; tr. 3/150-51).

²⁷ The CCC clause had the same requirement (finding 9).

56. Hesitant to expend more contract funds in the absence of a modification actually reserving funds to the contract, KRI then shut down for the winter and demobilized from the jobsite on 15-18 September 2006 (SR4, tab 17 at 416-36). This was only slightly different from its original and amended 2006 plans (SR4, tab 18 at 10, 14, 19; tr. 16/69).

57. During the 2006 construction season, Northern Mechanical at the Dutch Harbor quarry was “not getting the yield of armor stone that he had hoped for” so KRI went to its “backup plan, which was Western Marine’s Sand Point Quarry” (SR4, tab 10 at 50-51, tab 19 at 1194-95; tr. 2/54-56, 4/82-86; *see* findings 5, 27).

They had a pit there and they were making exactly the same products. There was another boat harbor being built 160 miles away to the east. And that was one of the beauties of bidding the job at the time we did at False Pass was we had two great sources of rock 160 miles on either side of our project. And so, the problem was that by not having the funding available to cut a [purchase order] for that, their job finished at the end of 2006 and they de-mobed out of the pit [back to Seattle].

(Tr. 2/54-56, 7/217-18; *see also* SR4, tab 24 at 158-59)

58. On 19 September 2006 the Corps issued unilateral Modification No. P00006 which increased the contract funding from \$8.35 million to \$10.45 million (SR4, tab 155 at 15). CO Williams described the surrounding circumstances as:

[PM Wierzbicki] stated that the additional \$3.0M will be transferred from DOT in early next fiscal year. Any termination actions or further discussion with the contractor have been postponed until we get word of passage of the congressional bill that should contain additional funds for False Pass. If additional funding is not received by early next calendar year, we will begin discussions with the contractor on either extending the contract[] or terminating it.

(SR4, tab 14 at 2127)

59. Because of the remote location and short construction season, advance planning and preparation over the winter 2006/2007 (October through March (finding 8)) was particularly important (finding 1). KRI’s expert witness Mr. Egbert testified:

The lack of funding really deprived [KRI] of the opportunity to plan for and to perform or make the advance obligations and cost commitments that it needed for the 2007 season. So the time frame is that the – [KRI] operated under the – operated since the May partnering meeting with the thought that they were going to have a funding cap of [\$]10.5 million, and that existed up until March of 2007.

So [KRI] looked at the fact that they had spent \$6.1 million or something like that – not spent. They had earned. The earnings under the contract were [\$]6.1 million,^[28] and doing the math, you've got – you've got [\$]4.4 million available. So you've got the [\$]10.5 million funding cap and subtract [\$]6.1 million that's been earned under the contract, and there's a little over \$4 million left.

You subtract, if the contract ended that day, then [KRI] would have to demobilize. Well, the balance of their demobilization line item on their application was \$1 million. So that \$4 million that's left is now down to \$3 million, and they would have to pay for the rock that's been produced in the quarry but not paid for.

How much does that cost? Well, that's really an unknown cost and that's a judgment call. So say it's [\$]1 million. So now...you're left with \$2 million. You've got [\$]13 million dollars' worth of work to perform and \$2 million in the bank.

So you really can't go forward with very much. I mean you could order bridge and dock materials, but then you can't – you don't have any money to fund any labor on site. If you go to the site, it can't do much. You can't put a dent in a \$13 million scope of work with \$2 million.

So [KRI]'s hands were really tied. From the time they demobilized in September of [2006], [KRI]'s hands were tied until March 1st of 2007, when another \$3 million or so was put into the contract.

(Tr. 6/152-53, 155-56, 162-64, 7/223)

60. On 16 October 2006 KRI notified CO Williams that, in order to prepare for the 2007 construction season and make timely commitments for transportation, crews and

²⁸ Pay Estimate #5, signed by ACO Jong, shows \$6,101,361.70 earned for work performed under the contract as of 4 December 2006 (SR4, tab 16 at 200).

materials, KRI needed to know by mid-November 2006 whether funding for the rest of the project was available. CO Williams did not respond to KRI's request (*see* finding 45 (Corps had reason to believe that full funding of the contract in 2007 was likely but did not share that information with KRI)). (SR4, tab 11 at 374, tab 19 at 1189-90, tab 190 at 5, tab 192 (PART 1) at 19; tr. 2/58-66, 3/191-95, 4/91-94, 7/210-11)

61. On 17 October 2006, a month after KRI had demobilized from False Pass for the winter (tr. 3/191, 4/92), the Corps expressed concern by letter about leaving just core rock in the breakwaters over the winter (SR4, tab 10 at 54), however:

[W]e asked the Corps for their input. You know what, during this whole period of time, all of 2006 [construction season], they gave no input. None. So you know, we did what we thought was the right thing to do. And we asked them on more than one occasion to give us some input, no response.

(Tr. 3/191, *see also* 7/197-98, 16/14-15) By doing so, KRI was able to complete all three breakwaters to the contractually-required minimum height so that dredging could commence "right off the bat" in the 2007 construction season and minimized the risk that rework of the rock layers would become necessary due to winter wave action (SR4, tab 19 at 1188; tr. 2/49-50, 4/90-92, 94-96, 6/152, 7/197-204, 13/64-65). Prior to demobilizing in September 2006, KRI performed an interim survey of the core rock placed in 2006 in the breakwaters and planned another survey if/when it returned to the jobsite in 2007 which, when compared to the 2006 survey, would identify any winter damage (tr. 13/64-65). Upon returning to the jobsite in 2007:

They've handled the winter just fine. There was very minor movement and only isolated to just a couple of spots and there was no material lost.

(Tr. 16/15) We have not found any evidence in the record before us, nor have the parties directed us to any, that the core rock placed in 2006 experienced any significant damage over the winter (*see, e.g.*, SR4, tab 19 at 1312; tr. 13/65).

62. On 29 December 2006 KRI sent a letter of concern to the CO:

We believe that a partnering meeting is in order. There are several pressing issues that require discussion and clarification. Most of the items on our agenda relate to funding, and the effect that the present funding limitation is having, and will continue to have, upon our materials

procurement, mobilization and work plan for the 2007 construction season.

The first order of business is to share with you our understanding of the present situation. In accordance with Modification P00006, the current funded amount for our contract is \$10,450,000. There has been much discussion regarding availability of an additional \$4,000,000. Our 3 August 2006 letter, Serial 019, requests that these funds be committed before October 1, 2006. This commitment was not made, nor was the Corps able to meet the November 2006 date which was suggested by your office as a likely point at which commitment of these funds would be forthcoming. Accordingly, as matters stand at year-end 2006, the \$10,450,000 funded amount still applies.

Further to that same point: Modification P00005, dated 16 July 2006, unilaterally deleted the Continuing Contract Clause from our contract and replaced it with the Incremental Funding Clause. KRI's position has been that the original contract cannot be altered unilaterally, and that KRI retains all of the protection and rights as may be applicable under the Continuing Contract Clause. On the other hand, we understand the Corps' Modification Action to mean that you intend to administer the project as though the Incremental Funding Clause was part of the contract.

With that background in mind, we have analyzed our work plan and schedule for the 2007 construction season. The schedule submitted on 26 October 2006 indicates a mobilization start on 1 April 2007, with construction on the east breakwater starting one month later. That schedule submission bears a caveat stating "Schedule is predicated on a timely notification of sufficient funding to purchase materials and secure related equipment, anticipated to be mid-November per our conversations."

Based upon our present cost forecast, and having in mind the restrictions described in the Incremental Funding Clause, a \$10,450,000 funding cap effectively forecloses KRI from performing any work on the breakwaters during the 2007 construction season. This conclusion is based upon the following calculation:

As of 12/ 27/06 amount funded	\$10,450,000
Payments to date	<u>6,101,361</u>
Available Funds	\$ 4,348,639

Items payable on or before 2007 mobilization	
Armor Rock to be billed	\$1,200,000
B Rock to be billed	500,000
Core Rock to be billed	510,000
Activity 74050, bridge materials (bid)	440,000
Activity 75050 dock material (bid)	1,347,000
TOTAL	\$3,997,000

Mobilization increment 4/1/07	<u>\$ 600,000</u>
Payable on or before 2007 mobilization	\$4,597,000

As these figures illustrate, there is a shortfall of \$248,361 (\$4,597,000 payable as against \$4,348,639 available funds equals \$2[4]8,361 shortfall). This does not take into account any termination or demobilization costs.

You can see why we are anxious to meet and explore the alternatives. If a partnering facilitator is not available, we should meet anyway with your key people and ours. KRI is prepared to work with you in developing the most cost efficient solution possible provided, of course, that KRI is not exposed to the financial risk of performing work for which we do not receive due and timely payment. We suggest a meeting anytime during the week of January 15, or the latter part of the previous week if you are able to assemble the necessary participants by then. Please advise[.]

(SR4, tab 11 at 135-36; tr. 2/53-56, 66, 68-72, 3/191-95) CO Williams thought KRI's suggestion for a meeting was "a good idea" (SR4, tab 14 at 2236), however, we have found no evidence such a meeting took place and CO Williams did not respond to KRI's letter of concern.

63. As of 4 January 2007 the Corps internally recognized a funding shortfall for the False Pass project of \$5,279,300, even after future receipt of an additional \$4 million from AEB (*see* finding 40), and was discussing ways to downsize the project because "the change in our current political situation has left this and many other projects without promising resolution for the funding short falls currently experienced" (SR4, tab 121). The Corps' project engineer Meyers described to ACO Jong the then-current state of the project, as well as its "Proposed Construction Direction":

Award date: 7-11-05

Award Amount: \$19,729,300.00

Awarded Options: \$3,748,300.00 (CLIN's 13-16 →
Bridge, Dock, Dredge to -5.334M,
and Dredge to -3.810M)

Performance Period: 890 calendar days

Contract Completion Date: 2-05-08^[29]

Current funding: \$10.45M

Potential additional funding: ~\$4.0M (Aleutian's East Borough)

Current Funding Shortfall: \$5,279,300.00

Construction Progress: Core Rock only has been
placed at all 3 breakwater locations

No breakwater has a complete
complement of placed core rock-
additional placement and shaping
will be required prior to the start of
B-Rock or Armor Rock placement

No dredging has been started

....

No inner or outer harbor fish
habitat construction started

No bridge work has started.

Proposed Construction Direction:

²⁹ This is an obvious typographical error, as the original contract completion date of 5 January 2008 had not been modified.

- Complete construction of South Breakwater IAW project plans and specs including:
 - Place balance of core rock for south breakwater and shape as required
 - Placement of B-Rock layer
 - Placement of Armor Stone layer

- Complete construction of North Breakwater IAW project plans and specs including:
 - Place balance of core rock for north breakwater and shape as required
 - Placement of B-Rock layer
 - Placement of Armor Stone
 - Construction of bridge as designed including all fish habitat requirements (to not construct the bridge at this time would be cost prohibitive in the future)

- Complete construction of East Breakwater IAW plans and specs including:
 - Place balance of core rock for north breakwater and shape as required
 - Placement of B-Rock layer
 - Placement of Armor Stone on the exterior edges of the northern and southern ends of the east breakwater as funding will allow

- Delay construction of the following items to another construction season (this will necessitate the execution of a contract extension mod and will included [sic] costs for move/de-move, KTR & Government housing/per diem costs:

- Mobe/De-mobe Costs → ~+\$1.7M estimated
- Construct dock @ end of Causeway → -\$1.952M → tear-off of Causeway end to facilitate construction will cost some \$'s, but may be off-set by savings from VE.
- Dredge & Stockpile to -5.334M → -\$608,400.00
- Dredge & Stockpile to -3.810M → -\$523,900
- Installation of Reef Balls, complete → -\$56,800.00
- Construct Nav-Aide Marker Base → -\$37,000.00
- Clear & Grub Disposal Areas → -\$37,500.00
- Hydro Surveys CLIN's 0002 -0008 → ~-\$98,000.00
- Dredge & Dispose Entrance Channel Mat'l → -\$939,300.00
- Construct Surface causeway surface layer → ~-\$21,000.00 surface layer from shore to bridge should be constructed this year
- Construct base causeway surface layer → ~-\$21,125.00 surface layer from shore to bridge should be constructed this year

Postponing the above mentioned items nets an initial reduction of -\$4,238,225.00 until the following year, but does not include the ~\$1.7M requirement for an additional mobe/de-mobe and camp costs for and [sic] additional year.

The estimated funding shortfall of \$5,279,300.00 less the available work item costs that can be postponed until next year of -\$4,238,225.00 still leaves a funding shortfall of \$1,041,075.00 → this means that ~\$1,041,075.00 worth of Armor stone cannot be produced or placed.

(SR4, tab 121; tr. 14/92-94) This information was not shared with KRI (tr. 2/74). We find that the Corps recognized that, due to the current funding at \$10,450,000, certain work would have to be deleted, descope or pushed into later years and that the Corps' estimate of shortfall at the time was much greater than KRI's \$248,361 (finding 62). We also find that neither KRI's nor the Corps' calculations of shortfall included potential claims or termination for convenience costs.

64. On 19 January 2007 ACO Jong, two weeks after he received the Corps' own state-of-the-project summary and funding shortfall calculation (finding 63), responded to KRI's 29 December 2006 letter (finding 62), and agreed that a meeting "was needed" (SR4, tab 10 at 62-63). The Corps suggested that a meeting take place over a month later "near the end of the third week in February 2007," by which time:

[W]e should have received word from Congress on the status of funding for this project and can clarify the funding and contractual issues you have.

(SR4, tab 10 at 62-63; tr. 2/72-73) A meeting did not take place until 20 March 2007 (finding 67; tr. 4/88-89), more than two months after KRI's requested meeting date of 15 January 2007.

65. On 1 March 2007 Modification No. P00007 was issued to increase the contract funding to \$13,450,000, reflecting the Corps' receipt of \$3,000,000 from the DOT for the False Pass project (SR4, tab 14 at 2127, 2259; *see* finding 55).

66. On 19 March 2007, one day before the scheduled Partnering Meeting (*see* finding 64), the Corps again unilaterally modified the contract. Modification No. P00008 added funds to make the contract fully funded in the amount of \$19,729,300, deleted the IFC and reinstated the CCC that had been in the contract at the time of award. (SR4, tab 14 at 2125, 2127, tab 155 at 19-20; tr. 13/72-75, 14/100-05) Until the issuance of Modification No. P00008, KRI could not be sure that the contract would be fully funded and not terminated. However, KRI's schedule had planned the start of the in-water work for the 2007 construction season to begin in April 2007 and, since the funding was not assured until the issuance of the Modification (finding 31 at (j)), none of the preparatory work normally performed

over the winter, such as making financial commitments to secure crew, materials and subcontractors for work to be performed in remote False Pass, had been performed.

March is too late in the year to begin planning for a mobilization and placing effort that same year, if you expect to function efficiently within the short construction season in the Aleutian Islands.

(SR4, tab 19 at 1201; *see also* findings 1, 59) As a result, KRI was only able to complete \$3,360,000 of the \$10,253,000 of the contract work it had planned for the 2007 season (SR4, tab 19 at 820, 823, 1189-90; tr. 9/53-58, 118-20).

67. In a letter dated 27 March 2007, KRI stated the following as a “follow up” to the 20 March 2007 partnering meeting:

This letter is a follow up to our March 20, 2007 Partnering meeting. We were relieved and gratified at that meeting to learn that funding for the balance of our contract work was available and that the Corps was deleting the Incremental Funding Clause which had been engrafted upon our contract by unilateral Modification P00005.

Raised and discussed at the meeting was a question regarding how our schedule for the remaining work had been impacted now that the funding risk was removed. We appreciated your frank recognition that as we had pointed out in our previous correspondence, our ability to purchase materials and mobilize for the 2007 construction season was critically affected.

Since the Partnering meeting, we have worked with our suppliers and our barging resources. We have evaluated the remaining work in terms of labor, equipment and project management requirements. Various scenarios involving added labor, overtime labor, added barging and additional equipment have been assessed, along with virtually every acceleration option we could come up with.

Regrettably, on a cost-benefit basis, our conclusion is that the chance of completing the project this year is so slim that an attempt to do so would be economically prohibitive. It is far more likely than not, even if we discounted the uncertainty of weather and the likelihood

that we will be unable to secure delivery of the dock and bridge materials until sometime in July, that we would end up incurring the cost associated with an accelerated 2007 work effort; and with all of that money having been spent, we still would incur the demobilization – standby – remobilization costs of an extra season.

We can detail all this for you, and present a schedule that reflects a 2007 completion. Making that effort and incurring the costs necessary to meet such a schedule is not a risk that KRI would undertake, and we cannot and do not recommend the Corps take that risk either. Absent contrary direction from you, our plan is to develop a schedule that defers the dock and bridge work into 2008. We will have that schedule in your hands this week, to be followed by a forecast REA reflecting the additional demobilization, standby and remobilization costs.

(SR4, tab 11 at 165-66) The Corps has not directed us to any evidence that the Corps provided “contrary direction” to KRI insisting that the project be completed in 2007. Because the additional funding of the contract occurred literally just days prior to KRI’s planned start of the 2007 work season in April, KRI could not begin to prepare for the 2007 construction season until immediately after the 20 March 2007 meeting.

So we were left to scramble on just securing the crews, tugs and barges, armor rock, supply, most notably the Flexi[-F]loat [see finding 71], that was probably the biggest headache because we identified that we needed it in [2006], but it was an expensive tool to assemble and put together and absent the funding it would not be something that we’d get reimbursed for most likely from the Government if we were terminated.

(Tr. 4/105; *see also* SR4, tab 19 at 1190-91; tr. 7/19-20) It was KRI’s assessment that the contract work it had planned to complete in the 2007 construction season could not be accomplished because it would take months to make up for the lack of winter preparatory work. As of late March 2007, KRI’s planned alternate armor rock source, Western Marine, had demobilized to Seattle and never came back to Alaska³⁰ (finding 57; tr. 2/137-39, 4/84-86, 16/9-11), its dredging subcontractor, Nehalem River Dredge, was no longer available for the 2007 season (tr. 4/51-52, 94, 7/173-74, 189, 221, 16/11) and

³⁰ Western Marine later in March agreed to sell to KRI approximately 12,000 tons of armor stone that it left behind at its Sand Point Quarry (SR4, tab 24 at 160-61).

the price of steel had increased significantly, which “basically ate up all of the savings” of the VECP bridge and dock design (SR4, tab 19 at 772-77; tr. 2/134, 4/101-04, 9/53-54). KRI proposed to develop and provide to the Corps an updated schedule that deferred the dock and bridge work into 2008³¹, “followed by a forecast REA reflecting the additional demobilization, standby and remobilization costs” (SR4, tab 11 at 165-66, 374; tr. 2/81-90).

68. By letter dated 10 April 2007 ACO Jong replied that:

Your plan to develop a schedule that defers completion of the bridge and dock until 2008 is unacceptable, until you receive a formal contract modification for an increase in time; and such a modification cannot be initiated until the Government receives an official Request for Equitable Adjustment (REA) with appropriate justification that supports such action. We look forward to reviewing your REA as well your plan for completing the remainder of the work through a schedule that reflects the most current conditions. Until then, you are to proceed with your construction efforts based upon the original contract completion date of 5 Jan 2008.

(SR4, tab 10 at 69) KRI’s Swantz, who prepared KRI’s schedules, testified:

I had to keep showing the January 5, 2008, completion date and...they wouldn’t accept anything else, so ultimately the tasks just kept building up towards the end of the job.

I needed to show them, yet I couldn’t show them in 2008 when they would legitimately happen....

....

...[T]he as-built reflected what was actually constructed.

....

³¹ The VECP bridge and dock were originally scheduled to be on the spring 2007 mobilization barge, but because of the delays caused by funding restrictions, it had to be sent to Alaska on a separate trip in 2008 (tr. 2/134-35, 3/127-28).

In general it was the best we could do was maybe a month out and then the tasks started to bunch up, so it would at least give people [an] indication of the near future, but the question mark hanging over the project kind of made the balance of the schedule not, I don't want to say not relevant, but not representative of what actually was occurring because at that point in time we already knew we were going to 2008.

....

The field crews would develop their own schedule in conjunction with me and those typically were two weeks out and they just, being there at the site they were able to better identify the situation.

(Tr. 4/106-09; *see also* finding 37; tr. 4/194-98, 5/35-44) KRI responded to ACO Jong on 18 April 2007 that:

[Y]our letter...sounds very much like an acceleration order. We believe such an order to be inconsistent with the understanding reached at the Partnering Meeting as to what the Corps wanted. You can appreciate our reluctance to incur acceleration costs in the absence of specific recognition by the Corps that it intends to insist upon adherence to the original date of January 5, 2008.

Finally, we are uncertain regarding what is meant by "an official Request for Equitable Adjustment (REA)". At the Partnering Meeting, we presented details of the impacts that resulted from funding issues on this project. The [CO] acknowledged that our correspondence over past months have spelled out what these impacts were. They included such critical matters as our being disabled from issuing purchase orders for needed materials, and our not being able to tie up the necessary transportation commitments, and so forth.

At this point, our Request for Equitable Adjustment of the contract time is tied to the schedule we are developing. This schedule shows the effects of the funding restriction. It does reflect "the most current conditions".

Our Request for Equitable Adjustment of the contract amount, however, only can reflect the presently known materials and transportation cost escalations, along with a forecast of an additional demobilization, standby, and remobilization expense. It would be impractical to forecast all of the time and cost impacts because the extent to which the course of events may further affect our already-impacted construction effort remains an unknown.

Our suggestion regarding the best way to deal with the situation is as follows:

1. We will continue to develop, and will submit, the schedule that reflects the known impacts, that is to say, “the most current conditions”, accompanied by a Request for Equitable Adjustment of the contract time to incorporate the new completion date shown by that schedule.
2. We will submit a Request for Equitable Adjustment of the contract amount that covers the material and transportation cost escalations incurred to date; and we will submit a proposal reflecting our forecast of the costs attributable to the additional construction season.
3. We do not want to jeopardize timely response to our Pay Request. If the Corps believes that, until there has been a formal action taken on our request for equitable adjustment of the contract time, it must have a schedule reflecting a 5 January 2008 completion date, we will provide one. That submittal will have to be qualified with a statement that such schedule does not “reflect the most current conditions” on the project, and does not depict the activity durations that in fact do reflect those most current conditions.
4. We will not undertake the costs and added effort that would be needed to accelerate our construction effort so as to try and achieve a

5 January 2008 completion date unless specifically directed to do so by the Corps.

We ask that you immediately advise us, upon your receipt and review of this letter, if in the event that our course of action has not been made clear; or whether the Corps prefers to direct some course of action other than what we have outlined in this letter.

(SR4, tab 11 at 248-49; tr. 2/90-94)

69. The Corps' expert witness, Mr. Ockman, testified that a contractor's schedules are supposed to include information identifying problem areas and/or delaying factors actually experienced on the critical path of the project, as well as any resultant impact on the contract completion date (tr. 11/123-24). Mr. Ockman further testified that:

[C]ontractors need to base their time extension requests on the schedule.

And more important they need to show...that the time extension is justified because the events leading to the request for additional time affect the critical path and absent those events, they would be able to finish earlier.

(Tr. 11/125) However, as a result of the Corps' repeated direction that, in order for KRI to be paid, it must submit schedules showing it would finish on time by the original contract completion date, KRI's submitted schedules artificially compressed remaining contract work, making them inaccurate representations of actual circumstances (*see, e.g.,* SR4, tab 10 at 69, tab 11 at 250-64; tr. 2/94-96, 4/75-76 ("not an effective tool for scheduling"), tr. 12/27-35). We find no evidence that the Corps objected to KRI's schedules that had to be known by the Corps' onsite QAR personnel to be inaccurate representations of what was actually planned and performed. Every schedule submitted by KRI between May 2006 and 13 November 2007³² contained specific language stating that it did not include funding clause impact information (tr. 12/32-33). Mr. Ockman specifically gave, as an example of an improper schedule, KRI's October 2006 schedule in which KRI noted that work originally planned to be performed in 2006 was deferred to 2007, yet the schedule showed no change to the planned completion date (tr. 11/124). For that reason, the schedules submitted by KRI for the 2006 and 2007 work provide no accurate information to us regarding how the work in that period was actually planned to be performed or how it was actually

³² The date on which Modification No. P00011 unilaterally extended the contract performance period to 5 January 2009 (finding 83).

performed. To the extent those schedules were relied upon by witnesses for either party as accurate representations of planned and/or actual work, we find their reports and testimony in that regard to have little credibility.

70. In a 3 May 2007 “Memo for Record,” CO Williams stated:

During the most recent partnering session held on March 19,^[33] 2007, funding issues were discussed.... During the course of the partnering session, [KRI] stated that they plan to submit a request for equitable adjustment detailing their reasons for the additional costs and time extension to September 1, 2008. It should be noted that there are several statements in the PIL that state, “Realize that limiting the Government’s liability increases the contractor’s risk and, therefore, is likely to increase the cost of the contract.” *In my opinion the funding issues spelled out in this memo did impact the contract.* Whether or not these impacts can be quantified will have to be addressed in an [REA] from the contractor. Some government personnel feel that any REA is unjustified since the contractor is currently behind schedule and will not finish the project on time even with full funding. Most likely in their REA the contractor will state that they slowed their schedule based on the funding issues. These issue[s] will need to be reviewed by the government in the context of the REA. [Emphasis added]

In addition a VE for Open Cell dock and bridge abutments has been submitted by the contractor. Only recently has the government received a complete VE package for review, so this may also factor in the delays. I expect that the contractor will also use VE delays to justify their REA.

(SR4, tab 14 at 2125, tab 28; tr. 13/101, 105-09) KRI’s Ryan Pleas’ notes from the meeting state his understanding that “[CO] Williams agrees that the funding issue has affected KRI schedule” (SR4, tab 190 at 6; tr. 2/79-80).

71. The Flexi-Float utilized by KRI in contract performance was a:

³³ This is an obvious typographical error as the date of the Partnering Meeting is 20 March 2007 in the balance of the record.

[M]odular barge constructed of cells and connected to produce different sizes and shapes of [floating] work platforms.... [T]he excavator (Hitachi EX 800) was fixed to the flexi-float work platform. Fabrication and assembly of the flexi-float did represent a significant expense, not to mention requiring an engineering design, acquiring the components, fabrication and shipping it to False Pass required approximately twelve weeks of time. Of course, there was no money to commit in 2006, and there would be no need for this equipment if the contract were to be terminated.

....

The flexi-float proved a very effective tool for the work, so much so that Dutra leased it from KRI in 2009 and used it to construct a similar project at Dutch Harbor (the Carl E. Moses Project).

(SR4, tab 19 at 1201-02; *see also id.* at 1311; tr. 8/158)

[T]he Flexi[-F]loat...also was equipped with spuds and winches, so it could move itself around, it could nose up to the breakwater and shape and then once a particular area was done it could move over and continue, so it was kind of its own a[u]tonymous little unit.

(Tr. 4/105-06, 5/29-30) Use of the Flexi-Float was not planned, nor included, in KRI's original bid and the cost of the Flexi-Float is not included in KRI's claim now before us (tr. 5/29-35, 8/158, 161-62; SR4, tab 5 at 279). KRI first considered the use of the Flexi-Float tool in August 2006 when it was placing core rock for the east breakwater. KRI discovered that its original plan to shape core rock using the Hitachi excavator working on top of each the breakwaters would not work for the east breakwater because the location of that breakwater further from shore and into the harbor presented safety issues. (SR4, tab 19 at 1200-01; tr. 15/23) KRI used the Flexi-Float pontoons as the water-based structure on which it mounted its excavator that performed the shaping and placement of B rock and armor stone the following season. The Flexi-Float was fabricated and mobilized to the jobsite after the contract was fully funded in March 2007. (Tr. 5/57-59, 7/19-20, 8/159-61)

72. In a phone call on 16 May 2007, CO Williams directed KRI to submit "the narrative portion of its REA by 25 May 2007 and the cost portion of its REA no later than 9 June 2007 (SR4, tab 10 at 82). By letter dated 25 May 2007 KRI submitted its request

for a “forecast[ed]” 289-day extension of the contract performance period, which would change the completion date for in-water work to 30 September 2008. KRI stated that it was preparing a REA addressing the impacts of the funding issues on its costs of contract performance. KRI further stated that “[d]etails of the entire situation are a matter of record” and attached to their letter “a chronology that catalogs developments over the past year.” (SR4, tab 11 at 373-81; *see also id.* at 388; tr. 2/97-102, 7/213-14)

73. By letter dated 2 July 2007 CO Davidson rejected KRI’s request for an extension of the contract performance period and further stated that the Corps was no longer interested in KRI’s VECP proposal for the dock and bridge because KRI had not provided certain calculations and safety information (SR4, tab 10 at 117-20, tab 124; tr. 13/17-18). This was the first direct contact by CO Davidson with KRI in the False Pass contract since she signed the contract at award (finding 8). It was at this point in the project that CO Davidson became the lead CO and CO Williams was in more of a supporting role as he was very busy with other contracts assigned to him (tr. 12/191-92, 13/128-32).

74. By letter dated 17 July 2007 CO Davidson again denied KRI’s request for an extension of the contract performance period and required that KRI submit a detailed recovery schedule no later than 30 July 2007 and to include a “detailed account of activities you plan to take to get back on schedule” for contract completion by the original contract completion date of 5 January 2008 established before the funding restrictions were unilaterally imposed (SR4, tab 10 at 132-34; tr. 2/109-10, 8/80-91).

75. KRI responded to CO Davidson’s 17 July 2007 letter:

Your C-0054 “Letter of Concern” transmitted on 19 July comes as a surprise and disappointment. We have dealt almost exclusively with Mr. Williams as Contracting Officer on this project. Your phone call to me on July 2, 2007 implied that you were assuming a hands-on role, but my sense from that conversation was that you fully understood the situation on the project, and were briefed on the seriousness of the impact caused by the government's unilateral attempt to modify the funding provisions of the contract.

....

...KRI repeatedly has advised the Corps, over the last several months, that this project cannot be completed by the 5 January 2008 Contract Completion Date. The delay stems directly from government funding restrictions.

We have spelled this out in correspondence and in meetings with your representatives. The situation is detailed in the Request for Equitable Adjustment of the contract time which we were requested to submit. The companion adjustment of the contract price, one aspect of which is the escalation in steel prices described in our VECP Serial Letter #50, is still being evaluated.

Your letter says that "at this time the government is requiring a detailed recovery schedule...which...shall also include a detailed account of actions you plan to take to get back on schedule...". I respectfully suggest to you that this directive is an unmitigated acceleration order. Please review our previous correspondence. We have made the point several times that the schedule submitted showing the original Contract Completion Date are for pay purposes only. These schedules do not reflect actual job progress, nor do they show impact to the schedule resulting from government-caused delay. You will see from the record that KRI has analyzed the cost and likely results of an accelerated work effort this construction season. Our analysis is that chances of recovery to the extent needed for a 5 January 2008 completion were so slim and exposed to uncertainties that it didn't make practical sense to try. The likely result would have been adding costs for the extra season to the compensable costs involved in the unsuccessful acceleration effort. Consequently, our course of action and progress on the project, as your staff has been advised, has been geared to avoiding the acceleration costs.

The project is in dire need of a partnering session. We will make ourselves available at the earliest date (excluding 2 & 3 August) you can schedule. I think a facilitator would be helpful, and request that you and I spend some time one-on-one before the general partnering session begins.

(SR4, tab 11 at 508-09; tr. 2/110-13, 8/6-10, 177-79; *see also* SR4, tab 5 at 36-38; tr. 2/130-31)

76. While KRI was disappointed with the tone of her letter, KRI's experience working with CO Davidson on the previous St. Paul Island contract was that she was a good communicator and KRI was pleased to have her involved in the False Pass contract.

And once [CO Davidson] came onboard,...[s]he got the parties together and we ended up getting [the bridge and dock issues] solved in a matter of no time. I mean for as long as this thing festered, it was amazing how quickly it could be solved.

....

...Kelly [Pleas]...called her right after [her] letter came and he just started up a dialogue and the two of them got it figured out and got it back on track and literally, it took a very small tweak to the design and it was approved. I mean it was a lot of just, that whole issue was really not a big deal. It was something that could have been solved if somebody had just done what she did and gotten together the parties, it could have been solved a long time ago.

(Tr. 2/103-07; *see also* tr. 7/182, 14/217-18, 223-25; *see also* SR4, tab 193)

77. A Partnering Workshop was set for 21 August 2007 with KRI's stated agenda:

2. Schedule Impacts to the Project. KRI would like an opportunity to review schedule impacts that have affected our progress and efficiency to date. Primary among these, as you might expect, is the funding restrictions by Mod. P-0005. I see this discussion beginning with a review presentation by KRI detailing the ways we believe our work has been affected. We would look forward to Corps reaction to that presentation.

3. Impacted Schedule. We will have in your hands, in advance of the meeting, a work shop schedule that reflects actual progress to date. It will be the basis for discussions and layout the anticipated sequencing and durations of the remaining project work. Again, we anticipate reaction and discussion from the Corps. I believe you would agree with me that it does not make sense for us to continue submitting schedules showing completion by the original January 5, 2008 date, just so that our pay estimates can be processed.

4. Cash Flow Issues: As is obvious to everyone, KRI has performed a significantly smaller part of the overall work to date than we had planned. This is the result of the schedule impacts recapitulated in Item 2. Our costs are going to be higher than planned because of the additional barging we will need, the winter-over cost, the expense of an additional demobilization and remobilization because of the extra season, and so forth. We would like to discuss the costs with you and your staff at the Partnering Workshop, and discuss ways and means of partnering a solution.

5. KRI's Pending REA. We submitted a Request for Equitable Adjustment of the Contract Time on 25 May 2007. It is our understanding that Mr. Williams and his staff had acknowledged that KRI had been impacted by the funding restriction. We also were confident that the time impact and the cost impact would be reviewed as separate issues. Our request was that the time issue be dealt with expeditiously so as to avoid the necessity for submitting artificial schedules reflecting the original contract completion date, and also to eliminate any need your staff might have to dispatch cure notices and requests for recovery schedules. I believe both sides understand where we stand on these issues, and KRI suggests that we work out something that recognizes where the project presently stands, where it is headed, what caused the impacts to the original schedule, and how we can work together toward an efficient, cost mitigating effort that takes these project realities into account.

We would appreciate receiving advance notification of any additional agenda items the Corps would like to put on the table, if you are able to do that. KRI is looking forward to this Partnering Workshop session as an opportunity. We do not see that there are any problems on the project that cannot be solved, and we do not feel there are any pending issues that the parties will be unable to resolve if the spirit is willing. You have my commitment for a full-fledged, cooperative effort.

(SR4, tab 11 at 568-69; tr. 2/114-15)

78. The minutes of the 21 August 2007 Partnering Workshop include:

1. **Value Engineering Change Proposal (VECP).**

....

KRI plans to take the VECP savings along with the dredging and rock underruns and applied [sic] them to the increased costs for OH and Mob/Demob to extend the project to September 8, 2008. With these costs accounted for, the net contract increase would be approximately \$743,857.00. As part of this change the rock quantities would be changed from Unit Prices to Lump Sum items. This allows the government to factor in the underruns and provide an avenue to apply the unit price savings back to the contract. If this is not done, accounting for the underruns will have to wait until the end of the contract. As for the underrun quantities, KRI is satisfied with the quantities for Dredging and B rock, but need to verify the quantities for the armor rock. James Swantz from KRI is in the process of verifying the numbers and plans to have the final pricing information submitted to the government...by August 27, 2007. **Action Item: KRI**

KRI and the government discussed whether to submit the changes as a VECP or Design change. Bill Walters made the point that rather than submitting the VECP and the other changes separately, it would be more efficient to consider the VECP a design change and roll all the changes into one bilateral mod. KRI will continue to work the changes and the VECP and the government will look into the best way to submit the changes. **Action Item: Government.**

2. **Funding/Cash Flow Issues.**

During the discussion on the funding issues, KRI referenced their Serial Letter 027 dated

December 26, 2006³⁴ which discussed their funding shortfalls. While this letter provided information on the contractor's status of funds, from the government's viewpoint, it did not provide a complete picture of financial impact to the contractor due to the continuing contract clause changes. KRI needs to logically lay out in detail how they were impacted by the contract clause changes. During discussion, KRI stated that they signed a subcontract in the amount of \$6.1 million for rock at the time of contract award which they applied against the \$10.5 million in funding provided by the government. The government stated that this is the type of information we need in the REA. KRI will submit their cash flow analysis on the funding changes as part of their request for equitable adjustment. KRI will provide the written REA on schedule and cost impacts by August 27, 2007 so the government can analyze them before the meeting on September 5, 2007.

Action Item: KRI

KRI presented draft numbers on the impact of the changes in funding. The draft proposal presented by KRI proposed a time extension for the contract to September 8, 2008 at an estimated additional cost of \$743,857.00. The contract would be increased to an estimated \$20,466,857.00. This is based on an underrun of approximately \$1.3 million. If these changes are not enacted, the contractor would request an increase of the contract to \$22,061,001.00. **Action Item: KRI**

3. **Schedule.** The Corp[s] will do a mod to increase the in water work window to November 15, 2007. KRI presented their schedule based on a completion date of September 30, 2008. **Action Item: Government**

(SR4, tab 13 at 9-10; tr. 2/115-18, 4/30-33 (VECP savings of more than \$1 million used to cover transportation and design of the dock and bridge), tr. 4/96-98, 112-13, 14/217-20; *see also* SR4, tab 10 at 156-57)

³⁴ The actual date of the letter is 29 December 2006 (SR4, tab 11 at 135-36; *see also* finding 62).

79. On 29 August 2007 KRI provided to CO Davidson its 11-page "Funding Impacts and Cash Flow" which included a narrative, spreadsheet and backup attachments for costs incurred as of 31 December 2006, which KRI summarized as showing that its costs of performance at that time were "about 22%" above the amount of available funding without taking into consideration "any additional T[/]C costs or the additional equipment standby costs pending the demob[ilization]" (SR4, tab 11 at 573-80; tr. 4/112-17). The Corps did not respond to KRI's 29 August 2007 submission (tr. 4/117).

80. The minutes of the 5 September 2007 partnering meeting state:

1. **Alternate Bridge and Dock.** [KRI's] Swantz handed out drawings on the alternate Bridge and Dock for review [tr. 4/117-18]. PND is still working on the calculations and should have them complete by September 13, 2007. KRI will review them and submit them to the Corps by September 19, 2007. The government should complete the review within two weeks. KRI has stated that they have reserved manufacturing space for the remaining sheet piles and can keep that reservation for a month at which time they well [sic] have to cancel or make a financial commitment with the supplier. Keeping to the schedule above, they expect a late February to early March delivery of the bridge girders to Seattle.
2. **Schedule.** The contractor handed out a revised schedule. [ACO] Jong asked what work they planned to do for the remainder of this construction season. KRI plans to complete the B rock on the east breakwater; complete the north breakwater; and complete the E breakwater to mean high water from Station 100 to 220. KRI plans to make one more trip to Sand Point to pick up rock. They are currently planning to demobilize for the season on September 30, 2007. To allow for potential delays the in water date will be extended to November 5, 2007. The revised completion date was discussed. The contractor originally proposed September 30, 2008 as the new completion date. The government expressed concern with this date since it would not allow sufficient time to complete the final documents on the

contract. Based on discussions, it was decided to extend the [contract] completion date to [January 5, 2009 and November 15, 200[8³⁵]] for completion of the in-water work]. KRI will be submitting a revised schedule reflecting the new completion date.^[36]

....

5. **Work Next Season.** [PM] Wierzbicki asked KRI if they would be adding additional crews next year since so far they have completed 37% of the work. [KRI's] Swantz stated that KRI will have a separate crew to build the bridge and dock. They also may add an additional barge. KRI plans [to] run multiple operations using two track hoes with GPS systems and one without....

....

6. **Draft Funding Requirements.** Referencing the draft funding requirements provide[d] by KRI dated August 27, 2007, no documentation was provided to back up any of the claimed increases in pricing for the new design. [CO Davidson] discussed the fact that since this is a sole source negotiation[,] all prices have to be backed up. In addition [she] asked that [KRI] submit a Certificate of Current Cost or Pricing Data. Using page 2 of the document, [KRI's] Swantz explained how he arrived at the numbers for the material differences. KRI will provide backup documentation supporting their numbers by September 19, 2007. In their revised submission, KRI will provide overhead and profit percentages.

No documentation was provided to support commitments to the rock suppliers. If KRI had a signed contract for all the rock from [Northern

³⁵ The language in the draft modification and the context of the discussions indicates to us that the "2007" was intended to be "2008" (SR4, tab 127 at 3).

³⁶ After the agreement to an extension of the contract completion date, KRI was able to submit an October 2007 construction schedule that "showed true representative work into 2008" (tr. 4/110-11).

Mechanical], why are [they] receiving Armor rock from [Northern Mechanical] and Sand Point. KRI explained that they were not getting the planned yield from [Northern Mechanical] quarry. KRI stated that based on funding limitations, it was better to work with the quarry. KRI referenced Serial Letter 055 that showed they were running out of money.

7. The wording in the draft mod was reviewed with KRI....
8. Since we are waiting on the final package [for the bridge and dock] to be submitted by 19 Sep 07, the rock sizing and in water work windows will be done with an earlier mod. KRI will submit changes as a complete package.

(SR4, tab 13 at 11-13, tab 14 at 2375-77; tr. 2/121-26; *see also* SR4, tab 19 at 1195-99) It was KRI's understanding that the bridge and dock design, as well as the time impact of the unilateral funding clause changes, had been addressed in the meeting and that only the dollars associated with both remained to be resolved. Once a DCAA audit was completed, KRI expected that a bilateral modification of the contract would be negotiated to settle the dollars. (Tr. 2/127-28)

81. By letter dated 18 September 2007, the Corps notified KRI that \$110,800 had been withheld from KRI's Pay Estimate #9 because, even though the parties had negotiated an extension to the contract completion date (finding 80), the Corps had not yet actually modified the contract and was still requiring KRI to show the original completion date and basing payment on the inaccurate schedule. "[Y]ou are behind schedule, and the attached project schedule is only proposed and not, at this time, contractually binding." The Corps' letter continued:

We understand that a pending contract modification is being worked by both parties to extend the contract completion date, but unfortunately all issues have not been resolved, nor has the pending contract action taken place. Once the pending contraction [sic] action has been executed and the Government has approved your proposed schedule, then these monies will be returned with the next pay estimate submission.

(SR4, tab 10 at 155)

82. By the end of the 2007 construction season, 63% of the contract work remained to be completed (finding 80; tr. 3/196-99).

83. Bilateral Modification No. P00010 dated 13 November 2007 extended the end of the period for in-water work from 1 October to 15 November (SR4, tab 14 at 1889; *see also* finding 80). Unilateral Modification No. P00011, also dated 13 November 2007, incorporated into the contract KRI's approved design for the VECF bridge and dock, now referred to as "Alternate Bridge & Dock."³⁷ The modification was "issued as a Notice to Proceed" and directed KRI to commence the work. The contract price was unchanged, pending definitization in a later modification (*see* finding 98), and it was anticipated that 75% of the bridge and dock work would be completed prior to definitization. (SR4, tab 14 at 1630-35; tr. 13/19-21) In addition, the contract completion date was formally extended to 5 January 2009. (SR4, tab 155 at 25-27; tr. 4/29). At the hearing CO Williams testified that the Corps extended the contract performance period because:

[W]e realized that by the time we accepted
the...design...there was nowhere [near] enough time to
install it within the original contract period.

(Tr. 13/19-20) However, in later testimony, CO Williams agreed with ACO Jong's statements made contemporaneously with the negotiation of the new contract completion date, that there was no additional time added for the bridge and dock (SR4, tab 10 at 65-66, tab 14 at 2203; tr. 14/110-11). KRI had not asked for additional time for the bridge and dock work (tr. 8/95, 105, 179-80) and it was KRI's understanding that the extension of the contract performance period was acknowledgement by the Corps of the time portion of the impacts on KRI's performance caused by the funding restrictions unilaterally imposed (tr. 2/129-30, 8/94-97, 106-07, 182-83). It was also KRI's understanding that, after completion of a DCAA audit of the pricing for the bridge and dock³⁸, another contract modification would be issued for an increase in the contract price resulting from the bridge and dock, as well as the monetary impacts of the unilateral funding restrictions (tr. 2/132-34).

³⁷ CO Williams testified that the bridge and dock design was not referred to as a VECF because approval and incorporation of the design was not going to result in a savings to either KRI or the Corps because the price of steel had gone up so much (tr. 13/20).

³⁸ Unilateral Modification No. P00012, dated 4 December 2007, expressly postponed the pricing of the alternate bridge and dock work until after a DCAA audit had been conducted (SR4, tab 14 at 1604-05).

84. CO Davidson requested a DCAA audit of KRI's 18 September 2007 proposal for the increased cost of the bridge and dock design in the amount of \$954,814. The DCAA audit report was issued 7 March 2008. (SR4, tab 19 at 541-77, 719)

85. The parties met on 10 April 2008 to negotiate the additional cost of the alternate bridge and dock as well as KRI's alleged impacts due to the unilateral change in funding clauses. CO Davidson conducted the meeting, the minutes of which show that:

9. The government and contractor discussed that this claim needed to be settled globally, looking at the contract as a whole. This means the burden is on the Contractor to provide the Government with supporting documentation showing where they are losing money on this contract. After that is provided, the parties must look at these items and assess whether this was contractor caused or Government caused. We discussed using the modified total cost method to negotiate settlement of this claim. By using the total cost method, the Contractor must show the actual costs and substantiated future cost. After we have this amount, then it will be compared to the actual price on the contract. If there is a loss, then we will discuss who caused the loss.
10. The Contractor said it was going to take some time to get all the documentation required for the global process. The Government asked how much time. The Contract[or] stated they would call the [CO] on Monday and set a date when all the documentation would be ready and when the parties could meet again.

(SR4, tab 13 at 14-16; tr. 2/134-42) CO Williams had no direct involvement with the funding of the project. Corps project manager (PM) Wierzbicki and the ACO were responsible for the funding of the project (*see also* finding 29). PM Wierzbicki died in April 2008 (*see* SR4, tab 32; tr. 2/155).

86. KRI mobilized to the jobsite and resumed work on 11 April 2008 (app. br. at 19).

Knowing the funding well in advance we got up there in the first week of April, so we were humming along. We were shaping rock, the dock and the bridge were going in

well, we were really pleased that the shaping, it's how the project should've gone when we knew the funding was there.

We were firing on all cylinders. The only constraint really was the supply of the armor stone, not so much the shaping of the armor stone, but the supply, our alternate source having not been available, we need to travel much further, and so the time between barges became the constraining factor.

(Tr. 4/121-24)

87. After losing its alternative/supplemental source for rock due to the funding restrictions (finding 67; tr. 4/84-86), KRI discovered that there were no other sources in Alaska that were producing the required armor rock. As a result, it had to go to suppliers in British Columbia, Canada, and the northwest United States, some of which were 2,000 miles away from the job. Transporting armor stone from those locations took up to 18 days to reach the jobsite and by this point in time the price of fuel was more than double what KRI had included in its bid. (SR4, tab 19 at 1195-99, 1315-16; tr. 2/137-39, 8/18-23).

88. By letter dated 23 April 2008 KRI submitted detailed cost data for the alternate bridge and dock design per CO Davidson's request two weeks earlier:

As agreed to in our meeting with you in Anchorage on April 10, 2008 we are submitting the attached documentation of accumulated cost-to-date of \$3,488,298.35 for mobilization and demobilization [for the VECP bridge and dock] from the beginning of the project through April 17, 2008. This information is what you requested in order to allocate additional money to the mobilization CLIN 0001.

The following documentation is taken from KRI's cost accounting system and organized by the cost code breakdown activities used to track and report costs to the accounting system. The reporting of daily labor to the appropriate activity codes is entered into the system weekly. Invoicing is entered into the AP system after coding by the field personnel.

In this submittal, the payroll analysis report shows only the labor involved in mobilization and demobilization through

April 17, 2008. It further breaks it down to cost code activity. Each employee charged to the activity is listed showing total hours worked and total cost including payroll tax burden. The AP report shows all invoices charged to the various cost code activities. As requested, copies of those invoices greater than \$3,000 are included in this submittal.

At this time, KRI is preparing documentation for the total accumulated cost-to-date for all activities for this project through April 17, 2008 plus forward pricing to finish the project. It is anticipated that the format and depth of documentation will be similar to this submittal. After your review please indicate if this meets your requirements. We are planning on having the information on the total cost for the completed project to your office as agreed by May 14, 2008 and then meeting with you on May 20, 2008.

(SR4, tab 11 at 1912; tr. 2/140-42)

89. On 14 May 2008 KRI submitted an uncertified³⁹ modified total cost REA in which it sought a total of \$16,049,937:

Please consider this letter as part of KRI follow-up to our April 10, 2008 meeting. We transmitted part of our documentation, consisting of our job cost accounting records for this project, under Serial letter 069 dated 13 May 2008. With this letter we are sending detailed job cost reports reflecting materials, labor and equipment expended on the project from inception through April 2008 [see finding 91]. As you requested, we have included copies of individual invoices in amounts exceeding \$3,000.

The remaining documentation will be forwarded not later than Wednesday, May 15, 2008. We believe this satisfies the mutually agreed commitment date. KRI is anticipating a meeting for resolution of the entire matter at our scheduled gathering in your office on May 20, 2008.

³⁹ KRI intended the 14 May 2008 submission, in the format requested by CO Davidson, to be an informal "starting point for negotiation" (tr. 3/34-46, 196-99).

The attachments to this letter set forth the KRI Request for Equitable Adjustment of the contract time and amount. The basis for this Request has been documented in extensive correspondence over the past year-and-a-half. At our April 10th meeting, we felt both sides recognized that fault was not at issue. The circumstances were not caused by either KRI or the Corps. They were the result of Federal Legislation.^[40] Specifically, the Corps necessarily responded to a mandated Congressional enactment when it issued Modification P-00005 on 17 July 2006 and deleted “EFARS 52.232-5001 Continuing Contracts (MAR 1995)” and inserted “52.232-5004 Incremental Funding Clause (IFC)”.

The resulting funding restriction seriously impacted our entire contract. KRI was precluded from mobilizing and carrying the job plan that was the basis for our bid. Every feature of our work was impacted. We were unable to buy-out the project. We were unable to make commitments to, and as a result were prevented from assembling, the field management and crews that we had confidently relied upon as the basis for our pricing of the work. Ultimately, we were prevented from effectively carrying out our plan for performing the work at the site, and had literally to dabble at the work and shorten the work season. These problems are carried over in to the 2007 construction season. In a period of spiraling prices, we were unable to commit to our suppliers because doing so would have exceeded the mandated funding limit. This meant that KRI could not purchase the dock and bridge materials, and these were items which experienced a month-to-month price escalation. This impacted rock placement on the south breakwater because these were concurrent construction operations. The effect upon our overall work increased because we were unable to commit to the experienced field personnel we had counted on to perform this work.

The impacts to our project work were both direct and indirect. A crucial example is the KRI rock supplier in

⁴⁰ Kelly Pleas testified that, based on information he learned after he wrote this letter, he no longer “agree[d] that Congress caused this problem” (tr. 8/53).

Dutch Harbor. Work in the quarry there had to be suspended. The reason? KRI could not haul rock away from Dutch Harbor as had been planned and scheduled. Both the quarry and the staging point for hauling to the project site had stockpile limitations. The result is that KRI now will have to purchase part of the project rock requirements from a different, more distant and more expensive source.

All of these subjects were discussed at our April 10th meeting. The focus of the meeting, from our viewpoint, turned to exploring how we should deal with the problem. Even though this was not a problem caused by anyone at that meeting, it nonetheless has resulted in a situation both sides have to deal with fairly and realistically. Discussion of the situation led to both sides searching for a way to pursue an appropriate adjustment of the contract time and price.

You were of the view that a Modified Total Cost method of pricing the Request for Equitable Adjustment was appropriate in the circumstances. That approach seemed reasonable and was acceptable to KRI. You asked that we document and submit our accrued project cost, and that we furnish a detailed forecast of the 2008 project completion pricing. This is the information we have developed, and which we are submitting in preparation for the May 20th meeting and negotiations.

This approach, as was discussed during the meeting, required that we establish our project cost. The purpose of these submittals is to demonstrate those costs to you and your staff. We recognize that our plan for resolution of this matter depends, partly at least, upon our forecast of the 2008 costs-to-be-incurred. You have to be concerned that these forecasts are viable. We have to be reasonably certain that KRI is not taking an unrealistic and unacceptable level of risk. This is an issue that we look forward to resolving with you at the May 20th meeting.

The question of contractor inefficiencies has been raised. We recognize that the Modified Total Cost method of pricing an equitable adjustment anticipates that the costs being claimed by the contractor have been reasonably

incurred, and that the contractor is not itself responsible for those cost over-runs which are at issue by reason of inefficiencies, or because elements of his bid may have been unrealistic.

We believe those issues can be worked through successfully between us. KRI's analysis shows, and we think we can satisfy you and your staff, that the entire plan and execution of the work on this project has been impacted by the Congressionally-imposed funding limitation. We recognize, and we expect, that you and your staff will be looking for contractor inefficiencies which were self-inflicted. KRI is prepared to meet and work through any issue in this regard that might be raised.

You will see from the project accounting we are presenting that the effect upon our work was devastating. The cost over-runs are beyond anything in our 25-year experience as a company doing business with the Corps in Alaska. The schedule below lays out our cost-accounting experience on the project as a result of the funding limitation that was imposed.

Total Costs Incurred from Job Inception through April 2008	15,074,601
Estimated Cost To Complete	14,798,083
Total Costs Incurred to Date Plus Estimated Cost to Complete	29,872,684
Original Bid (less profit and overhead)	16,237,822
Direct Costs	13,634,862
G & A @ 9.5%	1,295,312
Profit @ 7.5%	1,119,763
Request for Equitable Adjustment	16,049,937

The foregoing recapitulation presents an extraordinary, in fact from our view it is an astonishing, picture of what has occurred, and we expect reaction from your end will be identical to ours.

All we can say is that Congressional Legislation, regardless of how well-intentioned and cost-saving motivated it might have been, often ignores the operational realities of your agency and of our Company.

Please let us know if you require any additional information in advance of our May 20th meeting. We fully

recognize, at KRI, that this is a difficult and challenging scenario for you to deal with on the eve of your retirement, but you have our assurance that we will work diligently to develop a disposition that protects the interests of the Corps while allowing KRI to successfully complete the outstanding project issues and continue its history of productive work for the Corps and other public owners in Alaska.

(SR4, tab 11 at 2086-96; tr. 2/142-48, 3/27-37) Ryan Pleas testified:

[At the time the 14 May 2008 REA submission was made], we were being told that, I'm trying to settle this thing. This is, the job is going on. I'm trying to get some cash flow. And we're trying to put the best spin on it we can because we don't want to be confrontational. We're trying to get together with the Corps and settle this thing.

(Tr. 3/203-09) CO Davidson had announced she planned to retire in June 2008 and "there was a real push to get this done before she retire[d]" (tr. 2/149). The Corps did not request any information from KRI in addition to what it submitted in support of its 14 May 2008 REA (tr. 2/148-49, 152-53). A meeting was scheduled for 20 May 2008 (findings 90-92).

90. On 16 May 2008 KRI notified CO Davidson that its 5 May 2008 Pay Request in the amount of \$1,300,000.00 was reduced by the Corps and processed for only \$696,779.01. The difference was the amount of mobilization costs KRI had incurred and submitted as part of the Pay Request.

Needless to say, we have been counting on the Corps making full and timely payments....

I would like to take a moment and summarize for you KRI's financial situation on the project. As shown in our Serial Letter 070, costs to complete the project this year, exclusive of overhead, are \$14.8 million. In order to maintain our planned schedule for the remaining work, KRI requires a cash flow of roughly \$2.3 million per month. As of April 30, 2008, KRI's out-of-pocket costs on the project, exclusive of overhead, stand at \$15.5 million. Payments made by the Corps on the contract stand at \$10.5 million. The net cash shortfall exceeds \$4.5 million.

You can appreciate, considering the size of our company, that we have tapped deeply into our cash resources. The bottom of that barrel has been reached. There is no need for me, in this letter, to recapitulate the severe effect that the federally imposed funding restriction has had upon this project, and upon our company. We already have explored the dimensions of that problem with you and your staff.

Suffice to say, the cash flow situation is at a point where it will seriously impair our ability to maintain the schedule for 2008 completion. It could not be in the government's best interest, and it certainly is not in the best interest of KRI for us to scale back our operation and run the risk that this project will spill over into yet another year, with the inevitable cost escalations that will entail. I would appreciate talking with you about this issue one-on-one, and we would like to have it included as a priority item on the agenda for our Tuesday, 20 May 2008 meeting.

(SR4, tab 11 at 2097-98; tr. 2/150-52) The Corps did not respond to KRI's letter (tr. 2/152).

91. Sometime prior to the parties' meeting on 20 May 2008, KRI had provided to CO Davidson boxes of information to support its REA:

There were boxes and boxes of documents. Because, as you could imagine, there is a lot of invoices and payroll reports and all the backup in computer reports and binders and stuff. It was quite a pile of information.

(Tr. 2/166-67; *see* findings 88-89; *see also* tr. 4/119)

92. The parties met on 20 May 2008 to discuss KRI's REA. Ryan Pleas testified that:

I was in a very positive mood. I thought that when we were going into this meeting, we were actually going to, for the first time since this project had started, this is the first time [the Corps] actually agreed to sit down and go through the numbers and come up with some sort of plan to take care of this issue or the issues that had been in play in this job from Day 1.

....

You know it seemed like, at first, a typical kind of partnering type meeting. We met in Chris Tew's office.... I think he is chief of Contracting in the Anchorage Corps office.... [T]hey couldn't get a conference room.... There wasn't anything available at that facility.

So, Mr. Tew had a small conference table kind of off to the side of his desk. And so, somebody had suggested we use that because [Mr. Tew] was going to be in another meeting. So, we all went in and sat around that table. And [Mr. Tew] came into the office, I think right about the time we started our meeting.... I don't remember him sitting at the table. He was over by his desk or sitting behind his desk getting ready, apparently, for his other meeting. But we started our discussion....

....

My recollection is that Mr. Tew got up. He was kind of listening in. And he got up and I think we were just starting to talk about all the stuff, all the documentation we had provided [finding 91]. I think it was sitting in some boxes in the room there.⁴¹ And he got up and he walked over [to] the table and basically, as I remember it, he looked at my brother, Kelly, and said, I will give you five minutes to explain your case because I have got to go to a meeting. So, you explain your whole, basically, your whole case, why you are entitled, in five minutes because I have got to go to another meeting.... He seemed a little angry.... He just seemed agitated. But again, I didn't know Mr. Tew. I had never met him before. So, maybe that is just his demeanor. I don't know.

So anyway, Kelly spent about five minutes explaining as best as he could. I know Kelly kind of indicated it was a little unfair that he would be asking for a five-minute explanation when this problem took place over many years.

⁴¹ Ryan Pleas testified that "when I looked over at the boxes, it didn't look like anybody had looked at them" (tr. 2/167).

....

At the end of Kelly explaining in five minutes because Mr. Tew was like looking at his watch. He had to get going. He said something to the effect that you know what, really what you should do is go out and find the money and finish the job because we don't have any money. And for us to get the money, we have to go to Congress to get it. It will be easier, it will be faster for you to file a claim and get it from the Ju[dgment] Fund.

....

I was in shock and I am sure Kelly was, too. I know we were both in shock. It was just stunning.... [Mr. Tew left and] we were left with [CO Williams] and [CO Davidson]. And I think basically he just told us we are not going to deal with your REA. Just go find the money. Finish it yourself.

And I think the meeting kept going a little longer. We are still talking, I think, about the VECP, trying to come up with some way to settle that out. I mean at that point, I hardly was paying attention.

(Tr. 2/153-58; *see also* SR4, tab 13 at 17-18, tab 190 at 13; tr. 2/159-60, 4/30, 120-21, 8/27-29) Kelly Pleas testified:

That was like the worst day of my life.

(Tr. 8/28) Even though Mr. Tew was on the Corps' witness list, it never put him on the stand to testify nor did it offer any other credible contemporaneous evidence to rebut Ryan Pleas' testimony and notes on the subject of the 20 May 2008 meeting. After the meeting:

[KRI] had to decide what to do. So, one of the options was to just walk off the job.... I think we wrote a letter...right after this meeting, trying to get back together and try to resurrect this thing. We knew that [CO Davidson] was retiring. So, we figured that any chance of getting this thing done would be much better with her there. So, yes, I know we sent letters trying to salvage this thing.

(Tr. 2/161) Even though CO Williams declined KRI's phone requests for another meeting, KRI's 23 May 2008 letter formally requested another meeting with the Corps to go over KRI's REA:

This letter is a follow-up to our Tuesday meeting, and more particularly, to our Thursday afternoon phone conversation. We tried unsuccessfully several times to call [CO Davidson], and appreciate you talking with us. You have indicated that the Corps will not agree to our request for a further, immediate meeting. Apparently we have failed to convey to you, [Mr. Tew], and [CO Davidson] and the Corps' staff how critical the situation is on this project. Plainly and directly, the circumstances are such that we cannot wait for you and the others to meet internally next Tuesday, as you suggest, and begin formulation of a position letter.

I felt we made it very clear at the Tuesday meeting that, in order to complete the project in the 2008 construction season, KRI has to make multi-million dollar commitments for materials and transportation requirements within the next couple of weeks. We were advised that the Corps has no source of payment beyond the currently committed \$19.8 million. The forecast we prepared, at the Corps' request shows a project cost exceeding \$34 million. We left that meeting with the impression that everyone understood KRI cannot make the commitments for materials and transportation if the Corps is unable to fund the project requirements.

Since our April 10th meeting, we have been developing the backup that [CO Davidson] requested. She wanted a "global settlement" of the financial issues on this project. Needless to say, so did we. [CO Davidson] proposed, and we agreed, to a Modified Total Cost approach. Both sides were committed to arriving at this global settlement before [CO Davidson] retired in early June. The Tuesday, May 20th meeting, we understood, was the point at which the global settlement would be negotiated. You surely can appreciate our surprise and disappointment when we were told, at the outset of that meeting, that the Corps has no way of obtaining funds for this project beyond the current \$19.8 million until next year at the earliest. *How could the*

Corps expect to achieve a global settlement without money to pay for the work? Your suggestion that we “finish the job, file a claim”, in response to which you would “issue a Contracting Officer's Decision” is entirely unsatisfactory. We did not sign a contract which requires us to fund the work, even if the \$15 million differential between project cost and available government funding was something our bank would sponsor. [Emphasis added]

This project was commenced with a Partnering Meeting. It was at that Meeting the Corps advised that there would be a financing restriction imposed which was not part of the contract we bid and signed. Adding this clause to our contract was a fundamental alteration of the agreement. No one appreciated at the time how critical and material this unilaterally imposed revision to the contract was, because none of us forecast the spiraling costs for fuel, materials and the other project requirements. The Corps has to deal with this problem. It is unrealistic and unfair to suppose that the Corps simply can turn its back on the situation and expect that we will take care of it.

We need and respectfully request a Partnering Meeting early next week. We ask that you have Greg, Tony or one of the other legal staff present so that we can be represented. Would you please call me as quickly as you receive this letter? We thank you in advance for a prompt, and much needed response.

(SR4, tab 11 at 2105-06; tr. 8/171-176) Despite KRI's pleas, the Corps never met with KRI again after the 20 May 2008 meeting to discuss its REA (tr. 2/161-62).

93. By letter dated 29 May 2008, CO Williams announced that he would be taking over as the lead CO on the False Pass contract again and he required that KRI convert its REA into a certified claim:

This letter is in response to Serial Letters 067, 069, 070, 071, 073, and 074 submitted by you. We, too, recognize the importance of settling these issues as quickly as possible; however, the following tasks need to be accomplished before we can do so.

Based on the amount of your Request for Equitable Adjustment (REA), the government considers this a claim, not a REA. As such, you will need to treat this matter accordingly and certify your claim in accordance with FAR 52.233-1 Disputes (July 2002), Alt I (Dec 1991).

In your Serial Letter 070, dated 14 May 2008 you state your basis for this REA for over \$16 million having been “documented in extensive correspondence over the past year-and-a-half”. I do not concur with this statement, and simply referencing correspondence in a general basis does not sufficiently address your claim. Further, the government needs to determine the merit of your claim before any discussion regarding the resolution of disputed costs can occur.

In addition to the certification above in order for the government to review your claim, the following three points need to be addressed in detail:

1. Government action in violation of your contract or that gave rise to your REA.
2. Proof that government action caused impacts on your schedule/costs.
3. Proof of what schedule delays or additional costs that are reimbursable.

Once we have received in writing the cause and effect information detailed above, then a meeting between the Government and Kelly-Ryan to discuss this matter would be acceptable.

You are reminded that FAR 52.233-1 Disputes (July 2002), Alt I (Dec 1991), para. (i) states, “The Contractor shall proceed diligently with performance of this contract, pending final resolution of any request for relief, claim, appeal, or action arising under or relating to the contract, and comply with any decision of the Contracting Officer.” If it is your intent to stop performance on your contract before all work is completed, you are required to notify the government immediately so that we can take appropriate action to protect our interests including notification of your surety.

As indicated in the above paragraph, an immediate response is required on whether or not you intend to complete the contract. Please feel free to call me at (907) 753-5571 if you have questions regarding this matter.

(SR4, tab 10 at 184-85; tr. 13/83-86) All the work KRI had done to submit its 14 May 2008 REA with “boxes and boxes” of supporting documentation to CO Davidson’s requirements (findings 89, 91) was apparently treated by CO Williams as if it had never been provided. As Ryan Pleas testified:

We have been going through this for so long with this office and we have explained our position over and over again. And so now, he is basically ignoring everything that has happened prior to this and he is saying start over and explain your whole thing again.

(Tr. 2/164-65, 5/68-69)

94. By letter dated 11 June 2008, KRI expressed its disappointment in the apparent change in the Corps’ approach to KRI’s REA and the contract administration of the False Pass project:

This is a partial response to your May 29, 2008 letter. To begin with, I thought we were on a first-name basis with you, Sandi [Davidson], and the others on the Corps Project Delivery Team. We believed that KRI and the Corps are partners in this project. The positions taken by the Corps at our May 20, 2008 meeting obviously marked an about-face by the Corps, and a full-fledged retreat from the partnering commitment that all of us made over two years ago. From the “global resolution” that [CO Davidson] had proposed, and we had worked diligently to bring about, it now appears you have embarked upon a path of global conflict, with KRI being viewed as your opposition.

....

Since you repeatedly have refused KRI’s request for a follow-up partnering session to the May 20, 2008 meeting; and since your letter imposes enormous documentation pre-conditions to any meeting, these being conditions which you fully appreciate would divert attention, energy

and funds from KRI's construction efforts on the project, you effectively have mandated that we deal with the situation by jousting with the Corps on terms you have imposed. This seems to us a fundamentally different Agency approach than we have come to expect based upon the work we have done with the Alaska District Corps over the past 30 years. We remain convinced that you should reconsider the path you have chosen to deal with these issues, and persist in our belief that an immediate, full fledged, all-issues-on-the-table partnering session is the best way to present and pursue the interests of all concerned parties.

(SR4, tab 11 at 2107-08; tr. 2/167-68, 4/30-33) CO Williams did not respond to KRI's letter.

95. One week later, by letter dated 18 June 2008, the Corps' requested a proposal from KRI to perform additional work to stop beach erosion at the False Pass site (tr. 2/173). KRI responded:

Your Proposal Request raises questions and concerns regarding the Corps' management of this entire project. Preliminary assessment of this added work is that it will carry a substantial, six-digit contract value. KRI repeatedly has been hindered and frustrated in its performance of the work on this project by the funding restrictions that have been imposed. Based upon what we were told by the Corps at our May 20, 2008 meeting, you do not have funds to pay for the escalated costs of the work already under contract. How can it be that the Corps now proposes to significantly increase the performance costs by adding new work?

[KRI also asked if the Corps considered a termination for convenience of the contract at that point an option.]

(SR4, tab 11 at 2287-88; tr. 2/170, 173-76) Once again, CO Williams did not respond to KRI's letter.

96. By email dated 18 July 2008 and letter dated 21 August 2008, KRI continued to request that CO Williams engage with it to resolve the financial status of the project (SR4, tab 11 at 2342-43, tab 34 at 9; tr. 2/168-70, 5/69-70) There is no evidence that CO Williams responded to either communication.

97. KRI's Ryan Pleas testified that, faced with CO Williams' apparent refusal to engage on the subject of the financial status of the project, as well as his direction that KRI was nevertheless to proceed with the contract work to completion (finding 93):

Interestingly enough,...at this point, we could have, if [the incremental funding] clause had been in [the contract], we could have said we are stopping work...because [it] is going to use up all of the available funds for the contract. But by taking that clause and switching [back to the continuing contracts clause] with Mod [P00008], we no longer had the right to do that.

....

[Going back to the continuing contracts clause] gave us an opportunity to settle. This claim, there was no restriction on the Corps or on us on the funding. I mean the [continuing contracts clause] allowed you to go beyond the amount funded to the contract. And a contractor can work beyond that and you don't have to worry about not getting paid.

(Tr. 2/171-72)

[W]e could have made a decision to walk off the job. I mean, that was an option that we talked about. It was not something that we wanted to do. Our preference was to finish the job.

So, we ended up going to our bonding company and sitting down with them, explaining the situation and convinced them that the best option was to work with us and provide the financing to get the job done.

....

[Originally w]e had what they call limited indemnity, which is really hard to get. You have to have years of experience and you have to have a bonding company. And you have to have a good relationship with the bonding company, a good track record because bonding companies, they don't do that much anymore, especially for small contractors.

But we had a good track record through the years. So, they agreed, at one point, to give us a limit of each a half a million dollars. Most of the time, it is an unlimited guarantee. You just sign away everything you own to them. And if they have to, they can go after all of your assets. And Kelly and I had a limited, so we were half a million dollars each, at that time [to secure the bond for the full contract amount].

....

[W]e notified the bonding company that we had a problem. What we thought was going to get resolved in our May 20 partnering meeting was apparently not going to happen. So, we needed assistance or the bonding company would need to hire somebody to finish the job because one way or another, though, the job had to get done and it was up to them what they wanted to do.

What ended up happening was, of course, the bonding company, they wanted more indemnity from Kelly and I for them to participate in loaning the money. So, they asked for another million dollars each in indemnity. So, we agreed.

So, now our indemnity is, we raised our indemnity from half a million dollars to \$1.5 million each.

....

...I mean, it wasn't an easy decision but...we were very confident we had a good claim. We just, in our heart of hearts, felt that if we get this thing before reasonable people that we would be able to settle this thing. You know, it was something that we just thought that just needed to get to a place where somebody with a little less hands-on from the Corps side looking at it, maybe we could sit down and settle this thing.

....

...It was 6.25 percent interest on all funds advanced to the project. So, what we would do is we would make draw requests and provide the documentation. And they would fund the project on an as-needed basis. And we

would file, give them reports, keeping them up to date on where the project stands. And as the loan grew, of course, the interest is ongoing. And to this day, it is still 6.25 percent on the amount that we had to borrow.

....

[Safeco Surety] hired somebody to go out and look at the job. And they had hired, they actually hired an accountant to come in and look at our books. They satisfied themselves in short order that we were the ones to finish the job. I mean they knew that there was nobody going to finish that job more efficiently than we could.

....

[At the time of contract completion, KRI had borrowed and was obligated to repay to Safeco] [r]ight around \$10 million.

(Tr. 2/169-70, 176-80; *see also* SR4, tab 182 at 85-191; tr. 5/113-14, 8/29, 32)

98. Final pricing of the alternate bridge and dock was definitized by bilateral Modification No. P00013, dated 3 October 2008, which stated that:

Any additional costs for Alternate Bridge and Dock design and related Third Year Mobilization/Demobilization will be covered by changing the contract from a unit price to lump sum [of \$19,729,300].

(SR4, tab 14 at 1591-94; tr. 4/28-29, 13/24-25). The net monetary effect of Modification No. P00013 was zero; the additional cost of the alternate bridge and dock and associated additional mobilization was netted against the savings from KRI's underrun for rock. CO Williams testified that:

[M]y intent from changing unit price to lump sum was it effectively helped the contractor out. [KRI came to me with a request:] "In order to finish the contract,...we need to get a loan from our surety and it is imperative that we get the full contract amount."

At this point all parties predicted an under run [for] rock because this is [a] unit priced contract. The

contractor's pay based on the final survey and based on the quantities being placed up to this point, it was expected that would be an under run [for] rock, which would mean the contractor wouldn't get the full contract amount.

Obviously, by being able to have a set contract amount that they knew they were...going to get, it gave...their surety the confidence to give them a loan. That was the whole purpose of this. Effectively, we took the predicted shortfall and gave that to the contractor.

(Tr. 13/25-27) The contract completion date of 5 January 2009 remained unchanged. Modification No. P00013, as executed by the parties, included the following release language:

F. CLOSING STATEMENT

In consideration of the modification agreed to herein as complete equitable adjustments for the Contractor's Alternate Bridge and Dock design as submitted via serial letter H-061 dated 11 Oct 2007, proposal for adjustment, the Contractor hereby releases the Government from any and all liability under this contract for further equitable adjustments attributable to said Alternate Bridge and dock design and related Third Year Mobilization/ Demobilization (except for claims and all impacts related to the changes in funding clause as executed in unilateral Modification P00005, dated 17 Jul 2006 which deleted EFARS 52.232-5001 Continuing Contracts (MAR 1995) and replaced it with 52.232-5004 Incremental Funding Clause)[.]

(SR4, tab 14 at 1594) During the parties' negotiation of the release language, CO Williams repeatedly assured KRI that the above-quoted language reserved KRI's right to claim for all additional costs related to the Corps' unilateral changes of the funding clauses in the contract, while it released the Corps from liability for any further costs associated with the alternative bridge and dock design as well as any additional mobilization/demobilization costs associated with the bridge and dock (SR4, tab 169 at 1-5, 13, 21, 30-33; *see also* tr. 4/32-35, 37-41, 8/111-12, 13/27-28, 127-28, 14/150-57).

99. The contract specified that construction would not occur in the winter when endangered species birds were in the area (SR4, tab 14 at 442, 449-50, 461-62, 467) but that was based on the original date of no in-water work after 1 October each year

(finding 8). Modification No. P00010, however, extended the cutoff date for in-water work to 15 November of each year (finding 83). On 27 October 2008 ACO Jong advised KRI that it *could* do in-water work after 15 November if the following stipulations were met:

- A qualified person from the Alaska District Corps of Engineers is present on-site for all construction operations after this date;
- The Contractor agrees to shut down all construction activities if in the opinion of the Government representative a Stellar Eider comes within 250-feet of the outermost oceanside edge of the project site;
- The Contractor agrees that all construction operations will remain shut down until released by the same Government representative;
- The Contractor will provide transport to/from the project site for up to 3-representatives during this time, and
- The Contractor agrees that the stipulations identified above will be at no additional cost to the Government.

Please respond, in writing, to this office either positively or negatively by close of business on 31 Oct 2008.

(SR4, tab 10 at 225-26; tr. 86-90 (CO admitted that the weather after 15 November “is not the best.”)) By letter dated 5 November 2008 CO Williams offered to further relax the distance from KRI’s work to a bird (SR4, tab 10 at 231-33; tr. 13/90-91). As a result of the associated costs of complying with the Corps’ “five stipulations,” KRI suspended operations at False Pass on 16 November 2008, necessitating a fourth work season. KRI proposed to complete the project NLT 12 June 2009. The work left at the end of the 2008 season to be completed in 2009 was about \$1 million, or ~ 5%. (Tr. 8/37-38; *see* finding 100) The Corps found KRI’s proposal unacceptable and advised that liquidated damages would be assessed and threatened to terminate the contract for default (SR4, tab 19 at 772). We find that KRI was not contractually obligated to work beyond the contractual in-water work date and that its decision to demobilize for the season was reasonable given the weather considerations that late in the season at a remote Alaska jobsite (*see* findings 1, 59). We find no evidence in the record, nor have the parties directed us to any, that liquidated damages were ever assessed.

100. The parties participated in a telephone conference on 11 December 2008 during which the following was discussed:

KRI affirmed that their intention was to return to the project on April 1, 2009 and complete the project by June 30, 2009 per their most recent schedule #20.

....

KRI was asked about their plans for the start of work in the spring. KRI responded that they have just under two barge loads of armor stone remaining and the barges are scheduled to depart in early March to be on the job site in April. Two crews will work on the breakwaters simultaneously placing stone, one crew on the east breakwater and the other on the causeway. The plan is to complete the project on June 12, 2009, but the final drawings will not be submitted until June 30, 2009.

(SR4, tab 13 at 19-20, tab 14 at 2369-70)

101. The Corps accepted the project as substantially complete on 16 June 2009 and the Quality of Workmanship was rated Above-Average as it met or exceeded contract requirements (tr. 2/182, 5/68, 8/39, 13/220, 14/87-88, 15/83).

D. Claim and Contracting Officer's Final Decision

102. On 24 November 2009 KRI submitted five volumes to the Corps containing its 3,054-page certified claim in which it asserted its entitlement to damages in the amount of \$36,231,362 resulting from three breaches of contract by the Corps:

Material Breach No. 1: the removal of the CCC-5001 from the contract and the insertion of the IFC-5004 by unilateral Modification No. P00005;

Material Breach No. 2: the removal of the IFC-5004 from the contract and the insertion of the CCC-5001 by unilateral Modification No. P00008⁴²;

⁴² KRI appears, in its post-hearing brief and reply brief, to have abandoned its claimed Material Breach No. 2 as a stand-alone breach of the contract and we will not address it further.

Material Breach No. 3: breach of the duty of good faith and fair dealing to include Material Breach Nos. 1 and 2 as well as various enumerated Corps actions and inactions in its administration of the contract which caused the contract work “to become more difficult, more time consuming, and more expensive to perform.”

(SR4, tab 3 at 17-66; *see also* SR4, tab 2 at 5) KRI also sought an extension of the contract performance period to June of 2009 (SR4, tab 3 at 19; tr. 5/67-68, 72-83, 87-92, 194-98). By letters dated 30 September 2011 and 26 June 2013, KRI amended the amount sought in its claim to \$25,313,031, exclusive of Contract Disputes Act (CDA) interest (amended compl. at 30-34; SR4, tab 11 at 2622-25, tab 182 at 1-2, 7-11; tr. 5/104-09). KRI’s amended claim sought breach damages calculated as follows:

- A. Damages through 9 January 2007 in the amount of \$5,808,719.19, alleged to be calculated on the basis of termination for convenience principles and referred to by KRI as “Termination Settlement Pricing”;
- B. Damages from 10 January 2007 through project completion in the amount of \$19,326,328.55, calculated by KRI to be based on what KRI estimated the project would have cost the Corps if the project had been terminated for convenience instead of unilaterally incorporating the IFC-5004 into the contract and then the project was reprocured in 2008 which is referred to by KRI as “Restitution Pricing.”

(SR4, tab 5; tr. 3/59-60, 63-71, 5/95-96; amended compl. ¶¶ 71, 76-81)

103. On 22 January 2010 CO Williams notified KRI that he would issue a contracting officer’s final decision (COFD) on the subject of KRI’s 24 November 2009 certified claim no later than 24 November 2010, one year after receipt of the certified claim. On 4 March 2010 KRI filed its notice of appeal from a deemed denial of its 24 November 2009 certified claim which was docketed as ASBCA No. 57168. The Corps filed a motion to dismiss the appeal as premature and, after briefing by both parties, the Board found the period of time specified by the Corps for completion of the COFD to be unreasonable under the circumstances and denied the Corps’ motion. *Kelly-Ryan, Inc.*, ASBCA No. 57168, 11-1 BCA ¶ 34,629.

104. A DCAA audit of KRI’s 24 November 2009 certified claim was begun sometime in 2010 (SR4, tab 19 at 719-20) and the resultant DCAA audit report was issued on 23 March 2012⁴³ (SR4, tab 19 at 578-668, tab 138). The audit report states:

⁴³ We find no evidence that the Corps ever requested DCAA audits of KRI’s later amendments to its claim (findings 102, 106-08).

Entitlement to the price adjustment claim is a legal issue. Because entitlement is a legal issue, the primary purpose of our examination is to review the quantum aspects of the claim.

(SR4, tab 138 at 3) Despite this statement, the audit report devoted more than half of its 91 pages to the DCAA auditor's legal interpretation of contract clauses and determinations of entitlement ("to properly determine if the Government was responsible for the claimed costs") as its basis for questioning \$40,541,437, more than \$4 million more than the \$36,231,362 total costs claimed by KRI (*id.* at 9-24, 26, 30-41, 51-58, 67-70, 75-78; *see also* SR4, tab 19 at 669-752, tab 187; tr. 6/10-25, 29-59, 59-64, 113-16). We find the audit report not to be credible to the extent it makes such entitlement determinations which are beyond its authority.⁴⁴ We find the audit report credible only to the extent it analyzes claimed costs on the basis of whether KRI actually incurred the costs it claims to have incurred and that those costs are allowable and allocable to this project. We also find the credibility of the audit report to be further weakened by unrebutted evidence⁴⁵ that the audit work papers do not support the various audit methodologies described, nor certain of the amounts questioned. (SR4, tab 187 at 2-3, 7, 22, 25, 29, 31, 33)

105. On 30 May 2012 the Corps finally issued a COFD, 2½ years after submission of the certified claim and 1½ years after the parties entered into discovery in KRI's appeal from a deemed denial (SR4, tab 2; tr. 13/93-95, 109-12; *see also* amended compl. ¶¶ 82-89). CO Williams testified that this was the first COFD he had ever been involved with as a CO and he did not author the 101-page COFD. Instead, after the COFD was prepared by Corps attorneys and contracting personnel who had no involvement in the False Pass project, CO Williams took "several afternoons" to review it and provided two comments which were incorporated before he signed it. (Tr. 13/146-70, 14/35-39, 42-51, 14/35-36) The COFD denied KRI's certified claim in its entirety, taking no responsibility for any of the delays or increased costs incurred by KRI (SR4, tab 2).

106. On 12 June 2013, after receiving the COFD and DCAA audit report, KRI submitted its "Supplemental and Alternative Contract Adjustment Pricing of its Compensable Damages, using Modified Total Cost Methodology" ("MTC pricing submission") in the amount of \$20,482,166 using the methodology requested by the

⁴⁴ *See BAE Systems San Francisco Ship Repair*, ASBCA No. 58809, 14-1 BCA ¶ 35,642 at 174,535 (DCAA audit report is advisory only, only the CO has authority to decide contractor claims).

⁴⁵ The Corps did not offer testimony from the auditor or any other DCAA personnel involved in either of the two audits performed under this contract.

Corps and recommended by DCAA (SR4, tab 5 at 70; tr. 5/128-32, 171-82, 8/25-26, 138). KRI broke down the total amount of its MTC pricing submission as follows:

<u>Total cost before adjustments:</u>	
Total booked direct costs from KRI's Job Cost History Report	\$34,970,152
-Less booked actual equipment, maintenance and repair costs	-4,743,786
-Plus equipment, maintenance and repair costs estimated using Corps manual EP 1110-1-8	4,724,661
-Plus equipment standby expense	1,643,123
Total direct job costs	\$36,594,150
<u>Adjustments to total cost called for by MTC pricing principles:</u>	
-Plus allowable direct job costs not booked in KRI's Job Cost History Report	16,532
-Less "KRI adjustments for extra costs not the responsibility of the government (costs not included in the bid estimate, cost over-runs that were the responsibility of KRI"	-3,915,062 ⁴⁶
-Less additional costs questioned by DCAA "or determined by KRI to be unallowable, unallocable, not the responsibility of the government, or understated in the bid"	-87,987
-Miscellaneous costs not allowed per DCAA audit	-137,367
<u>Total direct job cost, adjusted per MTC pricing principles:</u>	\$32,470,266
-Plus G&A (11.383%)	3,696,090
Subtotal	\$ 36,166,356
-Plus profit (10%)	3,616,636
Subtotal	\$ 39,782,992
-Less amount paid by the Corps under the contract	-19,445,279

⁴⁶ KRI's support for this reduction to its MTC pricing is contained in the record at Stipulated Rule 4, tab 5 at 166-313.

Subtotal, claim without additional bond expense	\$ 20,337,713
-Plus "additional bond expense that will be incurred by KRI for the claim amount" when paid	144,453
Total, MTC pricing claim, exclusive of CDA interest	\$20,482,166

(SR4, tab 5 at 68-70) The 1190-page MTC pricing submission provided KRI's alternative calculation of damages arising from the three material breaches articulated in KRI's 24 November 2009 certified claim, relied on the thousands of pages of documentation previously provided to the Corps with KRI's 24 November 2009 claim (finding 102), as well as including explanations of each category of cost along with supporting documentation (including copies of all supporting invoices over \$3,000).

- This is not a new and different claim. It is based upon the same entitlement principles, and the same project and cost records, upon which KRI based its November 26, 2009 certified claim submittal to you.
- The method of quantifying KRI's recoverable damages is the principal difference between this submittal and KRI's original submittal.
- KRI maintains its position that the damages to which it is entitled on this appeal should be calculated and awarded on the Termination For Convenience and Restitution Pricing which we utilized in the Original Equitable Adjustment/Breach Claim.
- KRI's submission of this Modified Total Cost alternative is not intended to substitute for, or to amend, the Original Equitable Adjustment/Breach Claim. It is supplemental and alternative.

KRI has reviewed carefully the comments made in the CO[F]D and the DCAA Audit Reports regarding the company cost records. This Modified Total Cost submittal has accounted for those comments wherever we found that an adjustment needed to be made. Those adjustments to some extent will affect the cost calculations used in the November 2[4], 2009 submittal. Such adjustments will be made by amending the Complaint filed with the ASBCA. The Amended Complaint also will assert a separate Count utilizing the Modified Total Cost Pricing.^[47]

⁴⁷ KRI filed the referenced amended complaint with the Board on 31 May 2013.

I have been advised that because the Modified Total Cost Pricing is what the Government agreed should be the “method to negotiate settlement of this claim,” it would be appropriate, even though not required, that the cost or pricing data be certified. Accordingly, I hereby certify that the cost or pricing data submitted herewith to the Contracting Officer or the Contracting Officer’s representative in support of KRI’s Supplemental and Alternative Contract Adjustment Pricing of its Compensable Damages, are accurate, complete and current as of the date of this letter.

(SR4, tab 5 at 2; *see also* tr. 8/45-59)

107. On 13 May 2014, KRI submitted a third amendment to its claimed termination/restitution damages (*see* finding 102) in the total amount of \$28,233,818, exclusive of CDA interest (SR4, tab 182 at 1-29, 52-195; tr. 5/83-86, 92-95, 104-18, 165-71, 182-88, 9/28-33).

108. Also on 13 May 2014, KRI submitted an update to its alternative MTC calculation of damages (finding 106) in the total amount of \$23,402,953, exclusive of CDA interest (SR4, tab 182 at 30-195; tr. 5/118-34, 9/34-35). The update started with the \$20,482,166 total presented in the original MTC pricing submission (finding 106) and then presented additional adjustments as follows:

<u>Total, MTC pricing claim, exclusive of CDA interest</u>	\$20,482,166
<u>Description of additional adjustments:</u>	
-Less “Credit for Revised Demobilization Transportation Impact” for equipment left at Dutch Harbor and not demobilized to Seattle	-612,296
-Plus calculation error in estimated equipment, maintenance and repair costs using Corps manual EP 1110-1-8	462,360
-Plus “Cost of Borrowing” through 30 April 2014 (<i>see</i> findings 92, 97)	3,052,477
-Less claim preparation costs booked to job costs	-2,353
-Less bond adjustment in original MTC pricing submission	-144,453
<u>Adjusted Subtotal</u>	\$23,237,901

-Plus updated "additional bond expense that will be incurred by KRI for the claim amount" when paid	165,052
<u>Total, MTC pricing claim, exclusive of CDA interest</u>	\$23,402,953

(SR4, tab 182 at 50) The 195-page updated MTC pricing submission included explanations and supporting documentation.

109. Just a few months before the hearing in this appeal, KRI's expert witness Mr. Humphreys updated his expert report in which he recommended the further recalculation of KRI's MTC pricing submission to increase its claimed damages to \$31,111,139, exclusive of CDA interest (SR4, tab 19 at 1175-76).

110. We find that KRI's use of the Corps manual to estimate its equipment costs for purposes of its claim submissions was not appropriate under the circumstances that its actual equipment, maintenance and repair costs were available and calculated accurately enough that KRI was able to determine the specific amount of its actual costs in order to reduce its claimed costs by that amount and then add the higher estimated amount resulting from use of the manual. After careful examination of the record before us, we further find that the actual Total Booked Direct Costs, as well as the adjustments, reductions and additions to actual costs made by KRI, that are listed in KRI's first and second MTC pricing submissions (findings 106, 108) are supported by the contemporaneous documentation provided to the Corps and DCAA by KRI from its Job Cost History Report and accounting records. With the exception of its attention to KRI's use of the Corps manual to estimate equipment and equipment-related related costs, the Corps has offered arguments challenging KRI's claimed costs but it has offered almost no credible factual evidence to rebut KRI's claimed costs. We, therefore, find the claimed costs contained in the first two MTC pricing submissions to be credible presentations of KRI's actual costs incurred in performing the False Pass project.

111. KRI's complaint and amended complaint reiterated the three material breaches contained in its certified claim as the legal basis for the damages it now seeks (*see* finding 102).

DECISION

KRI's certified claim seeks damages it claims resulted from material breaches of the contract by the Corps which caused the contract work "to become more difficult, more time consuming, and more expensive to perform" (SR4, tab 3 at 39). The claimed material breaches now before us for decision are: (1) the removal of the CCC-5001 from the contract and the insertion of the IFC-5004 by unilateral Modification No. P00005; and, (2) a continuing breach of the implied duty of good faith and fair dealing by the

Corps in its administration of the contract (findings 102, 111). It is the Corps' position that it did not breach any of its express or implied duties or obligations under the contract and that none of the delays, interruptions or additional costs claimed by KRI were caused by the actions or inactions of the Corps.

In order to meet its burden of proof with respect to each claimed breach of contract, KRI must prove that: (1) there is a valid contract between KRI and the Corps; (2) there is an obligation or duty on the part of the Corps arising out of the contract; (3) the Corps has breached that duty or obligation; and (4) KRI has suffered damage as a result of the breach. *Military Aircraft Parts*, ASBCA No. 60009, 16-1 BCA ¶ 36,388 at 177,410.

A breach is material if it relates to a matter of vital importance or goes to the essence of the contract. "The standard of materiality for the purposes of deciding whether a contract has been breached 'is necessarily imprecise and flexible.'" In determining the materiality of a breach, we may consider some or all of the "significant" circumstances from the RESTATEMENT (SECOND) OF CONTRACTS § 241:

- (a) the extent to which the injured party will be deprived of the benefit which he reasonably expected;
- (b) the extent to which the injured party can be adequately compensated for the part of that benefit of which he will be deprived;
- (c) the extent to which the party failing to perform or to offer to perform will suffer forfeiture;
- (d) the likelihood that the party failing to perform or to offer to perform will cure his failure, taking account of all the circumstances including any reasonable assurances;
- (e) the extent to which the behavior of the party failing to perform or to offer to perform comports with the standards of good faith and fair dealing.

Consumers Oil Co., ASBCA No. 24172, 86-1 BCA ¶ 18,647 at 93,713-14. "[I]t is not to be expected that, in every case, each of the five [§ 241] circumstances will be

pertinent.... It is to be expected, however, that circumstances (a) ('the extent to which the injured party will be deprived of the benefit which he reasonably expected') will always be a pertinent consideration." *Hansen Bancorp, Inc. v. United States*, 367 F.3d 1297, 1312 (Fed. Cir. 2004); *see also Consumers Oil*, 86-1 BCA ¶ 18,647 at 93,713-14 (it is "important" to consider the extent to which the injured party will be deprived of the benefit of the exchange). Ultimately, whether a breach is a material breach depends on the nature and effect of the violation in light of how the particular contract was viewed, bargained for, entered into, and performed by the parties. *Stone Forest*, 973 F.2d at 1551.

Highland Al Hujaz Co., Ltd., ASBCA No. 58243, 16-1 BCA ¶ 36,336 at 177,165 (some citations omitted).

There is no dispute that, at all times relevant to the matters before us, there was a valid contract between KRI and the Corps and the first element of proof is therefore met. We will next address elements 2 and 3 with respect to each claimed breach of contract. Finally we will address whether and to what extent KRI's claimed damages have met the requirement of element 4.

A. Removal of the CCC-5001 from the contract and the insertion of the IFC-5004 by unilateral Modification No. P00005

1. Material Breach of an Express Term of the Contract

The first material breach claimed by KRI is the Corps' unilateral removal and replacement of the CCC-5001 with IFC-5004 in Modification No. P00005 a year after contract award. It is the Corps' position that the unilateral actions of removal and replacement were not a breach, arguing that the CCC-5001 and IFC-5004 were essentially the same clause and so the exchange was merely an administrative change to the contract that was within CO Williams' authority (gov't br. at 53-55). The FAR defines an administrative change as one that does not affect the substantive rights of the parties (finding10).

On 11 July 2005 the parties executed the contract for the False Pass project that is now at issue and the bargain struck by the parties included, among other rights, duties and obligations, KRI's express obligation to perform the contract work by 4 January 2008 and the Corps' express obligation to fund the contract in accordance with the CCC-5001. It is difficult to imagine a contract term of more vital importance than the funding clause that established the Corps' funding obligations. The failure to

fulfill an express obligation contained in the contract is a breach of contract. *Metcalf Construction Co. v. United States*, 742 F.3d 984, 990 (Fed. Cir. 2014).

The great weight of the voluminous record before us makes clear that there were very significant differences between the CCC-5001 and IFC-5004 in the way they affected the funding of contract work, claims and termination costs. The CCC-5001 made the Corps liable to pay a contractor for work performed, as well as possible claims and termination costs, from funds beyond those reserved to the contract. It was this potential for future liability beyond the funds reserved to the contract that Congress expressly prohibited by its passage of the E&WDA. (Findings 4, 9, 20, 23, 30) The IFC-5004, a new clause unilaterally added to KRI's contract a year after contract award to replace the CCC-5001, limited the Corps' liability to whatever funds were reserved to the contract; any work, claims or termination costs incurred beyond that amount would no longer be paid in the future from other funds as they had been under the CCC-5001 (findings 4, 23, 30-31). This was acknowledged by HQUSACE to be a "big deal" and a "huge" "sea change" in the way the Corps had traditionally conducted its business when dealing with continuing contracts (findings 20, 30). The record supports KRI's description of how, after the unilateral addition of IFC-5004 to its contract, the False Pass project became a very different construction project from the one advertised, bid and awarded:

The financial flexibility available to the contractor under the CCC[-5001], stands in stark contrast to the strict limitations under the IFC[-5004], which include the necessity for estimating and maintaining a holdback reserve to cover costs which attend the risk of termination, very much a real risk because the project is not in next years' budget and thus has not been "funded" for those years, accompanied by the contractor knowing that he is not entitled to be paid for contract work performed or obligations incurred which exceed the amount funded to the contract. These differences...foreseeabl[y] can, and in fact, do, affect the way that a contractor plans and executes his construction operation. That contractor having bid and planned his project with assurance that the entire contract amount is available for him to use and to commit, but on the eve of starting work is advised that just a part of the money is there, and he must not spend or make commitments beyond that lesser amount because the Government is not obligated to pay any more than that lesser amount, in addition to which he must calculate and not spend whatever sum may be needed to cover claims from costs of termination, the cost of demobilization,

amounts owed to subcontractors and suppliers for expenses they have incurred regardless of whether their product has been incorporated into the project, and so forth.

(App. br. at 36-37; *see also* app. br. at 47-54) Not only did the change in funding clauses potentially require very different planning of the work for any contract, but KRI's False Pass contract was further complicated by the unique requirements of an already-shortened construction period in an extremely remote location with unique supply circumstances (findings 1, 3, 32, 34-35, 59).

HQUSACE recognized with the passage of the E&WDA in November 2005 that changing the funding clause in existing contracts without negotiating appropriate consideration could constitute a breach of contract and it immediately issued guidance to both the program management community and the contracting community making clear that, while it was mandatory to change the funding clause in contracts such as KRI's that were not funded in the out-years, a unilateral modification of the existing contracts was "not sufficient." The Corps' guidance took care to specifically direct that the Corps' compliance with the legislation by program management and contracting personnel be accomplished in a manner that would limit the Corps' financial risk while at the same time making sure the affected contractors' financial risk was also limited. Both guidance documents directed that a bilateral modification was to be negotiated and, if that could not be accomplished, then either additional funds were to be reprogrammed to the contract or the contract was to be terminated for convenience. (Findings 4, 20, 23, 30-31) It is undisputed that CO Williams was fully aware of HQUSACE's guidance but consciously ignored it and took none of the three directed actions. Instead he chose to replace the funding clause by unilateral Modification No. P00005. Even though HQUSACE and his supervisor directed him to rescind the unilateral modification and follow the guidance, he ignored their direction. (Findings 29-30, 32, 40, 42-45, 47)

When CO Williams unilaterally removed the CCC-5001 and replaced it with the IFC-5004, admittedly without attempting to negotiate with KRI, the Corps reduced its own contractual obligation without giving any valuable consideration in return to KRI. As we said in *Supply & Service Team GmbH*, ASBCA No. 59630, 17-1 BCA ¶ 36,678 at 178,599:

After all, if one party were to simply reduce its obligations under the contract and the other received nothing in return, there would be no consideration to the short-changed party for having waived its contractual expectations.

This is the very definition of a material breach of an express term of the contract.

The Corps argues that the contract (whether it contains the CCC-5001 or the IFC-5004) expressly precludes a claim for breach of contract (gov't br. at 49-50). However, what the funding clause in the contract actually prohibits is a breach of contract claim based upon a failure to add funds to the contract (*see* findings 9, 31). There is no language prohibiting claims based on other breaches of contract. The basis of KRI's first alleged breach is not that the Corps failed to add funds, but that the Corps unilaterally changed the entire funding clause long after the bargain was struck at the time of contract award, the effect of which was a shifting of financial risk to KRI for work, claims and/or termination costs which had been allocated to the Corps under the CCC-5001 at the time of advertisement, bid and contract award. KRI's other breach claim, addressed below, is an alleged material breach of the implied duty of good faith and fair dealing. There is also nothing in the contract precluding this claim. We find no legal basis for the Corps' argument that the contract prohibits KRI's breach of contract claims and reject it.

The Corps argues that there were always enough funds reserved to the contract in 2006 for KRI to complete the work as it had originally planned. The contemporaneous record amply demonstrates that, when KRI set aside enough funds to cover the possibility of claims and termination costs as it was repeatedly directed by the Corps to do, there were only enough funds reserved to the contract to perform the \$6.1 million of work that KRI completed prior to demobilizing for the winter (findings 34, 36-37, 51). In that case, the Corps argues, KRI breached the contract by failing to provide the proper notice under the IFC-5004 in anticipation of an exhaustion of funds. First, the record shows that KRI provided multiple notices to the Corps during the 2006 construction season that, once it set aside the amount for possible claims and termination costs as required by the Corps, the remaining funds reserved to the contract required that KRI reduce its planned work for that season. If KRI's notices did not meet the letter of the unilaterally imposed IFC-5004, it was because, by the time the Corps actually modified the contract to include the clause, the time for notification had already passed (findings 31, 42). Second, the source of the breach argued by the Corps, the IFC-5004, did not exist in KRI's contract until the Corp's breach of that contract by unilaterally replacing the CCC-5001 with the IFC-5004 over a year after contract award. The Corps' breach of contract was, therefore, the first, or antecedent, breach which provided KRI with a legal excuse for nonperformance with the notice requirement under the IFC-5004. *Laguna Construction Company*, ASBCA No. 58324, 14-1 BCA ¶ 35,748 at 174,948, *aff'd*, *Laguna Constr. Company v. Carter*, 828 F.3d 1364, 1369-71 (Fed. Cir. 2016).

On the basis of the foregoing, we find that KRI has met its burden of proof as to elements 2 and 3 of its claimed material breach of an express contract term.

2. Material Breach of the Implied Duty of Good Faith and Fair Dealing

KRI claims next that the Corps' unilateral replacement of the CCC-5001 with the IFC-5004, in addition to being a breach of an express term of the contract, also breached the Corps' implied duty of good faith and fair dealing (finding 102). In addition to the rights, duties and obligations expressed in the contract, both KRI and the Corps owed each other the implied duty of good faith and fair dealing that is inherent in every contract.

In *Metcalf Construction Co. v. United States*, 742 F.3d 984, 990 (Fed. Cir. 2014), the United States Court of Appeals for the Federal Circuit affirmed the basic principle that the parties to a government contract are under a duty of good faith and fair dealing in the performance and enforcement of the contract, and that failure to fulfill that duty constitutes a breach. "The covenant of good faith and fair dealing...imposes obligations on both contracting parties that include the duty not to interfere with the other party's *performance* and not to act so as to destroy the *reasonable expectations* of the other party regarding the *fruits of the contract*." *Id.* at 991 (citing *Centex Corp. v. United States*, 395 F.3d 1283, 1304 (Fed. Cir. 2005)).

In order to prove a violation of the duty, a contractor need not necessarily prove that the government specifically targeted action to obtain the benefit of the contract or that the government's actions were undertaken for the purpose of delaying or hampering performance of the contract. *Metcalf*, 742 F.3d at 993. Rather, the implied duty of good faith and fair dealing is "limited by the original bargain: it prevents a party's acts or omissions that, though not proscribed by the contract expressly, are inconsistent with the contract's purpose and deprive the other party of the contemplated value." *Id.* at 991.

Military Aircraft Parts, 16-1 BCA ¶ 36,388 at 177,411.

In particular, a "bait and switch" breaches the duty of good faith and fair dealing. *Teresa A. McVicker, P.C.*, ASBCA Nos. 57487, 57653, 12-2 BCA ¶ 35,127 at 172,463. A bait and switch occurs when the government

awards a significant contract benefit to a contractor, only to improperly eliminate that benefit soon thereafter.

K2 Solutions, Inc., ASBCA No. 60907, 17-1 BCA ¶ 36,801 at 179,375-76. The Court of Appeals for the Federal Circuit found a breach of the implied duty of good faith and fair dealing in *Centex Corp. v. United States*, 395 F.3d 1283 (Fed. Cir. 2005), and *First Nationwide Bank v. United States*, 431 F.3d 1342 (Fed. Cir. 2005), both cases in which legislation was specifically targeted to eliminate a material part of the consideration and precise benefit contracted for.

The issue is not whether Congress can enact legislation that abrogates or modifies existing government contracts; the issue is whether the government is liable for the consequences of such action. While a contract does not prevent Congress from enacting legislation, the government may incur liability for damages when the legislation materially affects performance of the contract. *Winstar*, 518 U.S. at 870; *see Mobil Oil Exploration*, 530 U.S. at 619-20.... When the government as contracting party makes a promise in exchange for a benefit, it is bound by mutual obligations, as any party to a contract is bound.

[The legislation at issue] was directed at existing contracts to which the government was a party, and retroactively abrogated contract provisions entered into under the prior policy.... The Court of Federal Claims correctly held that the United States is liable for the financial consequences of this action as it affected existing contracts.

First Nationwide Bank, 431 F.3d at 1350-51; *see also Centex*, 395 F.3d at 1309.

Cases in which the government has been found to violate the implied duty of good faith and fair dealing typically involve some variation on the old bait-and-switch. First, the government enters into a contract that awards a significant benefit in exchange for consideration. Then, the government eliminates or rescinds that contractual provision or benefit through a subsequent action directed at the existing contract. The government may be liable for damages when the subsequent government action is specifically designed to reappropriate the benefits the other party expected to obtain from the

transaction, thereby abrogating the government's obligations under the contract. [Citation omitted]

Precision Pine & Timber, Inc. v. United States, 596 F.3d 817, 829 (Fed. Cir. 2010).

The Corps was aware, prior to its preparation of the solicitation for the False Pass project, of the impending passage of the E&WDA legislation which directed a change in the Corps' policy regarding the funding of continuing contracts (finding 4), a change that HQUSACE recognized would be a "sea change" in how it funded continuing contracts (findings 20, 30). Nevertheless, the Corps (HQUSACE and the Alaska District) advertised, accepted bids, and awarded the False Pass contract with the CCC-5001 in it instead of the IFC-5004, with full knowledge that the CCC-5001 would have to be replaced with the IFC-5004 at some later time. The Corps did not share this knowledge with KRI. (Findings 20, 47) By its failure to share the information, the Corps retained to itself all knowledge of the need to later remove the CCC-5001 funding clause from the contract and replace it with the more restrictive IFC-5004. Without any knowledge of the coming change in funding clauses, KRI prepared its bid and planned its means, methods and schedule for completing the contract work based upon the CCC-5001 with which it was familiar. As Ryan Pleas testified:

I mean, if...that project had that IFC clause in it before we bid it, I could have assessed the risk and I might have said, "You know what? I don't know if I want to bid this job." I can't take that kind of risk, or if I bid it, I'm going to put a bunch of money on it because the IFC clause, especially in a contract that's remote in Alaska, is a whole different duck.... Under the continuing contracts clause, we don't have to – we're not worried about the funding stream.

(Finding 35) Contemporaneous evidence shows us that the Corps (Alaska District) was well aware that the change in funding clause from the CCC-5001 to the IFC-5004 was required and could impact KRI's schedule and costs. Nevertheless, the Corps elected to withhold this information from KRI until 3 April 2006, almost a year after contract award and months after the Corps' receipt and acceptance of KRI's schedule and cash flow forecasts based on the CCC-5001. (Findings 26, 29, 32, 34) The Corps thus kept all reduction of financial risk to itself, while at the same time it increased KRI's financial risk, rather than limiting KRI's risk as required by the E&WDA, EC and PIL (findings 4, 23, 30).

On the basis of the foregoing, we hold that the Corps' unilateral replacement of the CCC-5001 with the IFC-5004 constituted a bait-and-switch which is a breach of the Corps' implied duty of good faith and fair dealing.

B. Continuing Breach of the Implied Duty of Good Faith and Fair Dealing

KRI further claims that the Corps continued to breach its implied duty of good faith and fair dealing by engaging in a “multi-year pattern of delay and avoidance” by refusing to discuss or otherwise address the contract performance and financial impacts suffered by KRI as a result of replacement of the CCC-5001 with the IFC-5004 (finding 102). As we discussed above, the Corps had the implied duty under the contract to not delay, hamper or otherwise interfere with KRI’s performance of the contract and thereby to deprive KRI of its reasonable expectations of the contract’s value at the time of contract award. This duty was in addition to the express terms of the contract such as the partnering, changes and disputes clauses that imposed express duties and obligations upon the Corps. The Corps argues that all delays and impacts experienced by KRI in the performance of the contract were caused by KRI and not by the Corps.

The contemporaneous record shows that, during the 2006-2009 contract performance period, the Corps’ recognized that the change from the CCC-5001 to the IFC-5004 was a significant change in how the Corps funded contracts such as the one awarded to KRI and that the change could affect KRI’s means, methods and schedule. The Corps (Alaska District) negotiated a bilateral contract modification with Western Marine (*see* finding 29), the contractor on the only other continuing contract project in the Alaska District over \$10,000,000, but never attempted to fulfill its affirmative duty to negotiate a bilateral contract modification with KRI under the False Pass contract (findings 29, 42-45, 47). The Corps repeatedly directed KRI to be sure to set aside enough of the funds reserved to the contract to cover any additional work, and potential claims and termination costs (items that would have been the Corps’ liability under the CCC-5001 but were KRI’s liability under the new IFC-5004), contemporaneous evidence that the Corps knew and understood the significant differences in the two clauses. The Corps also repeatedly assured KRI that it could submit a claim for any impacts resulting from the unilateral change in funding clauses along (*see* findings 11, 34, 68, 89, 92, 94, 98), which is compelling contemporaneous evidence that the Corps also understood that the funding clause change could affect KRI’s planned and actual performance of the contract work.

As we have found, any analysis of actual work performance in comparison to KRI’s schedules for construction seasons 2006 and 2007 are of little value to us because the Corps would not process KRI’s payment requests unless KRI’s schedule showed the original contract completion date. This forced KRI to manipulate its schedules to show planned work to be something other than was actually planned in order to comply with the Corps’ demand. (Findings 37, 68, 75, 77) The Corps, for the first time in its COFD, offers arguments with little, if any, credible evidentiary support in an attempt to convince us that all delays and increased costs experienced by KRI

were of its own making. Except as expressly addressed below, we have carefully considered these arguments and found them to be unpersuasive.

For the first time in the COFD the Corps argued that KRI delayed the start of the project in 2006 because it was not ready to begin work. The contemporaneous record, however, is very clear that KRI's late start was the Corps' specific choice after acknowledging that the effect of the IFC-5004 on the funding available for the 2006 construction season, after KRI set aside a certain amount to cover items that would previously have been funded under the CCC-5001, was less than the work KRI had planned to perform in its previously-approved schedule for 2006. It was also the Corps' decision to delay the bridge and dock work (regardless of whether the original design or KRI's VECP) to a later season. (Finding 34)

The record shows that there was a very real concern on the part of the Corps and KRI that Congress would not appropriate additional funds in support of the False Pass project beyond those already reserved to the contract in 2006 and that, if there were no additional funds, the contract would need to be terminated for convenience (findings 34, 40, 46, 48, 58). This very real possibility of termination for convenience, and KRI's estimated potential costs associated with it, required KRI, under the IFC-5004 and in compliance with the Corps' continued reminders to do so, to continue to set aside a certain amount of the funds reserved under the contract in 2006 to cover additional work, claims and termination costs. Nevertheless, CO Williams refused to meet with KRI to discuss the matter and further refused to even consider termination because that would likely result in the end of a project that the Corps had been trying to get done for 10 years (finding 46). Over the winter between the 2006 and 2007 construction seasons, when KRI would normally have been making arrangements and financial commitments in preparation for the 2007 construction season, KRI could not do so because it had no way of knowing whether there would actually be a 2007 construction season: (1) if Congress did not appropriate more funds, the contract would be terminated for convenience and there would be no further work to prepare for; and, (2) until the Corps issued a contract modification reserving additional funds to the contract and it was known that the contract would not be terminated, there were not sufficient funds remaining, after setting aside funds to cover costs previously covered by the CCC-5001, to cover the commitments that KRI had to make in preparation for the 2007 construction season. KRI was in a holding pattern of the Corps' making and there was no contact from the Corps with regard to funding from the fall of 2006 until March 2007 when KRI was first made aware that the contract was not terminated and Congress had appropriated the balance of the contract award amount of funds. KRI had planned to mobilize for the 2007 construction season in April 2007. However, since it had been unable to perform the necessary preparation over the winter, it was not able to perform a good deal of the work it had planned to complete in that season. The Corps argues that the reason KRI was unable to perform as it had planned in the 2007 construction season was because of rock production

difficulties by its subcontractor, Northern Mechanical. The contemporaneous record, however, shows that Northern Mechanical's difficulties were with production of armor stone, the final layer of rock to be placed on the breakwaters, and that there was no issue with production or placement of either core rock or B rock in that season. In fact, the Corps recognized in Modification No. P00013 that KRI had actually needed less rock than originally planned (i.e. a rock underrun) to complete the breakwaters to contract specifications (finding 98).

In July 2007, CO Davidson became involved as the primary CO and her first contact with KRI was to demand, without any apparent recognition of the unilateral funding clause change and the resulting impacts to KRI's schedule, that KRI complete contract performance by the original completion date. Once she was more fully informed by KRI as to what had occurred before her involvement, CO Davidson requested that KRI submit an REA in two parts: the first part, REA I, was to address KRI's request for an extension of the contract performance period due to the impacts of the unilateral funding clause change and the second part, REA II, was to address KRI's request for compensation for the monetary impacts suffered by KRI as a result of the impacts of the unilateral funding clause change. KRI did so. (Findings 72-73, 76, 77, 85, 88-89, 91) The parties met on 20 May 2008 but CO Davidson's professed goal of negotiating a global settlement of all issues then-existing was never realized. Instead, chief of contracting Tew told KRI that:

[KRI] should...go out and find the money and finish the job because [the Corps doesn't] have any money. And for [the Corps] to get the money, [it would] have to go to Congress to get it. It will be easier, it will be faster for [KRI] to file a claim and get it from the Ju[dgment] Fund.

(Finding 92)

CO Davidson retired in June 2008 and CO Williams resumed the lead CO role for the False Pass project. CO Williams immediately abandoned KRI's 13 May REA submission and CO Davidson's plan to use the REA as a basis to negotiate a global settlement. Instead, he required KRI to prepare and submit a certified claim meeting more stringent requirements than those required by CO Davidson. (Findings 93-95) KRI submitted its certified claim on 24 November 2009 (finding 102). Following Mr. Tew's direction to KRI to find the money, complete the project and file a claim, as well as CO Williams' direction to proceed to perform the contract to completion (finding 93), KRI, as an experienced marine construction contractor in long-term good standing with its surety, was able to borrow the money to fund the contract's completion (finding 97).

Throughout the contract performance period the Corps had encouraged, sometimes directed, KRI to continue work to complete the False Pass project that the Corps had been trying to get accomplished for ten years. All the while, the Corps, knowing it had no more money to fund the contract work, also encouraged, and sometimes directed, that KRI submit REAs or claims for the extra time and extra costs KRI had continuously notified the Corps it was experiencing as a result of the continuing impacts of the Corps' post-award unilateral modification adding the IFC-5004 to the contract in 2006. When KRI submitted REAs and claims, the Corps consistently failed to respond to them in any meaningful way. Finally, 3 years after contract completion, CO Williams signed a 101-page COFD that was authored by others not involved with the contract in which the Corps denied liability for any of the impacts experienced by KRI. The Corps had gotten the False Pass project completed, at KRI's great expense, and now argues before us that it owes KRI nothing more than the original contract amount.

On the basis of the foregoing, we hold that the Corps' continued failure to address KRI's many attempts to resolve the funding issues and related impacts to KRI's performance of the contract work constituted a continuing breach of the Corps' implied duty of good faith and fair dealing. KRI has met its burden of proof of elements 2 and 3 of its claims for breach of the Corps' implied duty of good faith and fair dealing. We now turn to the fourth element of damages.

C. Damages

Having found that KRI has met its burden of proving elements 1-3 of breach of contract, we now turn our attention to the fourth element of damages.

The RESTATEMENT (SECOND) OF CONTRACTS § 344 (1981), sets forth the pertinent principles underlying the judicial remedies for breach of contract:

Judicial remedies under the rules stated in this Restatement serve to protect one or more of the following interests of a promisee:

(a) his "expectation interest," which is his interest in having the benefit of his bargain by being put in as good a position as he would have been in had the [breach never occurred],

(b) his "reliance interest," which is his interest in being reimbursed for loss caused by reliance on the contract

by being put in as good a position as he would have been in had the contract not been made, or

(c) his “restitution interest,” which is his interest in having restored to him any benefit that he has conferred on the other party.

CI², Inc., ASBCA No. 59948, 16-1 BCA ¶ 36,410 at 177,533. Each of these remedies is designed to make the non-breaching party whole; the one most appropriate to the circumstances is to be applied.

KRI claims that:

Thus, impacts from the Government breach were immediate, from and after the April 3, 2006 Partnering Meeting. The impacts were substantial, necessitating a major revision and reduction of KRI’s original work plan. And the impacts were continuing, spilling over into the 2007 construction season and severely impairing construction operations all that season due to the uncertainty of further funding, the potential for termination, which meant that the hold back reserve had to be maintained; and residual effects spilled over into 2008 because of the substantial (63%) amount of work that still remained to be done, and because of the armor rock supply issues which trace directly back to 2006.

(App. br. at 117) As a result, KRI claims damages: (a) for the period from contract start through 9 January 2007 in the amount of \$5,808,719.19 using Termination Settlement pricing; and, (b) for the period from 10 January 2007 through contract completion in the amount of \$19,326,328.55 using restitution pricing (findings 102, 107). In the alternative, KRI argues that the damages to which it is entitled should be calculated using the modified total cost methodology as requested by the Corps, recommended by DCAA and agreed to by the parties (findings 106, 108).

There was no termination of KRI’s contract and there is therefore no basis for using termination settlement principles in the calculation of breach damages. KRI’s use of restitution pricing in its calculation of damages claims that the value to the Corps of the False Pass project should be based on the contract prices for other allegedly similar projects which were awarded by the Corps in 2008-2009 (SR4, tab 3 at 77-101). We find KRI’s arguments in this regard to be based on speculation which is not an appropriate basis for the calculation of damages under the circumstances before us here. We do, however, find KRI’s un rebutted evidence of the escalation in the costs of various

components of the performance of the allegedly similar projects to be credible evidence which corroborates KRI's evidence of its own actual increased costs.

Under the circumstances presented in this appeal, we believe expectation interest principles to be the most appropriate method of calculating a remedy to provide KRI with the benefit of the bargain it made in the contract as advertised, bid and awarded. *Teresa A. McVicker, P.C.*, ASBCA Nos. 57487, 57653, 12-2 BCA ¶ 35,127 at 172,465 (citing *Anchor Savings Bank, FSB v. United States*, 597 F.3d 1356, 1362 (Fed. Cir. 2010)).

With respect to the measurement of expectancy damages, the RESTATEMENT (SECOND) OF CONTRACTS § 347 (1981) provides as follows:

Subject to the limitations stated in §§ 350-53, the injured party has a right to damages based on his expectation interest as measured by

- (a) the loss in the value to him of the other party's performance caused by its failure or deficiency, plus
- (b) any other loss, including incidental or consequential loss, caused by the breach, less
- (c) any cost or other loss that he has avoided by not having to perform.

CI², 16-1 BCA ¶ 36,410 at 177,533 (emphasis omitted). Proof of breach damages requires that: (1) the damages were reasonably foreseeable by the Corps at the time of contracting; (2) the damages were caused by the Corps' breaches of contract; and (3) KRI has supported the damages with reasonable certainty. *Yankee Atomic Elec. Co. v. United States*, 536 F.3d 1268, 1273 (Fed. Cir. 2008).

We have found that the Corps was well aware at the time it awarded the contract that the change in funding clauses made mandatory by the E&WDA would likely result in increased time and/or costs to perform existing continuing contracts. Nevertheless, the Corps made the conscious decision to advertise, accept bids and award the False Pass contract with the CCC-5001, knowing that the clause would have to be replaced by the IFC-5004 after award. When the Corps unilaterally replaced the CCC-5001 with the IFC-5004, it breached the contract. When the Corps time and again failed to address KRI's repeated notifications of incurrence of increased costs throughout performance of the contract, all the while directing that KRI complete the contract, it breached its implied duty of good faith and fair dealing, as well as its

express duties under the Changes and Disputes clauses. The incurrence of damages in the form of increased performance time and increased costs resulting from the Corps' breaches of contract was therefore clearly foreseeable by the Corps at the time it awarded the contract. The False Pass project was the only large project performed by KRI at all times relevant to the matters before us and there is no credible evidence in the voluminous record before us that the costs claimed by KRI were not incurred in performance of the False Pass project. We are satisfied that any costs incurred by KRI in performance of the False Pass project which were not caused by the Corps' breaches of contract have been removed from its claimed damages. We have found that the record supports KRI's appropriately adjusted first and second MTC pricing submissions as credible presentations of the increased costs, incurred by KRI as a result of the Corps' breaches (finding 110).

KRI's various REA and claim submissions all start with the total booked direct costs incurred by KRI on this project. DCAA audited nearly all of those costs and, with very few exceptions, found them to have been supported as incurred. To the extent the DCAA audit credibly questioned certain claimed costs for reasons other than unauthorized entitlement determinations, we are satisfied that KRI has removed them from its amended claim calculations. The Corps' own expert witness, Mr. Cotton, agreed that KRI's documentation supported its calculations in its various updated claim pricing submissions. Mr. Cotton also opined that \$2,100,000 of KRI's updated claimed total costs had not been audited by DCAA and, therefore, should not be considered. (Tr. 10/166-67, 182-85, 202-06) It is not a requirement of KRI's burden of proof that costs supported by it to the Corps have been audited, particularly when it is the Corps' decision alone whether or not to request an audit or supplemental audit. The failure of the Corps to request an audit of the claimed incurred job costs, or any portion of them, is certainly not dispositive of whether those costs have been incurred. It is well established that the "preferred" method of proving a claim is by 'actual cost method.'" *Systems San Francisco Ship Repair*, ASBCA No. 58809, 16-1 BCA ¶ 36,226 at 176,734. Audited or not, we have found KRI's claimed job costs to be supported in the record and to be credible presentations of actual job costs (finding 110).

After due consideration of the voluminous record before us, including documentary, testimonial and expert witness evidence from both parties, we find KRI to be entitled to the following damages resulting from the Corps breaches of contract:

Total booked direct costs	\$34,970,152
-Plus later-identified costs not booked	16,532
-Less reduction in demobilization	-612,296
-Less unallowable costs	-87,987

-Less other costs disallowed by DCAA	-137,367
-Less costs "that are not, or might not be, the responsibility" of the Corps	-3,915,062
Total adjusted direct costs	\$30,233,972
-Plus G&A (11.383%)	3,441,533
Subtotal	\$ 33,675,505
-Plus profit (10%)	3,367,550
Subtotal	\$ 37,043,055
-Less amount paid by the Corps under the contract	-19,445,279
Subtotal	\$ 17,597,776
-Plus cost of KRI's borrowing to comply with CO direction to complete the project while at the same time refusing to discuss KRI's claimed monetary impacts	\$3,052,477
Total	\$20,650,253

(SR4, tab 5 at 68-70, tab 19 at 1175-81, tab 182 at 50-51)

The Corps argues that the cost of borrowing in KRI's claim is expressly unallowable because it is interest, however, under the circumstances now before us, the cost of borrowing the funds to complete the Corps' project as directed was a direct result of the Corps' breaches of contract and a business expense not reasonably foreseeable by KRI at the time the contract was awarded and the parties' bargain was struck. The Court of Appeals for the Federal Circuit has agreed that:

[W]hile interest on a claim is not recoverable, interest *as* a claim should be.

....

Such an award is not one of interest, but a direct consequence of the breach. Proper circumstances for award in that case was debt that is "directly traceable [and] clearly in connection with" the Government's breach.

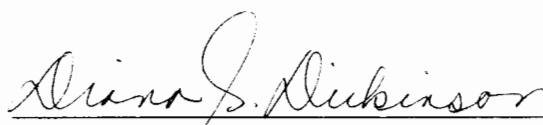
Arizona Public Service Co. v. United States, 93 Fed. Cl. 384, 394 (2010) (citation omitted). KRI argues in its reply brief that the total amount of the expense is now larger than the amount it previously claimed and further states a daily rate to use in

calculation of the amount up to the date of payment to KRI (app. reply br. at 40-41). While we are mindful that such an expense is, in fact, a continuing expense, the record has been closed since the end of the hearing in this matter and we decline to award an amount larger than the one contained in KRI's claim which we have held is supported by record documentation. Likewise, KRI's claims included estimated additional bond expense which we do not include in our calculation of breach damages because the actual amount is unknown and not supported in the record before us.

CONCLUSION

We sustain the appeal in the amount of \$20,650,253, plus CDA interest pursuant to 41 U.S.C. § 7109 calculated from 24 November 2009 until paid.

Dated: 5 December 2017



DIANA S. DICKINSON
Administrative Judge
Armed Services Board
of Contract Appeals

I concur



RICHARD SHACKLEFORD
Administrative Judge
Acting Chairman
Armed Services Board
of Contract Appeals

I concur



OWEN C. WILSON
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. 57168, Appeal of Kelly-Ryan, Inc., rendered in conformance with the Board's Charter.

Dated:

JEFFREY D. GARDIN
Recorder, Armed Services
Board of Contract Appeals