ARMED SERVICES BOARD OF CONTRACT APPEALS

Appeal of --	)	
	)	
Black River Limited Partnership	)	ASBCA No. 51754
	)	
Under Contract No. DACA87-86-C-0059	)	

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OPINION BY ADMINISTRATIVE JUDGE LIPMAN

INTRODUCTION

This appeal concerns the captioned fixed-price contract to finance, design, construct, permit and operate a high-temperature-water (HTW) and co-generation facility at the Fort Drum Army Base in Watertown, New York. The contract included a tax adjustment clause intended to adjust the amount of the monthly Capacity Charge paid to appellant under the contract in the event of changes in tax legislation. Upon the passage of the federal Tax Reform Act of Act of 1986 (TRA), the parties negotiated a contract modification to increase the amount of the monthly Capacity Charge.

In our earlier proceedings limited to consideration of legal entitlement, ASBCA No. 46790 was an appeal from a contracting officer's decision rescinding the contract modification on the grounds that the adjustment was not authorized by the tax adjustment clause and that appellant's request for a tax adjustment had not been accompanied by all current cost or pricing data as required by the Truth in Negotiations Act, 10 U.S.C. § 2306a (TINA). ASBCA No. 47020 was an appeal from the contracting officer's deemed denial of appellant's claim for an increase of $814,133 in the monthly Capacity Charge, the amount by which the contracting officer had reduced the Capacity Charge, plus future adjustments based on the producer price index.

In our original decision (97-2 BCA ¶ 29,077), we concluded that, although the date of contract award, despite the contrary intent of the parties, followed the passage of the TRA, contract reformation was appropriate so that the tax adjustment clause apply to the tax law changes in the TRA, thereby entitling appellant to an increase in the monthly Capacity Charge. We also concluded, however, that data submitted by appellant in support of its tax adjustment request, which resulted in the contract modification increasing the Capacity Charge, was not current, complete and accurate, as required by TINA, and thereby entitled the Government to a price adjustment under the contract.

This appeal results from the parties' inability to agree upon the appropriate Capacity Charge increase by application of our earlier decision. The record consists of the documentary evidence as well as the transcripts of the total of 14 days of hearing conducted in both proceedings.[*] The findings of fact below, for the most part, either summarize or supplement the fact-finding in our original decision; we specifically identify where we depart from the original findings based on evidence in this proceeding.

FINDINGS OF FACT

1. On 12 July 1985, the Government, by the Army Corps of Engineers (Army or COE), Huntsville Division, issued a request for proposals (RFP) for a contractor-owned, contractor-operated production plant to provide HTW to serve energy needs at Fort Drum. The RFP solicited two project options, with offerors permitted to submit proposals for either or both options: (a) a plant generating HTW for sale, or (b) a plant cogenerating HTW and electricity for sale. The RFP placed upon the contractor the sole responsibility for the means necessary to provide a facility which conformed to the performance and functional requirements of the contract. In addition to construction, the contractor was responsible for designing, obtaining necessary permits, and financing the project. The RFP required the contractor to provide initial HTW service 23 months from the date of the notice to proceed and to provide full HTW service 35 months from the date of the notice to proceed. Under the contract, the Army would compensate the contractor its capital and operating costs for designing, constructing, permitting, financing and operating the HTW facility, as well as the contractor's return on investment, by a monthly Capacity Charge and a monthly Fuel Charge. Those payments were to be fixed pursuant to the competitive award process and by the terms of the contract, and were to be subject to adjustment under the

[*] Citation references to our earlier proceedings (ASBCA Nos. 46790, 47020) begin with an "E."

contract only for changes in the producer price index, changes in emission standards, or for changes in federal, state or local taxes, as set forth in more detail below. (E-R4, tab C; E-AR4, tab 4)

2. The RFP required proposals to include a financial plan, including factors such as capital cost, energy production data, annual operating revenues and expenses of the facility, insurance and taxes. It included financial qualifications and arrangements (*e.g.*, equity contribution) among the evaluation criteria. The RFP included clause H.9, entitled TAX ADJUSTMENT, which provided for an adjustment in the charges to the Government in the event of changes in federal, state or local taxes. At an August 1985 pre-proposal conference, the Army advised that the clause did not cover taxes on income and offered no protection for changes in legislation regarding investment tax credits or accelerated depreciation. (E-AR4, tabs 4, 6)

3. Prior to receiving award of the contract, appellant's predecessor was J.A. Jones Construction Company (Jones). Appellant, Black River, is a limited partnership organized by Jones for the sole purpose of performing the captioned contract and to which the contract was novated by contract modification following award. (E-AR4, tabs 41, 186; R4, tab 547-4; E-ex. A-79; E-tr. 1/56-57)

4. In the 1985-86 time period, Major General James L. Kelly, retired from the COE, was a special assistant to Jones' president, Mr. Johnny Jones, with responsibility for evaluating new business opportunities. In 1985, Mr. Paul Johnson, then Deputy Assistant Secretary of the Army, invited General Kelly to a briefing on the Army's plans to privatize Fort Drum. Congress thereafter decided to privatize only the Fort Drum heating plant and adopted plans to privatize up to 18 other heating plants. (Tr. 1/39-44)

5. Jones' proposal for this contract represented that it had demonstrated the ability to raise substantial capital in prior project financing (R4, tab 5, pp. 2.2-1, 2.2-2). Prior to 1985, Jones' primary experience had been as a builder, as opposed to being a developer, equity investor or having experience in raising long-term debt and equity capital (tr. 1/44, 58-59). General Kelly was involved in helping the Jones management to identify the risks associated with Jones' participation in the HTW project. He considered that the 23-month schedule requirement was among the risks in view of the Jones' responsibility for designing, permitting and financing the project, in addition to limitations in the construction season in the Fort Drum area. (E-R4, tab W; tr. 1/46-50, 60, 2/13-14) However, the risk of the tight schedule was tempered by the historical rarity of COE exercising its power to terminate contracts for default (tr. 1/76). Other potential risks included the possibility of a convenience termination and the unpredictability of the Government's annual appropriations process (tr. 1/63-64, 145-46)

6. Jones' engineering subcontractor was to be the Duke Power Company (Duke Power). Duke Power and its successor, Duke Energy Co. (Duke Energy) was also a General Equity Partner in the HTW project with a 10 percent interest. The basic technology

included in Jones' proposal, a fluidized bed boiler, was well developed by that time. Jones proposed a circulating fluid bed able to burn coal and wood chips, as required by the Army, with environmental benefits; it was "second generation" technology only recently developed in Europe. It was commercially acceptable, but it was relatively new and had been employed only in small-scale "test bed" contexts in the United States and had never been used in Europe with coal. (E-R4, tab W; E-tr. 2/22-23, 8/194; E-Ex. G-4 at 3; R4, tab 5 at 2.2-1; tr. 1/51-53, 89, 2/9-15) Duke Power had not previously designed that form of co-generation facility (E-R4, tab 102).

7. While the RFP contemplated the use of anthracite coal, which is cleaner and has a higher Btu per pound content than bituminous coal, Jones proposed using bituminous coal which was less expensive to burn (E-tr. 3/83, 87-88; tr. 3/100).

8. The proposed plant was a co-generating facility, generating HTW for sale to the Army and electricity for sale to the Niagara Mohawk Power Corporation (NIMO). Revenues from the sale of electricity were anticipated to be the major portion (approximately 70 percent) of the plant's total revenues. Jones did not have a contract with NIMO when it submitted its proposal but, under the Public Utilities Regulatory Practices Act (PURPA) as well as under a New York statute, utilities such as NIMO were required to pay a minimum of six cents per kilowatt hour for electricity purchased from qualifying facilities; under its proposed contract with the Army, Jones would be a qualifying facility under the statutes. Jones was seeking, and ultimately obtained, a contractually protected floor of six cents even if the New York law were to change, but at the time of its proposal it did not know whether the New York Public Utilities Commission would approve a contract in that form. In its best and final offer (BAFO), Jones projected that electric prices would increase above six cents by 1993 and would further increase to 15 cents by the end of the contract term. Duke Power anticipated a "very healthy return," with an internal rate of return (IRR) of 31 to 32 percent even with a constant price of six cents. In fact, after 1986 electric prices decreased and appellant never received more than the six cents contractual minimum. (R4, tab 18; exs. A-208, G-15; E-tr. 5/10-14; tr. 1/53-55, 2/15-16)

9. On 23 October 1985, Mr. William Garnett, Jones' Treasurer, prepared a memorandum, referencing "Pricing Risk Assumptions," which was stated "to summarize the risk and assumptions being used in developing the bid . . . to be used as an internal document to secure necessary approval prior to the final bidding for the project." It included the following with respect to "Return on Investment Criteria:"

> We will establish a minimum cash on cash return of 15% on the equity investment of the owners of the Ft. Drum steam facility. This return would be measured over the initial five year operation of the plant. The total 25 year term to include the fair market residual value of the plant would have a higher return. We will look to our financial advisor to carefully

> structure this segment of our proposal and the tax benefit pass through.

(E-R4, tab B, ex. 5)

10. On 26 November 1985, Mr. Garnett prepared a revised memorandum which included the following revised sentence in reference to "Return on Investment Criteria:"

> The total 25 year term to include the fair market residual value of the plant would have at [sic] a higher return of approximately 21%.

(E-R4, tab B, ex. 6)

11. As part of the preparation of its proposal, Jones prepared pro formas, which are computer pricing models consisting of spreadsheets which record certain business assumptions for a project and, based upon the assumptions, the expected cash flow. Jones' pro formas dated 3 December 1985 and 6 December 1985 indicated an after-tax internal rate of return of 53 percent for the entire projected period of the contract. The pro formas also included a calculation showing a 15 percent "Internal Rate Return Cash on Cash," which constituted an internal rate of return on pre-tax cash flow for the first five years of the contract. Jones' proposal of 6 December 1985 did not include the 15 percent calculation. The 6 December 1985 proposal stated that the company had "arranged for the utilization of its financial advisor The First Boston Corporation of New York City (First Boston), to assist in the financing arrangements of this project if [Jones] should be selected to develop the project." At that point, Jones had not retained First Boston to assist it in developing either its initial proposal or its BAFO and had had only preliminary discussions with First Boston as to whether an acceptable financing structure could be developed. (E-R4, tabs E, F, G-1; R4, tabs 5, 501-03; tr. 1/58)

12. Jones' 6 December 1985 proposal contained a finance plan which, while stating that in view of the uncertainty regarding tax issues it could not determine the optimum form of financing, included a pro forma which assumed a 12-year debt repayment schedule and $10 million in equity. The proposal also indicated that it was premised on Jones' ability to take advantage of the tax benefits existing at that time, which included the investment tax credit and the ability to accelerate depreciation. (E-R4, tab 11 at §§ 2.2.3.1.1 and 2.6.1)

13. During negotiations in February 1986, Jones learned that the Army would be amending the RFP's tax adjustment clause and requesting best and final offers. Jones advised the Army that its proposal contained tax assumptions and that its proposal would have been as much as 30 percent higher had it bid assuming the applicability of the proposed tax law changes. (R4, tab B, ex. 8)

14. Because Jones realized that it had only limited experience in raising long-term equity and investment capital, it retained First Boston as its financial advisor for the project. First Boston's fee was premised upon Jones' success in receiving award of the project. First Boston's Project Finance Group personnel assigned to the HTW project were Mr. John Stevenson, the most junior member of the team having recently graduated from college, Mr. Dan Moore, and Mr. Tarlton Long. All were important to providing Jones with the required service in the project. Jones provided First Boston with all necessary technical information, including estimated construction and operating costs, the construction schedule and the projected HTW and electric revenues. (Tr. 1/59, 99-102, 182-83) Mr. Stevenson was the First Boston person responsible for preparing the pro formas and for their updating throughout the project (tr. 1/111, 119). In submitting pro formas to Jones, First Boston did not attach all of its work papers, although at some point Jones would have seen them (tr. 1/121).

15. First Boston believed that the project Jones had bid in its initial proposal could not be financed because (a) the assumed debt coverage ratio (cash available as generated by the project divided by the required principal and interest repayments) was too low to provide the cushion needed to attract debt capital and (b) the internal rate of return assumed for equity was too low to attract the needed equity capital. First Boston believed that the net after-tax rate of return on investment required to attract equity to a project with the risks presented by the HTW project was in the range of 30 percent or higher. (Tr. 1/104-08, 115, 123, 133, 164)

16. On 3 March 1986, the Army issued its Amendment No. AM00006 to the RFP revising the TAX ADJUSTMENT clause. Jones' asked its tax counsel, Mr. Mark Regante, then of the firm of Milbank, Tweed, Hadley & McCloy (Milbank, Tweed) to review the language of the amended clause. He did so, and advised Jones that the amended clause did not offer protection for the tax changes that were then under consideration by Congress. (E-R4, tab B, ex. 11; E-tr. 1/87-89)

17. As part of its effort to serve Jones by evaluating the financial assumptions, First Boston created pro formas. On 5 March 1986, First Boston provided Jones with three pro formas identifying different scenarios. The first was an attempt "to solve for the financing scenario which produced [the] lowest HTW [price] under the [then existing] tax law." That model specified a 70/30 debt-to-equity ratio, a debt coverage ratio of 1.5 and an after-tax IRR of 33.2 percent. The second scenario attempted to solve for the lowest HTW price under the "proposed" tax law. It specified an 80/20 debt-to-equity ratio, a debt coverage ratio of 1.5 and an IRR of 28.6 percent. The third scenario was one in which only equity capital was to be used under the "proposed" tax law, and it indicated an IRR of 15.7 percent. Each of the pro formas included a computation based on an "after tax NPV [net present value] @ 15%." First Boston intended its assumptions to be "aggressive," designed to produce the lowest HTW price, including the lowest debt coverage ratio and an IRR which could still attract the required debt and equity capital. (R4, tab 504; tr. 1/111-14, 122-23)

18. On 10 March 1986, First Boston refined and re-ran the models. This version, too, had a 70/30 debt-to-equity ratio, a debt coverage of 1.5 or above and an after-tax IRR above 30 percent. It also contained the NPV calculation described above. (R4, tab 505; tr. 1/122-23).

19. In a telephone conversation on 12 March 1986, a First Boston official advised Jones' Mr. Garnett that the TAX ADJUSTMENT clause in the RFP Amendment No. AM0006 appeared not to give Jones adequate protection from possible tax changes in the areas of depreciation and the possible loss or delay of tax credits; he advised that Jones properly qualify its BAFO (E-R4, tab XXX, ex. 3).

20. On 13 March 1986, First Boston made final refinements to the pro forma model prior to its BAFO and produced a final pre-BAFO run. It included a monthly Capacity Charge of $637,410.50 and a monthly Fuel Charge of $4.10 per MBTU, and reflected a "Total Project IRR" of 37.4 percent and an NPV at a 15 percent discount rate of $21.7 million. (R4, tab 506)

21. While completing its BAFO pricing proposal, Jones' computer system in Charlotte, North Carolina, crashed. Prior to submitting the BAFO, however, Jones' Mr. Garnett added an additional $10,000 to the $637,401.50 figure First Boston had generated on its computer, increasing Jones' proposed monthly Capacity Charge to $647,410.50. (E-tr. 4/133-34; tr. 1/124)

22. With the exception of that last minute change, the 13 March 1986 First Boston pro forma (First Boston Pro Forma) reflected the Jones' assumptions underlying its BAFO. First Boston did not preserve an electronic copy of the pro forma. It was its practice to continually update and modify the last pro forma to avoid the risk of discrepancies between and among pro formas. (Tr. 1/123-26)

23. Jones' BAFO price contained no contingency for potential increases due to tax legislation (E-tr. 3/80-81). Its 13 March 1986 BAFO cover letter did not express continuing reservations about the language of the Tax Adjustment clause in Amendment No. AM0006 to the RFP, but stated that Jones "interpret[s] your revised paragraph to be responsive to our concerns in that the Army will adjust their payments should a change in the tax laws adversely affect the tax credits, depreciation and the projected income stream." Jones did not consider that its BAFO cover letter had withdrawn the tax qualifications it had expressed in its initial proposal. (E-R4, tab B, ex. 34; E-tr. 3/99)

24. On 25 April 1986, the Army notified Jones of its selection as the successful offeror (E-AR4, tab 19). By letter of 2 May 1986, Jones advised the Army that it was proceeding to finalize arrangements regarding the sale of power, debt financing and equity participation (E-AR4, tab 20).

25. On 2 May 1986, Jones met with First Boston and its attorneys from Milbank, Tweed, including Mr. Jay Worenklein, then a partner with the firm. Jones' General Kelly's contemporaneous notes reflect that the attendees discussed the timing of the change from J. A. Jones Construction Company to a special purpose corporation, Jones Black River Services, Inc. The notes also indicate that Mr. Worenklein was to effectuate the change and General Kelly's notes state that "Jay will put together the bait & switch structure." Following the meeting, Mr. Worenklein in fact drafted the contract language concerning the switch to a special purpose corporation. General Kelly testified that he used the phrase "bait & switch" as a memory device, that he had a poor recollection of legal terms, and that he did not use the term with reference to any other matter on this project and had incorrectly used it in that instance especially in view of the fact that Jones has already informed the Army of the planned change. (E-R4, tab B, ex. 15; tr. 1/67-68) We so find.

26. On 12 May 1986, Jones' Mr. Garnett provided the Jones Project Finance Committee with pro formas prepared by First Boston. The pro formas presented different scenarios and evaluated different debt financing alternatives, leasing and possible equity investments. Mr. Garnett's cover memorandum included the following:

> The cases also provide for a partner providing a 70-75% cash equity in exchange for 50% of the cash flow. This our first effort on an unbalanced percentage for the ownership interest being other than the actual cash contributions on a one-for-one basis.

All of the cases show an IRR in excess of 30 percent (other than the lease case, which shows no IRR), and all included an after-tax NPV calculation at 15 percent. (R4, tab 7)

27. Shortly after Jones' notification that it was the successful bidder, it held an internal meeting on 22 May 1986 at which various financing plans were presented by First Boston. Among the plans presented were the "pro rata input of equity" or, in the alternative, 100 percent construction financing with no cash input of equity during construction. The meeting agenda included the following:

> Achieve returns suitable for risks undertaken.
> Completion commitment: Project profits
> Equity investment: 15% unleveraged, after tax
> 25-30% leveraged, after tax

The presentation included two sets of pro formas dated 21 May 1986, both of which assumed partner participation. In Case 1, under the old tax law, with no increase in the Capacity Charge, First Boston derived an IRR of 33.2 percent and an NPV at 15 percent of \$23.3 million. In Case 2, under the proposed new tax law, with a 25 percent increase in the

Capacity Charge and Fuel Charge, First Boston derived an IRR of 32 percent and an NPV at 15 percent of $31.6 million. (E-R4, tab U)

28. On 3 June 1986, Jones' Mr. Garnett sent a memorandum to Jones' president containing a risk analysis of the project. Among the risks indicated were adverse financial conditions of Jones through mid-year 1986 requiring its parent guarantee, a reduction in potential cash flow due to possible decreases in electric rates and plant thermal efficiency, and cost increases including those for bituminous coal, delayed start-up and capital costs for the physical plant. The projected project returns included a $5.1 million fee for the $62.3 million construction project, a $1 million developer fee, and $3 million per year for operation and maintenance in addition to equity return. Another advantage indicated was Jones' opportunity to "obtain [the] first major privatized power project in [a] new multi-billion dollar growth market with [a] structure that could be reproduced by Jones." (E-R4, tab B, ex. 18)

29. Following award, Jones advised the Army that potential lenders in the project were not comfortable with the wording of the TAX ADJUSTMENT clause and, following exchanges of drafts and negotiations between counsel for the parties, the following TAX ADJUSTMENT clause was incorporated into the contract:

> The rate provided herein includes no allowance for any changes in federal, state or local taxes by reason of any changes in the tax laws of the United States, the State of New York or any political subdivision or instrumentality of the State of New York which may be imposed after the date of contract award. In the event of any amendment of the tax laws of the United States, the State of New York or any political subdivision or instrumentality of the State of New York enacted after the date hereof that has the effect of increasing or reducing the net after-tax rate of return on investment of the Contractor (or if the Contractor is a partnership, its partners) assumed by the Contractor in computing the rate set forth herein, the Capacity Charge shall be adjusted, upward or downward as the case may be, to that amount which shall preserve such net after-tax rate of return on investment, recomputed by taking into account the effect of such tax law amendment and all prior amendments for which an adjustment to the Capacity Charge has been made.

(E-R4, tab C; E-tr. 2/222) The clause included in the contract, which incorporated Government comments, was drafted by Milbank, Tweed's Mr. Regante, whose intent was that the phrase "after-tax rate of return on investment" referred to the project's IRR and considered the terms IRR and "rate of return on investment" to be synonymous. (E-R4, tab B, ex. 19; E-tr. 1/96-97, 133-34)

30. The parties signed the contract in June 1986. The contract later received required Congressional approval, and the Army ultimately issued a notice to proceed (E-AR4, tabs 129-39; E-tr. 3/116). On 18 June 1986, the date Jones signed the contract, First Boston produced a pro forma model run labeled "Base Case [for] Army Bid" which reflected an after tax total project IRR of 33.2 percent; it also contained the words "after tax NPV @ 15%." (R4, tab 515; tr. 1/135-36)

31. On 31 July 1986, Mr. Garnett sent appellant's president an updated risk analysis which, among other things, indicated: (a) that the tax law would change "requiring use of indemnification provisions of Army contract which must work to keep very high return"; (b) that the fluidized boiler technology risk appeared to be "minimal"; (c) that, under the proposed new tax law, repayment of equity could be in two years; (d) that Jones could realize "returns of up to 43% on investment"; and, (e) that the "potential pretax cash flow available to Jones for a 50% participation could be $300 million in first 20 years of operation . . . in addition to construction profit, developer fee and O&M company profit." (E-R4, tab B, ex. 20)

32. On 18 September 1986, First Boston's Mr. Stevenson faxed to appellant's Mr. Garnett a draft Descriptive Memorandum for the "$93,000,000 Project Loan and Credit Facility for the Fort Drum Cogeneration Project." The purpose of the Descriptive Memorandum was to provide prospective participants with pertinent information to make an informed decision as to participation in the project. It contained three detailed pro formas dated 18 September 1986 identified as "Base Case (Old Law)," "Sensitivity Case 1 New Law Equity in Year 3," and "Sensitivity Case 2 New Law BAFO Plus 30%." The three sets of pro formas attached to the draft contained no IRR calculations, but included NPV calculations at a 20 percent discount rate, as follows: Base Case - NPV @ 20% = $15.9 million; Sensitivity Case 1 - NPV @ 20% = $9.8 million; Sensitivity Case 2 - NPV @ 20% = $18.7 million. The Descriptive Memorandum describes Sensitivity Case 2 as follows:

> This case assumes the expected changes in tax law as outlined in Sensitivity One. In this case, however, HTW prices were increased by 30% to reflect the indemnification against changes in tax law which the Army has agreed to provide the Project's owners. The figure of 30% was discussed with the Army in a preliminary conceptual discussion held in the Spring of 1986. The actual HTW price increase which is still to be negotiated with the Army may turn out to be either higher or lower.

(E-R4, tab Y)

33. In September 1986, First Boston, on behalf of Jones, issued the Descriptive Memorandum. Although it was provided to prospective debt and equity investors, it was prepared primarily for prospective lenders and, therefore, it contained neither IRR nor NPV

calculations, which were not considered relevant. However, a potential investor could perform its own calculations of NPV at whatever discount rate selected using the net after-tax cash flow line of each pro forma. (E-R4, tab AA; tr. 1/37, 131, 137, 148-49)

34. By letter of 29 September 1986, First Boston's Mr. Stevenson sent a letter to Duke Power, Jones' subcontractor and a potential equity investor, addressing some concerns expressed by Duke Power regarding the equity rates of return in the HTW project. Mr. Stevenson advised of difficulties in calculating a single IRR where there are multiple cash flow "sign changes" (inflows and outflows), a problem which was said to exist in the "Base Case" pro forma accompanying the Descriptive Memorandum. (R4, tab 19)

35. On 6 October 1986, Duke Power prepared an internal memorandum (a) discussing a document from First Boston setting forth the proposed terms for Duke Power's partnership on the HTW project, and (b) recommending that Duke Power make an equity investment in the project. The memorandum states that, although the First Boston analyses contained a "base case" reflecting projected cash flows under the then-current tax law, the memorandum was limited to two analyses under the proposed tax law changes. Under the new tax law, with no change in the Capacity Charge under the TAX ADJUSTMENT clause (case one), the memorandum projected an after-tax IRR of 27.7 percent to an "equal partner." Under the new tax law, with a 30 percent increase in the total HTW price (case two), the memorandum projected an after-tax IRR of 36.8 percent to an "equal partner." (The rates for a "limited partner" were 21.5 percent and 27.3 percent, respectively). It also included an NPV calculation, with no elaboration in the text, of NPV @ 20% = $9.8 million for case one and NPV @ 20% = $18.8 million for case two. (Ex. A-208)

36. In anticipation of the tax reform legislation, First Boston's Mr. Stevenson sent Jones a memorandum dated 2 October 1986 which indicated three different IRR rates which could be presented to the Army as a basis for a tax adjustment. Those rates were (a) 17 percent (stated to be average cost of capital of the project), requiring an 8.3 percent Capacity Charge increase, (b) 33 percent, requiring a 37 percent Capacity Charge increase, and (c) 44 percent, which Mr. Stevenson called "the current expected IRR," requiring a 52.7 percent Capacity Charge increase. Mr. Stevenson wrote that "33% makes the most sense because it was the number we used to originally bid the Army" and that "the Army contract specifically states the owners' after tax rate of return should be made whole rather than the average cost of capital." Mr. Stevenson considered that the full impact of the tax change was borne by equity investors and that preserving the weighted average cost of capital would ascribe some of the impact of the tax changes to debt lenders who received their payments from pre-tax dollars. Mr. Stevenson also believed that the 44 percent rate, although the currently expected IRR, should not be used because it reflected the "improvement" to the project which had been realized in the months subsequent to the Jones bid. (R4, tab 529; tr. 1/153-54, 184-85)

37. In a memorandum dated 3 October 1986 to Jones, First Boston's Mr. Stevenson set forth three cases with the same IRR rates as in his 2 October 1986

memorandum, but stated that he had corrected a depreciation schedule which altered the required Capacity Charge increases for the three IRR rates to 11.5 percent, 46.3 percent and 66.3 percent, respectively (R4, tab 530).

38. On 22 October 1986, the Tax Reform Act of 1986 (TRA) became law. Among other things, it (a) reduced the corporate income tax rate from 46 percent to 34 percent, (b) eliminated the availability of the investment tax credit, and (c) reduced the rate of accelerated depreciation with an impact upon the HTW project causing (i) the 10 percent of the facility previously recovered over 19 years be recovered over 31.5 years using the straight line depreciation method, and (ii) that the 90 percent of the facility previously qualifying for the five-year ACRS life be recovered using a 20-year ACRS life and the 150 percent declining balance/switch to straight line method (E-R4, tab 173 at SW00000009).

39. In a 22 October 1986 meeting, First Boston advised the Army that, since a typical project of this nature produced a return on equity of 25 to 45 percent, First Boston had recommended, and Jones had incorporated, a 33 percent rate of return in its BAFO. In order to compensate Jones for the impact of the TRA's tax changes, Jones stated that the Capacity Charge would have to increase by 68.8 percent, resulting in a total price increase of 48 percent. First Boston also informed the Army that appellant would accept an up-front, lump-sum payment of $8 million ($14 million pre-tax) in lieu of the adjustment of the Capacity Charge over the life of the contract. (E-AR4, tab 154; E-ex. A-29; E-tr. 2/232-34, 3/129-33) Following the meeting, the Army advised Jones that its request for a tax adjustment would have to include an explanation of how Jones had calculated the original Capacity Charge upon which contract award had been made (E-tr. 3/142).

40. Because of the substantial potential increase in the Capacity Charge and contract price, the Army considered terminating the contract for its own convenience. However, it did not take that action because of the potential delay in HTW delivery to Ft. Drum. On 10 November 1986, the Army issued the notice to proceed. (E-R4, tab 31; E-AR4, tab 157; E-tr. 2/313-14)

41. On 18 November 1986, First Boston sent a memorandum with "economic projections" to Jones. Based on certain assumptions, it indicated that a 50 percent increase in the HTW price, comprised of the Capacity and Fuel Charges, would yield a total project IRR of 52 percent and that a zero increase in the HTW price would result in an IRR of 31.2 percent. It also included pro formas which reflected that price increases ranging from zero to 50 percent would produce a "project cash return" ranging from 56.1 percent to 134.6 percent. (E-R4, tab DD)

42. On 21 November 1986, Jones submitted to the Army its "Request for Tax Adjustment to Capacity Charge" pursuant to the TAX ADJUSTMENT clause of the contract. It sought a 68.6 percent increase in the Capacity Charge to a new monthly charge of $1,091,463, which would result in an overall contract price increase of 48 percent. Jones further indicated (a) that the tax adjustment request was based upon the figures presented in

the 22 October 1986 meeting, (b) that there had been an error in those figures and that the accurate amount requested should be a 75.69 percent increase in the Capacity Charge, producing an overall price increase of 53 percent, but (c) that in an effort to expedite the adjustment Jones was requesting only the 68.6 percent increase. The tax adjustment request was supported by a pro forma entitled "Ft. Drum Cogeneration Facility As Bid to the Army March 13, 1986" (As Bid Pro Forma). The As Bid Pro Forma was not an actual pro forma used in preparation of the BAFO on 13 March 1986, but was prepared specifically for submission with the tax adjustment request. First Boston's Mr. Stevenson, who prepared the As Bid Pro Forma, no longer had an electronic version of a pro forma reflecting the BAFO assumptions because the pro formas had been updated. In preparing the As Bid Pro Forma, his intent was to accurately reflect the BAFO assumptions; Mr. Stevenson reversed the post-BAFO changes in the pro formas existing at around the time of the tax adjustment request until the model reflected the BAFO assumptions. (E-R4, tab B, ex. 34; tr. 1/154-57)

43. The As Bid Pro Forma reflected an IRR of 33.3 percent but, in contrast to previous pro formas including the 13 March 1986 pro forma, the As Bid Pro Forma did not contain any calculations for, or reference to, NPV. Mr. Stevenson considered that NPV calculations were not relevant because the purpose of the presentation in support of the tax adjustment request was to demonstrate what was necessary to restore the project economics to the equity investor, which was an IRR of 33 percent. (R4, tab 532; tr. 1/159-60)

44. The As Bid Pro Forma reflected (a) the inclusion of an escrow account, which was not among the Jones' BAFO assumptions, and (b) the application of a four percent escalation factor to projected limestone costs rather than the five percent factor (a labor, rather than material rate) which had been used in error in previous pro formas. (E-R4, tab B, ex. 34; R4, tab 541)

45. The Army retained Stone & Webster Engineering Company (Stone & Webster) to analyze Jones' request for a price adjustment and to determine if it was "fair and reasonable." In performing its analysis, Stone & Webster was to use the data which Jones included in its request for tax adjustment and it did not independently verify Jones' claimed IRR of 33.3 percent or other numbers alleged to be the BAFO assumptions. Stone & Webster concluded that the method used by Jones to determine the amount of the tax adjustment was reasonable and consistent with the language of the contract and the applicable provisions of the new and old tax law. As discussed in more detail in our findings below, Stone & Webster also recognized that the adjustment consisted of a "severe increase" in the cost to the Government and observed that some of that increase could be avoided, without reducing Jones' return on investment, if the parties could agree upon a lump sum payment, or even an accelerated payment over five years, rather than an increase in the capacity charge over the life of the contract. (E-AR4, tabs 170, 173; E-tr. 2/48-49, 90-91)

46. The Government did not audit Jones' tax adjustment request because the official approving the audit waiver considered that, pursuant to the contract, the tax adjustment was intended to restore Jones to its presumptive after tax profit regardless of its actual profit and that "the change in rates will be based on a contract formula using known objective data available to the general public." (E-R4, tab B, ex. 35)

47. In January 1987, the parties executed Modification No. P00002 (Mod 2) to the contract, increasing the monthly capacity charge to $1,091,463 and Jones signed a Certificate of Current Cost and Pricing Data with respect to the data provided in support of Mod 2. (E-R4, tab B, exs. 39, 41)

48. Beginning in early 1987, some Government officials became interested in the reasons for the substantial increase in the cost of the contract as a result of the TRA and Mod 2. They began an effort to persuade appellant to voluntarily renegotiate the tax adjustment permitting a payment which would be more favorable to the Government. (E-AR4, tabs 193-202; E-tr. 2/70-74, 325-26)

49. By letter dated 12 March 1987, First Boston provided appellant with information regarding the possible refinancing of the project debt or equity. Among other things, First Boston raised the possibility of refinancing the project equity so that appellant had no cash investment in the project, which could cause the internal rate of return to "go off the screen and become meaningless." (E-R4, tab SS)

50. In July 1987, First Boston issued a Direct Placement Memorandum for the refinancing of the project. The refinancing provided for no equity contribution, contained NPV calculations at 15 percent, and included no IRR calculations. (E-R4, tab VV) Appellant obtained refinancing at a favorable rate and it advised the Government of the financing structure (E-AR4, tab 218). Originally, First Boston did not believe that appellant would be able to obtain 100 percent financing. Appellant's ability to obtain financing with no equity contribution was due to changes in the market for private placements such that insurance companies which lent long-term (20 years) fixed-rate money were attracted to the project, which they then considered as "robust." (Tr. 1/178-80)

51. In October 1987, following extensive internal discussions dating back to at least May 1987, the Government, by letter (RFP II), requested appellant to submit a proposal to modify the Capacity Charge by structuring an alternative method of payment, consisting of varying the Capacity Charge on an annual basis in lieu of the equal payment method, with the objective of reducing the life cycle costs to the Army (E-AR4, tabs 47, 49, 203-210, 212-215, 220). Appellant advised the Government that although, prior to the execution of Mod 2, it had proposed alternative forms of payment, including a lump sum payment, in lieu of an increase in the Capacity Charge, it was no longer able to do so because the projected cash flow under Mod 2 formed an integral part of its refinancing deal (E-AR4, tabs 48, 51). The parties were unable to reach an agreement to modify the Capacity Charge and, in January 1988, the Government rescinded RFP II. The Government considered, however, that, at

some future appropriate time, it might (a) examine and assert a contractual right to a revised Capacity Charge, including one under the Price Reduction for Defective Cost or Pricing Data, or (b) terminate the contract for its own convenience and take title to the facility with compensation to appellant (ER4, tab BBB; E-AR4, tabs 52, 223).

52. Appellant completed its refinancing in March 1988 (E-ex. A-49). The Government pursued a strategy of awaiting the completion of construction before pursuing an effort to renegotiate the Capacity Charge payment (E-AR4, tabs 229, 230, 232).

53. In 1989, the Government contracted with Robbins, Pope & Griffis, PC (RPG) to study the circumstances surrounding the issuance of Mod 2. RPG issued its report in January 1990 and concluded, among other things, that the data appellant submitted in support of Mod 2 was not in accordance with TINA. (E-AR4, tab 241)

54. In April 1990, the Army requested that the Defense Contract Audit Agency (DCAA) perform an audit to determine whether appellant had submitted defective cost or pricing data in support of the tax adjustment (E-R4, tab B, ex. 50).

55. After a dispute developed between the parties relating to access to records, they, along with their respective counsel, met on 18 December 1991. At the meeting, LTC Buckner M. Creel, IV, who had assumed responsibility as contracting officer in December 1990, indicated that the Government was "outraged" at appellant's earning a 33 percent rate of return on the project, that there was no risk in doing business with the Government and that a 10 percent rate of return would be reasonable, and that if he did not get back $5 million per year from appellant the Government could get another contracting officer. (E-exs. A-59, -60; E-tr. 4/42-45, 8/119) In order to ascertain the impact of LTC Creel's position, appellant's General Kelly asked appellant's Mr. Woodcock to prepare a paper on the issue. In response, on 31 December 1991, Mr. Woodcock sent a memorandum advising appellant's General Kelly and Mr. Garnett as follows:

> Pursuant to our conversation on December 30, I have calculated the project NPV's using a 10%, 15% and 33% discount rate.
>
> Note that lowering the discount rate substantially reduces the price increase required to restore the owner's NPV. This occurs because under a lower discount rate the [investment tax credit] and accelerated depreciation become less valuable relative to the annual operating cash flows that are now subject to a lower tax rate.

The memorandum was accompanied by a table reflecting the NPVs. (E-R4, tab B, ex. 44; E-tr. 4/165-66)

56. On 1 June 1993, DCAA issued its audit report finding that Jones had submitted cost or pricing data in support of Mod 2 that was not accurate, complete and current as of the date of the parties' agreement on price, a date later than BAFO (E-R4, tab B, ex. 70).

57. On 12 August 1993, LTC Creel issued his decision concluding that the tax adjustment under Mod 2 was not supported by current cost or pricing data. The decision focused on appellant's failure to provide pro formas, including that dated 18 December 1986, as of the date of agreement on price for Mod 2, and did not specifically discuss pro formas or other cost and pricing data existing prior to or on the date of BAFO. The decision included an interpretation, not previously discussed by the parties, that the net after tax rate of return in the BAFO was a cap to be used in determining adjustments due to changes in tax laws and that intervening events between contract award and the tax law change must be considered in determining what impact, if any, a change in the law might have on a contractor's return on investment. The decision concluded: (a) that the Government was entitled to a refund; (b) that the monthly Capacity Charge be reduced by $537,581 to $783,771, to reflect the adjustment found due as a result of Mod 2; (c) that the amount of the overpayment from February 1989 through July 1993 was $27,777,905, plus interest of $6,367,466; (d) and that, to recover the overpayment, the monthly Capacity Charge be reduced to $276,552 for the remaining contract period, subject to revision based upon applicable interest rates. (E-R4, tab B) As a result of the decision, the Army has been withholding from appellant payments in excess of $800,000 per month (E-tr. 4/54).

58. The Army terminated the captioned HTW contract for its own convenience effective 30 September 1999 (tr. 3/116).

59. In this proceeding (ASBCA No. 51754), we have been presented with fact and expert evidence on the issue of the return on investment which appellant intended to receive at the time of BAFO, as well as the rate of return on investment which could be reasonably anticipated from a project of this nature. We also have been presented with extensive expert evidence, in both testimonial and documentary form, regarding: (a) the impact of the TRA upon appellant, and (b) the NPV and IRR methodologies and their use, or potential use, in calculating the tax adjustment to the Capacity Charge. In our initial proceeding in ASBCA Nos. 46790 and 47020, our findings and decision were based, in part, upon considerably more limited evidence on all of the above issues. Based upon the more fully developed and accurate record now before us, as more fully discussed below, we substitute the findings below in lieu of our findings in the section "Expert Evidence - Impact of the TRA and the IRR and NPV Methodologies" and other findings in our original decision (97-2 BCA ¶ 29,077, beginning at 144,745) which we specifically identify below.

60. The witnesses included Mr. John Stevenson, formerly of First Boston, who was quite credible and whose testimony included fact testimony on the contemporaneous advice tendered Jones by First Boston on the rate of return on investment required to attract equity capital for the project. On the issue of rates of return reasonably expected in 1986 for different types of investment projects and on the more general issues involving the NPV

and IRR methodologies, the record now includes the testimony of several expert witnesses. The record also contains references to several texts on corporate finance. Expert testimony was provided by Mr. Joseph Robbins of RPG, Ms. Anita Molino and Dr. Richard Bower. In assessing their testimony, we have considered (a) the nature and extent of their education and experience, (b) the extent to which they reviewed and were familiar with the evidentiary record, (c) the substance, internal consistency and intellectual honesty of their expert reports, (d) possible conflicts of interest relating to other professional activities, and (e) the substance of, and their demeanor during, their sworn testimony in direct and cross examination. Our findings reflect our assessment, based upon the above criteria, that Dr. Bower's analysis was extremely persuasive and Mr. Robbins and Ms. Moline were not persausive.

61. In 1986, 15 percent was approximately the return an investor could expect from an investment in an established, diversified corporation whose stock was publicly traded. When financial leverage (*i.e*., debt) is added to project finance it creates more risk and increases the return on investment expected by the equity investors. It is inconceivable that 15 percent could represent the equity return expected on the HTW project where Jones assumed a 70/30 debt-to-equity ratio. Assuming that debt-to-equity ratio, if 15 percent were Jones' required equity return on the HTW project Jones' BAFO would have proposed to the Army a Capacity Charge of approximately $15,000 as opposed to the $647,411 in Jones' BAFO and the $917,000 and $2,070,000 in the offers of Jones' competitors. (E-ex. A-98; ex. A-222; tr.1/116-17, 132-35, 162, 4/51-52)

62. At the time of Jones' BAFO, the HTW project contained sufficient risk to warrant expectation of a significantly higher return on investment. It consisted of a lease arrangement where (a) appellant, the lessor, assumed most of the risk of ownership and operation, (b) income, including that from electricity sales, was sensitive to economic conditions which could also affect a Government decision to terminate the contract, and (c) it involved a specialized asset which could be simply removed for a different use. (E-R4, tab B, ex. 36; ex. A-222; tr. 1/149, 162) First Boston's conclusion that a 33 percent after-tax rate of return, after giving effect to 70 percent debt financing, should be used in developing the BAFO was based upon its knowledge of the marketplace in 1986, its assessment of the risks of the HTW project and the need for First Boston to be confident that it could attract the required equity participation; the reasonableness of its conclusion was supported by the response to First Boston's solicitation for equity participants. The Jones BAFO was based upon a 33 percent IRR; that percentage was reasonable and an IRR of 15 percent would be unreasonably low to attract equity capital. (R4, tab 561; ex. A-222 at 4, 10-17; tr. 1/65-66, 106-07, 113, 133-34, 147-50, 3/18-19) We so find.

63. NPV and IRR are both discounted cash flow methodologies which may be used to evaluate investments. Both methods recognize the importance of discounting future dollars or cash flows in assessing investments to reflect the fact that funds received and put to use sooner are worth more than those received later. NPV and IRR are closely related. NPV is the dollar value resulting from the present valuing of a stream of cash flows,

including the initial investment, at a given discount rate. IRR is the specific discount rate produced by a set of cash flows when the NPV is equal to zero. (Exs. A-222 at 8, -249 at 168)

64. IRR is a rate, calculated as a percent. NPV is not a rate; NPV is a value, calculated in dollars, at a specified discount rate. The TAX ADJUSTMENT clause refers to a rate, rather than a value, to be preserved. (Ex. A-222 at 8-9) Because lenders are paid in pre-tax cash flows and all of the risks of tax law changes in the HTW project were to be borne by the equity investors, the applicable IRR is the IRR derived from the after-tax equity cash flows assumed at BAFO (tr. 1/110, 153, 183-85).

65. NPV may be expressed by the general equation: NPV @ (discount rate) = (dollar value). IRR may be expressed by the specific equation: NPV @ (IRR) = $0. IRR does not "result" from the calculation of a net present value that is either positive or negative. Rather, IRR is calculated independently by determining the discount rate at which a set of cash flows produce an NPV of zero. While there are an infinite number of net present values that can be calculated from the same set of cash flows simply by selecting different discount rates, only the discount rate that produces a zero NPV can be the rate of return on investment. (Exs. A-222 at 8, -249 at 168, -258 at 92, -278; tr. 3/89, 4/43-45)

66. Dr. Bower's analysis included four scenarios, discussed in detail below, under which the Capacity Charge adjustment is examined. One of the tax adjustment calculations involved the use of an "Adjusted Pro Forma," which Dr. Bower created by (a) identifying inconsistencies between the As Bid Pro Forma and the First Boston Pro Forma, and (b) selecting the assumptions that would produce the lowest Capacity Charge adjustment required by the TAX ADJUSTMENT clause. (Ex. A-222 at 6-7)

67. One limitation in solving for IRR, rendering it meaningless as a decision tool in some instances, is that it may produce more than one answer when the cash flows for a given period shift from negative to positive or positive to negative more than once. That limitation is not present in the First Boston Pro Forma, the As Bid Pro Forma or the Bower Adjusted Pro Forma. (Ex. A-249 at 171; tr. 1/152-53, 3/88, 164)

68. The IRR and NPV methodologies produce the identical tax adjustment using the same after-tax equity cash flows and a discount rate equal to the IRR. Using the Jones actual assumed net after-tax rate of return on investment at BAFO of 33 percent as the discount rate, the tax law change adjustment is the same employing either the IRR or NPV methodology. (Ex. A-222 at 4; tr. 3/165)

69. Cash flows in later years are discounted more than cash flows in early years because the use of the same risk-adjusted discount rate for each year's cash flow implies a larger deduction for risk from the later cash flows. The discount rate compensates for the risk borne per period; thus, the more distant the cash flows, the greater number of periods and the larger the total risk adjustment. Both NPV and IRR weight early years' cash flows

more heavily than later ones. If the discount rate is the same as the IRR, the weighting for each year is identical using either NPV or IRR. (Ex. A-222 at 17-18; -258 at 228; tr. 3/70-71)

70. Neither NPV nor IRR, used to calculate the tax adjustment under the TAX ADJUSTMENT clause, assume any reinvestment of after-tax equity cash flows paid to the HTW project investors. The calculation of rate of return on investment is independent of any use to which an investor puts cash flows received. Reinvestment of cash flows is an issue only when using IRR or NPV to evaluate mutually exclusive projects of different durations. Mutually exclusive projects exist when an investor has more than one investment option, but is unable to select all options. Whether a one-year investment at a certain IRR is a better investment than a two-year investment at a lower IRR depends on knowing whether the cash flows from the one-year investment can be reinvested, and the rate of reinvestment, for the second year. Neither NPV nor IRR measures for evaluating mutually exclusive projects are sensitive to this fact and thus both can produce incorrect answers. Reinvestment is not an issue when employing IRR to calculate the tax adjustment because the tax adjustment does not require comparison of two mutually exclusive projects. (Exs. A-222 at 4, 18-20, -258 at 99; tr. 4/52-59, 63) We make the findings in this paragraph in lieu of the inconsistent finding in our earlier opinion (97-2 BCA ¶ 29,077 at 144,713).

71. In its evaluation of the Jones tax adjustment request for the Government, Stone & Webster used an NPV methodology to calculate the tax adjustment required under the TAX ADJUSTMENT clause to compensate for the impact of the TRA. Stone & Webster performed its NPV calculation using two different discount rates: 33 percent and 10 percent. It used a 33 percent discount rate to determine the present value of the net loss to Jones due to the tax law change which it then restored by increasing the Capacity Charge. It also determined the present value to the Army of the incremental cost over two payback periods, 20 years and five years, discounted at 10 percent, the Government's imputed cost of money. Stone & Webster recognized the impact of the difference between the Jones and Army discount rates and recommended to the Army that it consider trying to negotiate the tax adjustment with Jones by seeking to pay Jones in a lump sum or by paying over five years. Stone & Webster also informed the Army prior to the execution of Mod 2 that if, in the future, it wished to compensate Jones based upon the present worth of incremental cash flows at a stipulated discount rate, it must "reword" the TAX ADJUSTMENT clause. (E-R4, tab 173; tr. 3/166-67)

72. In his analysis, Dr. Bower provided four scenarios involving adjustments to the Capacity Charge. Each of the Capacity Charge adjustment calculations was performed by (a) identifying the baseline assumptions including rate of return on equity investment in the environment prior to the TRA, (b) modifying those assumptions to eliminate the Investment Tax Credit, lengthen depreciation schedules and reduce the federal tax rate in accordance with the TRA, and (c) adjusting the Capacity Charge to restore the assumed net after-tax rate of return on equity investment. The first scenario is that presented in Mod 2, based on the As Bid Pro Forma, where there was a 68.6 percent increase in the BAFO Capacity Charge to

$1,091,463. The second scenario is what the Capacity Charge increase should have been, also based on the As Bid Pro Forma, had it been accurately calculated in the tax adjustment request, as Jones had contemporaneously informed the Army in the tax adjustment request -- a 75.69 percent increase in the Capacity Charge to $1,137,436. The third scenario used the First Boston Pro Forma (adjusted to include the BAFO Capacity Charge of $647,411), which resulted in a net after-tax return on investment of 37.95 percent and an 87.6 percent increase in the Capacity Charge to $1,214,394. In the fourth scenario, Dr. Bower calculated the tax adjustment using the Adjusted Pro Forma, in which, as stated above, he (a) identified inconsistencies between the As Bid Pro Forma and the First Boston Pro Forma and (b) selected the assumptions that would produce the lowest Capacity Charge adjustment required by the TAX ADJUSTMENT clause. Based on those criteria, Dr. Bower used the following assumptions in the Adjusted Pro Forma as compared to the As Bid Pro Forma: (a) a five percent limestone escalation factor versus the four percent factor used in the As Bid Pro Forma; (b) the addition to the escrow account (sufficient to cover the interest expense for at least a year) which was in the As Bid Pro Forma but not included in the First Boston Pro Forma; and, (c) a first-year capital expenditure of $16.7 million included in the As Bid Pro Forma versus the $16.65 million which was in the First Boston Pro Forma. Using the Adjusted Pro Forma, the adjustment required to preserve the assumed net after-tax rate of return of 33.01 percent is a 74 percent increase in the Capacity Charge to $1,130,164. Of the calculations in the four scenarios, the actual tax adjustment included in Mod 2 is the most favorable to the Army. (Ex. A-222 at 5-7; E-tr. 3/147-48)

73. Dr. Bower was not surprised by the size of the increase in the HTW Capacity Charge needed to preserve the assumed net after-tax rate of return under the TAX ADJUSTMENT clause. The Capacity Charge accounted for only about 30 percent of the assumed revenues, and approximately 70 percent of the revenues were projected to come from the sale of electricity to NIMO. Since, under the TAX ADJUSTMENT clause, the full impact of the tax adjustment was to fall solely on the Capacity Charge, the resultant percentage increase in the Capacity Charge was understandably significant. Had the TAX ADJUSTMENT clause been drafted to spread the impact of the tax law change across all assumed revenues, the percentage increase in the Capacity Charge would have been substantially less. (AR4, tab 561)

74. Mr. Robbins' analysis concluded that an 8.65 percent increase in the Capacity Charge was sufficient to restore appellant's net after-tax rate of return to its pre-TRA level. In the course of these proceedings, he prepared a series of reports. In his first two reports, Mr. Robbins used the method used in the First Boston Pro Forma, discounting each year's cash flows beginning with the first year. However, commencing with his third report and continuing through his testimony at the hearing in this appeal, Mr. Robbins, despite changes in input amounts, modified his NPV formula to discount the cash flows starting with the second year and thus maintained an 8.65 percent increase in the Capacity Charge as the tax adjustment. This modification in the method of computation, of which Mr. Robbins informed neither appellant nor the Board, resulted in a substantial understatement of the tax adjustment. (AR4, tabs 11, 13, 15; exs. A-266 through -269, -272; tr. 3/177-90, 4/20)

75. At the time of its BAFO submission, Jones assumed that equity would be invested on a pro rata basis with its borrowings. The pro rata infusion of equity served the interest of lenders because such infusion meant that equity investors would share the risk of project failure during construction. First Boston believed that, at the time of bid preparation, an assumption that equity infusion could await construction completion would have been too aggressive. Subsequently, First Boston determined that there was a reasonable possibility that, based on the banking market, lenders might agree to finance 100 percent of the construction period, with equity contributions first coming in at the end of construction. In return for that accommodation, at the financial closing in 1987 equity investors, including Jones in the form of letters of credit, had to provide guarantees which had the effect of limiting the financial obligations which the equity investors could accept outside of the HTW project. When First Boston ultimately solicited 100 percent financing by approximately 15 banks for the construction period, several lenders declined to participate, at least two of which cited the late infusion of equity capital as among their reasons (E-AR4, tab 18; R4, tabs 548-1 through 548-10; exs. A-207, -222 at 7; tr. 1/80, 117-18, 2/22-26)

76. The TAX ADJUSTMENT clause requires that, in performing the adjustment calculation, all pre-TRA assumptions be held constant except for the applicable changes in the tax law. If equity timing is changed from pro rata with debt to the end of construction, that change must first be made in the pre-TRA pro forma. In that manner, when the tax law changes are subsequently introduced into the pro forma, the difference will measure only the effect of the tax law change. Introducing the assumption of equity placement at the end of construction into the pro formas produces a higher IRR and a higher Capacity Charge adjustment than did Mod 2. (Ex. A-222 at 7; tr. 2/48-49)

77. At the time of Jones' BAFO submission, First Boston assumed debt financing using a two-year construction loan followed by a 10-year term loan. By September 1986, First Boston believed that it would likely be able to obtain financing only in the form of a two-and-one-half year construction loan and an eight-year term loan. First Boston made this change before soliciting debt participants because it believed that continuing to seek term loans of 10 years or longer would too greatly narrow the pool of interested lenders. In First Boston's view, obtaining long-term institutional investors willing to provide initial term financing for 19 or 20 years was totally unrealistic at the time of Jones' BAFO submission. At that time, the "long term fixed market," which consisted primarily of insurance companies, had "no appetite" for projects having the risks present in the HTW project. (Tr. 1/140-41)

78. In raising project debt in the 1986 time period, lenders would fairly commonly require that project owners place funds in an escrow account for the benefit of the lenders in case something were to go wrong on the project. At the time of the BAFO submission, Jones did not include a contribution to an escrow account as one of its assumptions. At some point following BAFO, Jones and First Boston included in their projections an annual

escrow calculation, equal to a year's principal and interest, for the benefit of lenders. (R4, tab 509; tr. 1/130-31) Eliminating the escrow account from the As Bid Pro Forma would produce a pro forma essentially equivalent to the First Boston Pro Forma. When the First Boston Pro Forma is used to calculate the tax adjustment under the TAX ADJUSTMENT clause, it results in an increase in the Capacity Charge greater than the adjustment in Mod 2. (Ex. A-222 at 5-7)

79. References to, and calculations involving, NPV on the pro formas described above were either irrelevant to the required return on equity or were intended to represent the weighted cost of capital to be used on the project's cash flows prior to the interest deduction. Weighted cost of capital is determined by adding the respective costs of debt and equity after they have been weighted according to the debt-to-equity ratio. Another term used for weighted cost of capital is "project return." Assuming that 15 percent represented the weighted cost of capital for the HTW project at a 70/30 debt-to-equity ratio and an interest rate of 11 percent for the debt portion (which First Boston had assumed in its pro forma), the required equity rate of return would be approximately 32 percent—consistent with the actual net after-tax rate of return on investment recommended by First Boston and used by Jones in its BAFO. (R4, tab 504; exs. A-222 at 9, -249 at 102, 108; tr. 1/183, 3/50-52) If, by contrast, 15 percent was the required rate of return on equity for the HTW project rather than its weighted cost of capital, the weighted cost of capital would then be 8.25 percent, approximately equal to the risk-free United States Treasury rate, which would be "ridiculously low" for the HTW project. (Ex. A-222 ; tr. 3/53-54)

80. Like weighted cost of capital, project return is the rate of return to all financial participants in a project, both debt and equity investors. Because a tax law change impacts equity investors, but not debt investors, it is improper to use project return or weighted cost of capital to preserve the return to equity. (Ex. A-249 at 159, 439-40; tr. 1/153, 183-85)

DECISION

In this contract to finance, design, construct, permit and operate a high-temperature water (HTW) and co-generation facility at the Fort Drum Army Base, the parties included the TAX ADJUSTMENT clause intending to adjust the amount of the monthly Capacity Charge paid to appellant under the contract in the event of changes in tax legislation. Upon passage of the Tax Reform Act of 1986 (TRA), the parties negotiated a contract modification (Mod 2) to increase the amount of the monthly Capacity Charge. Another contracting officer later rescinded Mod 2 on the grounds (a) that the adjustment was not authorized by the TAX ADJUSTMENT clause and (b) that appellant's request for a tax adjustment had not been accompanied by all current cost or pricing data as required by TINA.

In our earlier decision (97-2 BCA ¶ 29,077), we concluded that the TAX ADJUSTMENT clause in the contract entitled appellant to an increase in the Capacity Charge under the contract as a result of the passage of TRA. On that record, however, we also concluded that the data submitted by appellant in support of its request for a tax adjustment was not current, complete and accurate as required by TINA, thereby entitling the Government to a price adjustment under the contract.

<u>The Evidentiary Record</u>

Prior to the hearing in the captioned quantum appeal, the Government filed a Motion in Limine to Exclude Introduction of Certain Evidence at Trial. The presiding judge denied the motion, but permitted the Government to renew it in its post hearing brief. The Government has renewed the motion to exclude evidence and appellant has opposed the motion.

The Government contends that, based upon the doctrines of law of the case and *res judicata*, our earlier decision in the entitlement phase of the proceedings is binding on the "current quantum phase" and that the parties should not be permitted to relitigate matters decided in our earlier decision. Those issues which the Government contends have already been decided and may not be relitigated relate to our TINA determinations and include: (a) the use of net present value (NPV) versus internal rate of return (IRR) methodologies, including their strengths and weaknesses; (b) the nature and extent of the risk in the HTW project; (c) the timing of financing and equity infusion into the project; and, (d) the propriety of the use of a 33 percent IRR.

A key issue in this quantum proceeding is the determination of the net after tax rate of return on investment appellant was seeking at the time of its BAFO submission. It is in the context of our attempt to resolve that central issue that additional evidence regarding the NPV and IRR methodologies, as well as the omission of the NPV calculation on data appellant submitted to the Government, is directly probative in this quantum phase. Accordingly, neither *res judicata* nor the law of the case precludes us from examining the evidence in this proceeding to resolve the central issue yet before us.

The fact that our findings and conclusions here differ in some respects from those in our earlier decision does not stand in the way of our obligation to resolve the quantum issue.

Under the law of the case doctrine, the judicial tribunal retains discretion to reconsider or consider more fully a prior ruling. "Law of the case rules have developed to maintain consistency and avoid reconsideration of matters once decided during the course of a single continuing lawsuit. These rules do not involve preclusion by final judgment; instead they regulate judicial affairs before final judgment. . . . Although courts are often eager to avoid reconsideration of questions once decided in the same proceeding, it is clear that all federal courts retain power to reconsider if they wish." 18 WRIGHT-MILLER-COOPER, FEDERAL PRACTICE & PROCEDURE § 4478 (1981 & 2001 Supp.). Departure from application of the law of the case is appropriate where the evidence in the subsequent proceeding is substantially different, controlling authority has since made a contrary decision of the law applicable to the issues, or the initial decision was clearly erroneous and would work a manifest injustice. *Hughes Aircraft Co. v. United States*, 86 F.3d 1566, 1576 (Fed. Cir. 1996); *American Asphalt, Inc.*, ASBCA No. 44160, 95-2 BCA ¶ 27,614. The law of the case doctrine does not require a tribunal to perpetuate error once the error is brought to its attention. *McGee v. United States*, 63 F.R.D. 205, 209 (E.D. Pa. 1972). We have overturned prior findings and decisions where, based upon evidence newly before us, we were persuaded that our earlier decision was erroneous. *Kos Kam, Inc.*, ASBCA No. 34681, 96-2 BCA ¶ 28,569; *Control Data Corp.*, ASBCA No. 16448, 76-1 BCA ¶ 11,841.

A review of our original decision reflects that the key issues before us were (a) whether the contract's TAX ADJUSTMENT clause was applicable to the TRA, (b) if applicable to the TRA, the appropriate methodology of computing the tax adjustment due under the terms of the clause, and (c) whether the Government was due a price adjustment under TINA. We concluded that the TAX ADJUSTMENT clause was applicable to the TRA. We further concluded that the tax adjustment was to be calculated by using the data at the time of BAFO as the baseline, without consideration of post-BAFO data changes, and to measure the impact of the tax adjustment solely upon the consequences of the tax law changes. Our discussion of TINA was likewise centered upon the extent to which, if at all, post-BAFO data was to be considered in a determination of whether appellant had submitted data which was not current, complete and accurate. We also made findings, which led to conclusions, regarding differences between the NPV and IRR methodologies, the omission of NPV information from appellant's data, and the ramifications of the timing of appellant's equity contributions. The parties' briefs in our original proceeding reflect barely a mention of those issues and our findings there were based upon very limited testimony by a witness whom, as our findings above reflect, we have found to be unpersuasive in this proceeding. By contrast, the record on those and related issues in this proceeding includes substantially more fact evidence as well as expert testimony and treatises offered by both parties and bears little resemblance to that before us in the earlier proceeding. As we stated above, that additional evidence regarding the NPV and IRR methodologies, as well as the omission of the NPV calculation on data appellant submitted to the Government, is directly probative in this quantum phase. However, even were that not the case, the far more extensive record here presents evidence which is substantially different than in our earlier proceedings and, as reflected in our findings above and our decision on the merits below, our initial decision was clearly erroneous resulting in a manifest injustice to appellant to warrant our application of the exception to the law of the case doctrine.

The Government's motion to exclude evidence is denied.

The Merits

After the parties agreed upon and entered into Mod 2 to increase the Capacity Charge paid to appellant in implementation of the TAX ADJUSTMENT clause as a result of tax law changes due to the passage of the TRA, the Government unilaterally rescinded the modification and reduced the Capacity Charge payment on the ground that data submitted by appellant in support of its tax adjustment request, upon which Mod 2 was based, was not current, complete or accurate, in violation of TINA.

In order to sustain a contract price reduction under TINA, the Government bears the burden of proving defective pricing by a preponderance of the evidence by establishing: (a) that the data submitted by appellant was "cost or pricing data" under TINA; (b) that the subject data was not disclosed or was not meaningfully disclosed to a proper Government representative; and, (c) that the Government relied upon the defective data to its detriment in an overstatement in the contract price. In the last element, there is a rebuttable presumption that the "natural and probable consequence" of the nondisclosure or the use of defective data is a contract price increase. The contractor must then demonstrate that there was no reliance on the defective data or that there would have been no reliance had the data in question been disclosed. *Sylvania Electric Products, Inc. v. United States*, 479 F.2d 1342, 1349 (Ct. Cl. 1973); *Rosemount, Inc.*, ASBCA No. 37520, 95-2 BCA ¶ 27,770. The Government's overriding burden includes the requirement that it demonstrate a causal connection between the undisclosed or defective data and an overstated contract price. *Universal Restoration, Inc. v. United States*, 798 F.2d 1400, 1403 (Fed. Cir. 1986).

The crux of the Government's position is that appellant violated TINA in that, in connection with its tax adjustment request: (a) appellant failed to disclose the First Boston Pro Forma, which was the most current at the time of BAFO and should properly have been the baseline from which adjustments to the Capacity Charge should have been made under the Tax Adjustment clause; and, (b) its As Bid Pro Forma, which was created especially for, and was submitted with, its tax adjustment request, omitted data which had been included in the undisclosed First Boston Pro Forma.

The Government argues that "NPV @ 15% = $21.7 million" was the "net after tax rate of return on investment" which was to be preserved under the TAX ADJUSTMENT clause and that the omission of that calculation from the As Bid Pro Forma and the inclusion of an IRR of 33 percent misled the Government into agreeing to enter Mod 2 increasing the Capacity Charge by an excessive amount based on the 33 percent IRR rate.

The Government argues that the language "net after-tax rate of return on investment" in the TAX ADJUSTMENT clause is clear, and reasonably applies to the NPV @ 15% = $21.7 million calculation. Alternatively, the Government maintains that, if the language in the TAX ADJUSTMENT clause is ambiguous, the ambiguity be construed against appellant, whose counsel allegedly authored the clause, and that we accept the Government's reasonable interpretation. We do not agree.

We observe, initially, that the record reflects that the language of the TAX ADJUSTMENT clause was the product of the parties' negotiations and responsibility for the language in question cannot be placed solely at the feet of appellant's counsel. Further, a party wishing to have its interpretation adopted must establish that it held that interpretation at the time it entered into the agreement. Here, there is no evidence that the anyone representing the Government interpreted the TAX ADJUSTMENT clause as applying to anything other than IRR. We note, further, that we have found that IRR is a rate, calculated as a percent and that NPV is not a rate, but is a value, calculated in dollars, at a specified discount rate. While the TAX ADJUSTMENT clause could have been drafted with more specificity by the use of the term IRR, we conclude that the phrase "net after-tax rate of return on investment" may reasonably be interpreted as IRR, but that the calculation based on NPV could not reasonably be included within the language of the clause.

The result in this appeal does not turn solely on a matter of contract interpretation. The key issues before us are the determination of appellant's anticipated net after-tax rate of return on investment at the time of its BAFO submission, its reasonableness, and whether cost and pricing data which appellant failed to provide to the Government resulted in an increased contract price.

The Government contends that a "rate" can be a "ratio," and that: (a) as reflected in the First Boston Pro Forma, appellant's anticipated after-tax rate of return on investment was the ratio NPV @ 15% = $21.7 million; (b) appellant's investment, as indicated in the First Boston Pro Forma, was $22.2 million and its return was $21.7 million; (c) the adjustment due appellant as a result of the passage of the TRA is an adjustment in the Capacity Charge "to restore the return of NPV 15% equals $21.7 million"; and, (d) that adjustment is an 8.6 percent increase in the Capacity Charge. Based upon our record, we do not agree.

Our findings above reflect that appellant's BAFO was based on an IRR of 33 percent and that a rate of return to equity investors in that range was reasonable in light of the nature of the project, the anticipated debt-to-equity investment ratio and the realities of the marketplace in 1986. We have also found that, based upon those criteria, 15 percent, the percentage upon which the Government rests its argument, would have been an unreasonably low rate of return to attract equity investors.

While we are able to conclude that the calculation "NPV @ 15% = $21.7 million," which was included on the First Boston Pro Forma but omitted from the As Bid Pro Forma, did not represent the equity rate of return on the project, there is no equally conclusive evidence of what it did represent. Early analyses by appellant reflected in our findings indicate that it could have related to a then expected cash on cash return for the first five years of the project. Further, based, in part, upon expert testimony, we have found that the NPV calculations either (a) were irrelevant to the required return on equity or (b) represented the weighted cost of capital, or project return, to be used on the project's cash flows prior to the interest deduction, and that a weighted cost of capital of 15 percent here would have been consistent with a required equity rate of return of 32 percent.

The Government contends that the IRR methodology is flawed, is less reliable than the NPV method, assumes that project cash flow can be reinvested at the same IRR, and distorts the value of the cash flows during the early years of the project. Based upon our record, we do not agree.

We have found that a potential limitation in the IRR methodology, that it may produce more than one answer when the cash flows for a given period shift from negative to positive or positive to negative more than once, is not present in the First Boston Pro Forma, the As Bid Pro Forma or the Bower Adjusted Pro Forma, and we conclude, therefore, that the potential limitation has no bearing upon our decision. Our findings above also reflect that the IRR and NPV methodologies produce the identical tax adjustment using the same after-tax equity cash flows and a discount rate equal to the IRR and that, with the discount rate the same as the IRR, the weighting for the cash flows of each year is identical using either NPV or IRR. We have found, further, that, for purposes of calculating the tax adjustment under the TAX ADJUSTMENT clause, neither the NPV nor IRR methodologies assume any reinvestment of after-tax cash flows paid to the project investors and that reinvestment of cash flows becomes an issue only when using NPV or IRR to evaluate mutually exclusive projects of different durations.

Our findings reflect the importance of the timing of equity infusion into the project and that, at the time of its BAFO submission, appellant assumed that equity would be invested on a pro rata basis with its borrowings. The Government had previously taken the position that the computation of the adjustment to the contract to reflect the passage of the TRA required equity infusion at the end of construction. In its post-hearing brief, the Government, in a stated effort to reduce the points of contention, has agreed to the computation of the tax adjustment on the basis of the pro rata timing of equity investment. Thus, the timing of equity infusion is no longer at issue.

As reflected in our findings, the Government, almost throughout these appeals, has maintained that an 8.65 percent increase in the Capacity Charge was all that was required to compensate for the effects of the TRA. In its post-hearing briefs, however, the Government, apparently due to the inconsistency in Mr. Robbins' analysis reflected by our findings, concedes that "[i]f the Board determines that NPV should be calculated in 1985 dollars[,]" the appropriate adjustment would be 18.8 percent.

The Government contends that, because the Board, in our previous decision, granted reformation, a measure of equitable relief, in concluding that the TAX ADJUSTMENT clause applied to the TRA, the result must be fair and equitable, but that, as a result of the tax adjustment upon which the parties agreed in Mod 2, appellant obtained a "windfall" profit which we should not permit to stand. We believe that the Government errs.

In our prior decision, we reformed the contract to conform to the intent of both parties. That action was totally independent of the merits of, or the effects of, any TINA claim possessed by the Government. The Government's burden of proof on the TINA claim and damages therefrom exists nonetheless. With respect to the nature of appellant's profit, the record reflects that, at the time it entered into Mod 2, the Government was well aware of the dramatic effect upon the Capacity Charge and contract price resulting from the modification and was alerted by Stone & Webster, which had reviewed appellant's tax adjustment request, of alternatives the Government could seek to reduce the long-term substantial dollar impact upon the Government. Our role is not to arbitrarily place a limit upon costs to the Government or to limit appellant to what the Government considers to be a fair profit. Our task is to determine, based upon the facts before us, whether those costs and that profit resulted from a TINA violation.

We conclude, based upon the entire record, that the As Bid Pro Forma upon which the Government relied in entering into Mod 2 properly included appellant's assumptions, including its IRR rate, at BAFO, and that the omission of NPV calculations neither misled the Government nor resulted in an increase in the contract price. The data submitted to the Government by appellant in support of its tax adjustment request did not violate TINA and the Government's rescission of Mod 2, which provided for a 68.6 percent increase in the Capacity Charge, was improper. Appellant is entitled to a contract price adjustment restoring the monthly Capacity Charge under Mod 2, plus appropriate interest under the Contract Disputes Act of 1978 calculated from 11 October 1993, the date of submission of appellant's certified claim (see 97-2 BCA ¶ 29,077 at 144,745), until date of payment.

The appeal is sustained.

Dated: 5 April 2002

RONALD JAY LIPMAN
Administrative Judge
Armed Services Board
of Contract Appeals

I concur in result
See separate opinion.

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

I concur in result
See concurring opinion.

CARROLL C. DICUS, JR.
Administrative Judge
Acting Vice Chairman
Armed Services Board
of Contract Appeals

CONCURRING OPINION BY ADMINISTRATIVE JUDGE DICUS

I concur in result only. I am persuaded that the Government has failed to meet its burden of proof on quantum, but I would not alter our decision on entitlement ("*Black River I*"). My reasons are set out below.

The presiding judge's opinion holds that the record is devoid of evidence that the Government's professed interpretation of the TAX ADJUSTMENT clause was held at the time it entered into Mod 2. Such evidence is required where, as here, the other party's interpretation is found to be reasonable. *Fruin-Colnon Corp. v. United States*, 912 F.2d 1426 (Fed. Cir. 1990); *Lear Sigler Management Services Corp. v. United States*, 867 F.2d 600 (Fed. Cir. 1989). Moreover, the opinion holds that the clause cannot be reasonably read as including net present value (NPV) as within the phrase "net after tax rate of return on investment," while concluding that internal rate of return (IRR) may reasonably be included within the phrase. I concur in the foregoing interpretation. We did not reach that interpretation issue in *Black River I*, so it is not a change to the entitlement decision. The interpretation of the clause would appear to eliminate NPV from further consideration as a means of determining the tax adjustment, although the practical effect is not significant, as explained below.

Further, as to the Government's failure to meet its burden of proof on quantum, we held in *Black River I*, *inter alia*:

> We conclude that the data provided by appellant as BAFO data and in support of the tax adjustment request leading to Mod 2 was not current, complete and accurate, as required by TINA. The As Bid pro forma was neither accurate nor complete, when compared to actual pro formas contemporaneous with BAFO. In addition, appellant failed to provide the following cost or pricing data with respect to the tax adjustment request leading to Mod 2: (a) appellant's internal spreadsheets dated 25 November 1985; (b) First Boston pro formas dated prior to and including 13 March 1986; (c) First Boston's presentation of 22 March 1986; (d) the First Boston Descriptive Memorandum of September 1986; (e) First Boston's memorandum dated 18 November 1986; and, (f) First Boston's pro forma of 18 December 1986.

97-2 BCA ¶ 29077 at 144,750-51. We concluded that, as a result of appellant's failure to satisfy TINA requirements, the Government was entitled to a price adjustment. *Id.* at 144,752. This arises from a rebuttable presumption that the natural and probable consequence of non-disclosure is a price increase. *Id.* at 144,748. However, the Government still has the burden of proving the specific amount of that increase. *American Machine & Foundry Co.,* ASBCA No. 15037, 74-1 BCA ¶ 10,409 at 49,174.

It is the amount of the price adjustment that is now at issue. The Government's contentions, as I understand them, may be succinctly and simply restated as follows: (1) the undisclosed data show NPV calculations at a 15 percent discount rate; (2) NPV is the proper measure for calculating the capacity charge increase resulting from the TAX ADJUSTMENT clause; and (3), in effect, the 33.3 percent IRR rate would not have been agreed to during negotiations if the Government had known of the 15 percent NPV calculations in the undisclosed data. The Government states its ultimate position as follows:

> [T]he correct capacity charge adjustment should be an 8.6 percent increase over the BAFO price. If the Board determines the NPV should be calculated in 1985 dollars as First Boston did on March 13, 1986, the adjustment would be BAFO plus 18.8 percent.

(Gov't br. at 137) I understand this position to be derived principally from Mr. Robbins testimony and report. The first problem with this position is that the above interpretation of the TAX ADJUSTMENT clause takes NPV off the table in determining the tax adjustment itself. Since, under that interpretation, the tax adjustment is supposed to preserve appellant's net after tax IRR, and since one can solve for IRR using NPV, the Government could still prove its case by demonstrating that appellant's pre-tax adjustment net after tax rate was derived from a calculation using NPV with a 15 percent discount rate. That calculation converted to IRR would then form the net after tax IRR that would be preserved through the TAX ADJUSTMENT clause.

Although the Government has not argued its case in accordance with the above interpretation of the TAX ADJUSTMENT clause, it should still be possible to extract from the Government's presentation the amount to be excluded because of the defective pricing. While there is no blueprint for proving the specific amount of a TINA price adjustment, evidence should place the Board in the position of the parties at the time of the handshake and show how the undisclosed data would have been used to negotiate a lower price. The Government has not presented witness testimony from its negotiators intended to establish with specificity how the data would have been used during negotiations. This is a shortcoming, as the facts here do not present a situation where a vendor quote of $1.00 per item is not disclosed and a vendor quote of $1.25 per item forms the basis for negotiation. In the example, a difference of $.25 per item would be immediately apparent. Here, however, the record reflects that appellant considered numerous approaches to pricing the project before submitting its BAFO. The materiality of the undisclosed data to negotiations and the contract price is thus very hard to measure.

The Government has attempted to establish its position through expert testimony. Determinations as to credibility are the province of the presiding judge and seldom are such determinations candidates for second-guessing. *See, e.g., First Interstate Bank of Billings v. United States,* 61 F.3d 876 (Fed. Cir. 1995); *Hydromar Corp. of Delaware v. United States,* 25 Cl. Ct. 555 (1992). The presiding judge has categorized the considerations he used in reaching his assessment of the persuasiveness of the experts. He has also singled out Mr. Robbins for criticism. That criticism addresses the witness's modification of his method of computation without informing the Board or appellant. Thus, although the presiding judge has stopped short of asserting the witness was not credible, I can draw no other conclusion when I compare his articulated considerations with the witness's described conduct. His determination is, in my view, entitled to the deference of the other panel members who were not present at the hearing. Trustworthy expert evidence is a necessity if a party is to be persuasive in addressing these complicated facts involving sophisticated third party financing. With its principal expert's testimony rejected, the Government's position is materially weakened.

The Government's other expert, Ms. Molino, is barely mentioned in the presiding judge's opinion, except to find her unpersuasive. Having read her testimony, and particularly the cross examination, I also find her testimony unpersuasive. Accordingly, I would hold that the Government has failed to meet its burden of proof.

It must also be noted that we set the stage for the Government's argument by holding in *Black River I* that IRR "is less reliable and, at a rate of 33.3 percent, distorted the effect of the IRR in appellant's favor." *Black River I* at 144,750. However, we stopped short of holding that IRR is an *unreliable* method or mandating a rate less than 33.3 percent. In any event, the interpretation of the TAX ADJUSTMENT clause, *supra*, would appear to eliminate NPV as a means of calculating the tax adjustment, although its use to determine appellant's pre-tax adjustment rate is not thereby precluded. It is beyond question that appellant is entitled to submit evidence that the price adjustment should be less than that sought by the Government. The presiding judge properly took the evidence on IRR and the evidence of appellant's expert intended to show the 33.3 percent rate was reasonable in the circumstances, believed it, and felt compelled to alter the decision on entitlement as a result. It is here, as indicated above, that I differ. The evidence on quantum presented by appellant, which the presiding judge found so persuasive he would change *Black River I*, can also be seen as demonstrating that any price increase from the non-disclosure was non-existent or *de minimis*. Thus, in addition to the Government's failure of proof there is the additional factor created by the presiding judge's positive credibility determination with regard to appellant's expert and other witnesses and the persuasiveness of their testimony. That testimony may be seen as probative evidence that use of IRR at 33.3 percent, whatever its shortcomings, and despite the non-disclosure of the enumerated data, did not distort the contract price to such an extent that a price adjustment of any substance is necessary.

Finally, while it might be argued that we could craft some kind of a jury verdict, I believe we would go beyond mere speculation were we to do so. Accordingly, I would hold there should be no price adjustment as a result of our finding of defective pricing in *Black River I* and that the price agreed to by the parties in Mod 2 should stand.

However, I do not concur in the presiding judge's opinion regarding the reversal of our holding in *Black River I*. First, there is no need to do so if the panel adopts the basis I have proposed. Further, as far as I can tell, we have never reversed an entitlement decision based on evidence submitted in the quantum phase of the case. The presiding judge' s opinion would have us do so here in spite of the fact that the evidence relied on was not newly discovered and no attempt was made by appellant to file an appropriate motion to reopen the record of *Black River I*. Appellant here did not even file a motion for reconsideration, but filed instead an appeal to the Federal Circuit, which was dismissed as premature.[1] It is thus distinguishable from the cases cited as precedent for reversal of *Black River I*.[2]

The presiding judge's opinion applies only law of the case principles in altering *Black River I*. Even appellant appears to concede that application of *res judicata* principles would bar reconsideration of our holdings in *Black River I* (app. reply br. at 24-27). While ASBCA opinions have ruminated about law of the case in addressing whether the entitlement decision can be altered during the quantum phase, our decisions have generally done so while holding that *res judicata* applies. *See, e.g., W.C. Fore Trucking, Inc.*, ASBCA No. 40663; 93-2 BCA ¶ 25,703; *International Gunnery Range Services, Inc.*, ASBCA Nos. 43134, 43135, 93-1 BCA ¶ 25,394; *Maitland Brothers*, ASBCA No. 29825, 85-3 BCA ¶ 18,234. Another line of cases holds that entitlement decisions "at least" constitute the law of the case. *Thomas J. Papathomas*, ASBCA No. 51352, 99-1 BCA ¶ 30,349 at 150,089; and *Teledyne Continental Motors, General Products Division*, ASBCA No. 48364, 96-2 BCA ¶ 28,523 at 142,442. I read the cases as holding that the position advocated by the party seeking to amend the entitlement decision cannot demonstrate that it meets the lesser standard of law of the case, let alone the higher standard of *res judicata*. Even *American Asphalt, Inc.*, ASBCA No. 44160, 95-2 BCA ¶ 27,614, cited in the presiding judge's opinion, while discussing only law of the case standards, cites decisions holding that *res judicata* is the applicable standard, *e.g.*, *International Gunnery* and *Maitland Brothers*. Certainly, there is no ASBCA opinion expressly overruling the decisions applying *res judicata* in these circumstances.

Moreover, while the Federal Circuit has never addressed the issue of whether *res judicata* applies in a Board quantum proceeding, other circuits have applied the doctrines of *res judicata*, or claim preclusion, and issue preclusion, or collateral estoppel, in bifurcated

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[1] *Black River Limited Partnership v. West*, No. 98-1040 (Fed. Cir. Dec. 22, 1997).

[2] *Kos Kam* involved a motion for correction based on the existing record and *Control Data* involved a motion to reopen based on evidence found to be not available at time of trial.

proceedings. Under both, the matters decided in the initial phase may not be relitigated in the second phase. *See Greenleaf v. Garlock, Inc., et al.*, 174 F.3d 352, 357-671 (3d Cir. 1999); *John Morrell & Co. v. Local Union 304A*, 913 F.2d 544 (2d Cir. 1990), *cert. denied* 500 U.S. 905 (1991). Those cases rely on RESTATEMENT (SECOND) OF JUDGMENTS § 13 (1982), which opines at comment g, illustration 3, that disposition of liability is final in a bifurcated proceeding even though it is not immediately appealable.

The presiding judge's opinion relies on 18 WRIGHT-MILLER COOPER, FEDERAL PRACTICE & PROCEDURE § 4478 (1981 & 2001 Supp.) for the proposition that before final judgment a tribunal may reconsider issues previously decided. The cited authority is applicable only if the entitlement decision is not a final judgment and thus issue and claim preclusion do not apply. The only aspect of finality missing in a Board entitlement decision is that it is not *immediately* appealable. As the cited cases and the RESTATEMENT indicate, a liability judgment is final in a bifurcated proceeding and cannot be relitigated in the damages phase (or vice versa in *Greenleaf*). Finally, in discussing the expansion of *res judicata*, the Court in *Lummus Co. v. Commonwealth Oil Refining Co.*, 297 F.2d 80, 89 (2d. Cir 1961), *cert. denied* 368 U.S. 986 (1962), stated:

> Whether a judgment, not "final" in the sense of 28 U.S.C. § 2891, ought nevertheless be considered "final" in the sense of precluding further litigation of the same issue, turns upon such factors as the nature of the decision (i.e., that it was not avowedly tentative), the adequacy of the hearing, and the opportunity for review. "Finality" in the context here relevant may mean little more than that the litigation of a particular issue has reached such a stage that a court sees no really good reason for permitting it to be litigated again.

Our decisions have effectively held that such a stage is reached on entitlement issues upon ASBCA disposition of that phase of the appeal. If we are to rewrite *Black River I*, I think we would have to expressly overturn past Board precedent, which I am not prepared to do.

CARROLL C. DICUS, JR.
Administrative Judge
Acting Vice Chairman
Armed Services Board
of Contract Appeals

CONCURRING OPINION BY ADMINISTRATIVE JUDGE STEMPLER

I concur in result only. I concur with Judge Dicus' concurring opinion

MARK N. STEMPLER
Administrative Judge
Acting 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. 51754, Appeal of Black River Limited Partnership, rendered in conformance with the Board's Charter.

Dated:

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