ARMED SERVICES BOARD OF CONTRACT APPEALS

Appeals of --	)	
	)	
Lockheed Martin Corporation, Naval Electronics & Surveillance Systems - Surface Systems	)	ASBCA Nos. 53032, 54064
	)	
Under Contract No. N00024-88-C-5175	)	

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OPINION BY ADMINISTRATIVE JUDGE TING

Lockheed Martin Corporation, Naval Electronics & Surveillance Systems - Surface Systems'[1] (Lockheed Martin) Cost Plus Fixed Fee (CPFF) contract to qualify Unisys

[1] Lockheed Martin Corporation, Naval Electronics & Surveillance Systems - Surface Systems was formerly Lockheed Martin Government Electronic Systems. Some of the companies involved in these appeals have changed their identities over the years as a result of mergers and acquisitions. A footnote in one of Lockheed Martin's letters is helpful in identifying the companies' prior identities. This footnote explains: "Lockheed Martin Government Electronic Systems (GES) was formerly RCA, General Electric (GE), and Martin Marietta prior to becoming Lockheed Martin GES. Loral was formerly Sperry, Unisys, Loral, Paramax, Loral, and Lockheed Martin Tactical Defense Systems prior to becoming part of Lockheed Martin GES. Westinghouse is now Northrop Grumman." (R4, tab 60 at n.1) Raytheon Company's identity has not changed. Even though the correspondence in the record refers to the companies in their then-current identities, to avoid

Corporation (Unisys) and Westinghouse Electric Corporation (Westinghouse) as second source producers of the AEGIS AN/SPY-1D antenna and the AN/SPY-1D transmitter was terminated for convenience. Lockheed Martin appealed from a Termination Contracting Officer's (TCO) final decision unilaterally determining a net payment due based on her determination that subcontract effort must be excluded from Lockheed Martin's termination settlement proposal in computing the prime contractor's fee. Lockheed Martin seeks $9,571,258, and alternatively $5,524,466, under two separate theories of recovery. These appeals present the question of whether under the applicable contract clause and regulation costs relating to subcontract effort must be excluded as part of the base for determining prime contractor fee. Secondarily, we determine whether the TCO improperly disallowed a part of the antenna subcontractor's gross settlement and thereby improperly reduced the amount Lockheed Martin was entitled to recover as its gross settlement with the Government.

We decide entitlement and quantum.

FINDINGS OF FACT

Background

1. The AEGIS Weapon System is the heart of the AEGIS Combat System and is comprised of nine subsystems: (1) the AN/SPY-1 Radar System; (2) the Command and Decision System; (3) the Weapons Control System; (4) the Guided Missile Launching System; (5) the Fire-Control System; (6) the Standard Missile; (7) the Operational Readiness Test System; (8) the AEGIS Display Group; and (9) the AEGIS Combat Training System. The Fire-Control System and the AN/SPY-1 Radar System represent roughly 95 percent of the total AEGIS Weapon System cost. (R4, tab 209 at W-001596)

2. The SPY-1 Radar consists of the (1) Transmitter Group, (2) Signal Processor, and (3) Antenna. The primary function of the SPY-1 Radar is to search, detect, and track air and surface targets in heavy clutter and electronic countermeasure environments. The SPY-1 Radar uses phased array (rather than conventional rotating) antennas, which allow instantaneous electronic-beam steering. Radio Frequency (RF) energy is supplied by the SPY-1 Transmitter, with the Signal Processor cabinets interfacing the radar-controlled computer with the Antenna and Transmitter Group. (R4, tab 209 at W-001597)

3. In July 1987, in response to a request from the Assistant Secretary of the Navy, the Naval Center for Cost Analysis forwarded a study entitled "ANALYSIS OF

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confusion, we refer to the five companies involved in these appeals as Lockheed Martin (the prime contractor); Unisys (the first-tier antenna subcontractor); Westinghouse (the second-tier antenna subcontractor); Raytheon (the first-tier transmitter subcontractor); and Unisys (the second-tier transmitter subcontractor).

COMPETITIVE PROCUREMENT OF THE AEGIS WEAPON SYSTEM." The study identified the conditions under which second-sourcing of high-dollar value components of the AEGIS Weapon System would lead to savings, and estimated the magnitude of the savings achievable. (R4, tab 209 at W-001591-99) The study covered the Director/Controller and the Continuous Wave Illuminator (CWI) Transmitter components of the Fire-Control System and the Transmitter Group, the Signal Processor, and the Antenna components of the SPY-1 Radar. (R4, tab 209 at W-001596)

4. With respect to the SPY-1 Transmitter (transmitter), the study found that the Equipment Division of Raytheon Company (Raytheon) had been the sole-source producer (R4, tab 209 at W-001605). With respect to the SPY-1 Antenna, the study found that RCA had been the sole-source producer (R4, tab 209 at W-001610).

5. The study identified Unisys as the potential second-source for the AEGIS Weapon System. Westinghouse was identified as the second source for the SPY-1 Antenna. (R4, tab 209 at W-001613)

6. On the SPY-1 Radar System, the study estimated that with competition starting in FY 1989, competitive procurement could save the Navy $12 million on the transmitter and $75 million on the antenna through FY 2000 (R4, tab 209 at W-001615).

7. In attempting to create second sources for the AEGIS Weapon System components, the Navy began with the much simpler Fire-Control System (tr. 335-36). It used the Leader company contracting approach. In that case, Raytheon was the leader of the Fire-Control transmitter, and Lockheed Martin was the leader of the missile director. Unisys was the follower on both components. (Tr. 579-80) The entire knowledge transfer of the Fire-Control transmitter and director took approximately 18 months (tr. 580-81).

8. The Navy went through many changes in structuring the AEGIS Second Source Radar Qualification Program. At one point, the Navy considered being the "focal point" of knowledge transfer between the Original Equipment Manufacturer (OEM) of Lockheed Martin and Raytheon as Team A, and Unisys and Westinghouse as Team B. (Tr. 47) The Navy rejected this approach because it did not have the resources or the actual knowledge of production to competently qualify a second source (tr. 522). The Navy, in partnership with Lockheed Martin, ultimately decided to use the Leader company approach (tr. 525).

9. FAR Part 17 deals with "SPECIAL CONTRACTING METHODS." Subpart 17.4 deals with "LEADER COMPANY CONTRACTING." The concept of Leader company contracting is explained in FAR 17.401:

> Leader company contracting is an extraordinary acquisition technique that is limited to special circumstances and utilized only when its use is in accordance with agency

procedures. A developer or sole producer of a product or system is designated under this acquisition technique to be the leader company, and to furnish assistance and know-how under an approved contract to one or more designated follower companies, so they can become a source of supply.

10. FAR 17.402 **Limitations** provides:

(a) Leader company contracting is to be used only when--

(1) The leader company has the necessary production know-how and is able to furnish required assistance to the follower(s);

(2) No other source can meet the Government's requirements without the assistance of a leader company;

(3) The assistance required of the leader company is limited to that which is essential to enable the follower(s) to produce the items; and

(4) Its use is authorized in accordance with agency procedures.

11. FAR 17.403 **Procedures** provides:

(a) The contracting officer may award a prime contract to a--

(1) Leader company, obligating it to subcontract a designated portion of the required end items to a specified follower company and to assist it to produce the required end items . . . .

The Prime Contract

12. On 30 March 1988, the Naval Sea Systems Command (NAVSEA) entered into a letter contract (No. N00024-88-C-5175) (the 5175 Contract or the prime contract) with Lockheed Martin, known at that time as RCA Electronic Systems Department, a component of General Electric Company. The letter contract was in the amount of $19,161,500. (R4, tab 213 at C-012204)

13. Crafting the terms of the prime contract was a collaborative effort between NAVSEA and Lockheed Martin. While the Navy "put in all of the standard clauses," Lockheed Martin was responsible for defining the various reports or data items required to be generated. (Tr. 48) The letter contract contemplated subsequent definitization into a CPFF contract. If agreement on a definitized contract could not be reached, the contracting officer could determine a reasonable price, and the contractor could appeal pursuant to the Disputes clause. (*See* SP H-2, FAR 52.216-25, CONTRACT DEFINITIZATION (APR 1984), R4, tab 213 at C-012217)

14. SECTION B - SUPPLIES/SERVICES AND PRICES of the prime contract set out the Contract Line Items (CLINs) of the contract. CLIN 0001 was for "Second Source Manufacturer Qualification Program Planning;" CLIN 0001AA was for "Second Source Transmitter Qualification;" CLIN 0001AB was for "Second Source Antenna Qualification;" CLIN 0003 was for one face of "Antenna Phased Array Assembly;" CLIN 0004 was for one string of "Transmitter Group;" and CLIN 0007 was for "Data" for CLINs 0001 through 0004 and CLIN 0008. CLIN 0007 referred to the DD Form 1423s attached to the contract as Exhibit A. The price for CLIN 0007 was required to be included in CLINs 0001 through 0005, 0008 and 0009. (R4, tab 213 at C-012205)

15. SPECIAL PROVISION (SP) H-27, SUBCONTRACT RESPONSIBILITY, directed that Lockheed Martin award a Firm Fixed-Price (FFP) antenna subcontract to Unisys. It also directed that Unisys award a lower-tier FFP subcontract to Westinghouse. SP H-27 directed that a CPFF subcontract be awarded to Raytheon to assume the leader role on the transmitter. It was also directed that Raytheon award the lower-tier FFP transmitter subcontract to Unisys. (R4, tab 213 at C-012228)

16. SECTION C - DESCRIPTION/SPECIFICATIONS of the letter contract defined Phase I work to include CLIN 0001 (Second Source Manufacturer Qualification Program Planning) and applicable data from CLIN 0007. CLIN 0001 work was further specified as follows:

> 1.0 The Contractor shall provide to the Second Source Subcontractor a Technical Data Package (TDP) as required to permit the Second Source Subcontractor to analyze and plan in detail for the manufacture of the elements of the OT-146/SPY-1D Transmitter Group and the AS-3851/SPY-1D Antenna listed herein. . . .
>
> 2.0 The Contractor and its leader subcontractor, Raytheon, shall require the Second Source Subcontractor to conduct detailed analyses of the Technical Data Package and other referenced data, to develop and to document appropriate planning and to submit its plans for review and comment to the

> Contractor. The Contractor shall provide a copy of all second source submitted plans, as detailed below to the Government (PMS 400G). All data deliveries are to be in accordance with Exhibit A. The required studies and plans listed below are defined in more detail in Attachment A and Exhibit A.

The second source submitted plans included (1) Producibility Study, (2) Production Plan, (3) Reliability and Maintainability Program Plan, (4) Standardization Program Plan, (5) Safety Program Plan, (6) Configuration Management Plan, (7) Quality Assurance Plan, and (8) Integrated Logistics Support Plan. (R4, tab 213 at C-012208-209)

17. SECTION C defined Phase II work to include CLINs 0002, 0003, 0004, 0006, 0007, 0008, and if options were exercised, 0005 and 0009[2]. Under CLIN 0003, Lockheed Martin was required to provide the demonstration antenna and transmitter (R4, tab 213 at C-012210-211). In connection with CLIN 0007, Phase II required that "[t]he Data to be furnished hereunder shall be prepared in accordance with the Contract Data Requirements List, DD Form 1423, Exhibit A attached hereto" (R4, tab 213 at C-012212).

18. It was the Government's intent that the basic transfer of know-how would occur during Phase I (tr. 531). Learning from the prior Fire-Control Second Source Qualification Program, the Navy wanted to make sure that the followers understood the technical requirements before they ordered materials and began assembling the demonstration hardware. (Tr. 530, 548) As planned, Phase I would be complete six months after contract award (*see* SECTION F, R4, tab 213 at C-012213).

19. SECTION I of the letter contract, GENERAL PROVISIONS, incorporated by reference, FAR 52.212-13 STOP-WORK ORDER (APR 1984) - ALTERNATE I (APR 1984); FAR 52.233-1 DISPUTES (APR 1984); and FAR 52.249-6 TERMINATION (COST REIMBURSEMENT) (MAY 1986), among others (R4, tab 213 at C-012238-241).

20. FAR 52.249-6 TERMINATION (COST-REIMBURSEMENT) (MAY 1986) provides as follows:

> (a) The Government may terminate performance of work under this contract in whole or, from time to time, in part, if--
>
> (1) The Contracting Officer determines that a termination is in the Government's interest;

[2] CLIN 0005 is an unpriced option relating to Signal Processor Group, OL-356/SPY-1D; CLIN 0009 is an option for Verification Testing of Qualification Equipment (R4, tab 213 at C-012205).

. . . .

(c) After receipt of a Notice of Termination, and except as directed by the Contracting Officer, the Contractor shall immediately proceed with the following obligations . . . :

. . . .

(5) With approval or ratification to the extent required by the Contracting Officer, settle all outstanding liabilities and termination settlement proposals arising from the termination of subcontracts, the cost of which would be reimbursable in whole or in part, under this contract; approval or ratification will be final for purposes of this clause.

. . . .

(e) After termination, the Contractor shall submit a final termination settlement proposal to the Contracting Officer in the form and with the certification prescribed by the Contracting Officer. . . .

(f) Subject to paragraph (e) above, the Contractor and the Contracting Officer may agree on the whole or any part of the amount to be paid (including an allowance for fee) because of the termination. The contract shall be amended, and the Contractor paid the agreed amount.

(g) If the Contractor and the Contracting Officer fail to agree in whole or in part on the amount of costs and/or fee to be paid because of the termination of work, the Contracting Officer shall determine, on the basis of information available, the amount, if any, due the Contractor, and shall pay that amount, which shall include the following:

. . . .

(4) A portion of the fee payable under the contract, determined as follows:

. . . .

> (i) If the contract is terminated for the convenience of the Government, the settlement shall include a percentage of the fee equal to the percentage of completion of work contemplated under the contract, *but excluding subcontract effort included in subcontractors' termination proposals*, less previous payments for fee.
>
> . . . .
>
> (i) The Contractor shall have the right of appeal, under the Disputes clause, from any determination made by the Contracting Officer under paragraph (e) or (g) above or paragraph (k) below, except that if the Contractor failed to submit the termination settlement proposal within the time provided in paragraph (e) . . . .

(Emphasis added) Thus, a contractor has a right to appeal its disagreement with the contracting officer under (g), but not what has been agreed to under (f).

21. SECTION J contained LISTS OF DOCUMENTS, EXHIBITS, AND OTHER ATTACHMENTS which formed a part of the letter contract. Attachment A pertained to "Production Deliverables and Management Support Responsibilities of the Contractor," and had eight subparts: Attachments A1 - A8. (R4, tab 213 at C-012260)

22. Attachment A6 set out the major performance milestones of the AEGIS Second Source Qualification Program. Among the milestones listed were Producibility Study Review, Preliminary Manufacturing Readiness Review (PMRR), Critical Manufacturing Readiness Review (CMRR), and Mission Readiness Review Board Event. (R4, tab 213 at C-012340-341)

23. During Phase I, each follower was required to conduct a producibility study and to submit a report of its findings (R4, tab 213 at C-012310, attach. A, ¶ 3.7). This study was a precursor to the PMRR and CMRR milestones, and was to assure the leaders that the followers understood the TDP and what needed to be done to become a viable second source (tr. 61, 129).

24. The PMRR, also a Phase I event, was actually a meeting required to be held at the second source subcontractor's facility. A long list of topics would be reviewed by the leaders. (R4, tab 213 at C-012308, attach. A, ¶ 3.5.1) The PMRR was used to identify any problems that would cause delays and disruptions to the assembly or manufacture of the

demonstration antenna and transmitter (tr. 148). It is a tool used in major programs to mitigate risk (tr. 686-87).

25. The CMRR was a Phase II milestone. It too required a meeting at the second source subcontractor's facility. It too required review of a long list of topics. (R4, tab 213 at C-012309, attach. A, ¶ 3.5.2). By the time the CMRR took place, the second source subcontractors were supposed to have corrected the documentation and planning problems uncovered at the PMRR (tr. 543-44). The purpose of the CMRR was to ensure that the followers had acquired enough understanding of the antenna and transmitter before embarking on the more expensive part of the program relating to the procurement of materials and starting assembly. The CMRR too, is a risk reduction management tool. (Tr. 591-93)

26. Before a follower was qualified as a second source, it had to make a presentation to the Mission Review Board (MRB). At this event, the follower's entire performance would be reviewed to ensure it had completed all of the contract requirements and had the necessary organization, support infrastructure, logistics, configuration management and quality programs to become a second source competitor. (Tr. 117-18)

Prime Contract Data Requirement

27. As noted previously, CLIN 0007 of the letter contract required Data for CLINs 0001 through 0004, 0008, and if options were exercised, CLINs 0005 and 0009, and referred to the DD Form 1423s attached to the contract as Exhibit A (R4, tab 213 at C-012205). Paragraph 1.2.2, "Contract Data Requirements List (CDRL)" provided that "[t]he Contractor shall deliver all the CDRL Items in accordance with Exhibit A" (R4, tab 213 at C-012296).

28. Attached as Exhibit A of the letter contract were 20 pages of DD Form 1423s specifying 35 separate CDRLs or "data" Lockheed Martin was expected to deliver to NAVSEA (R4, tab 213 at C-012261). Among the CDRLs required to be delivered were COST/SCHEDULE STATUS REPORT (VARIANCE ANALYSIS REPORT), CDRL A007, and COST PERFORMANCE REPORT, CDRL A009. Both of these reports were required to be submitted to NAVSEA monthly. (R4, tab 213 at C-012264-265)

The "Flow Down" Requirement

29. Under the contract Statement of Work (SOW), the Contractor was required to "incorporate into the directed subcontracts the applicable sections of this SOW, suitably modified" (R4, tab 213 at C-012208). One of the items of the SOW was "ITEM 0007," which provided that "[t]he Data to be furnished hereunder shall be prepared in accordance with the Contract Data Requirements List, DD Form 1423, Exhibit A attached hereto" (R4, tab 213 at C-012212).

Special Provision (SP) H-36

30. SP H-36, EXCLUSION FROM CONTRACTOR FEE, provides:

> The Contractor shall exclude from this contract any consideration for Contractor fee *solely on the initial definitized price of the Subcontracts* placed with UNISYS hereunder for the second source qualification program.

(R4, tab 213 at C-012232; emphasis added)

31. Prior to initiating the AEGIS Second Source Radar Qualification Program, "[v]ery vigorous, robust" and "intense" discussions took place between the Navy and Lockheed Martin. Lockheed Martin opposed the program in principle, but understood the Navy had to execute its plan. (Tr. 975)

32. Several alternative plans were developed to implement the program (tr. 973). In September 1987, Lockheed Martin made a presentation to the Navy (tr. 975). A briefing chart which was a part of the presentation materials contained the following points:

? LEADER/FOLLOWER CONTRACT

? CPFF

? NO LEADER PROFIT ON UNISYS CONTRACTS

(R4, tab 167 at 25) Following this presentation, NAVSEA issued a Request for Proposal to Lockheed Martin by letter dated 29 September 1987 (R4, tab 166).

33. Douglas C. Levitas, Procuring Contracting Officer of the AEGIS second source contract at the time (PCO Levitas) explained that SP H-36 operated "to eliminate from the prime-contractor's cost base, from which fee would be determined, the cost of both pieces of the Unisys-follower subcontractor effort. Once that was eliminated, the fee was then determined on the prime-contract amount" (tr. 965).

34. To support his position that Lockheed Martin interpreted SP H-36 the same way, PCO Levitas referred to his Business Clearance Memorandum (BCM) of 3 February 1988. Attached to this BCM is a Proposal Summary submitted by Lockheed Martin. Attachment 5 of the Proposal Summary is a Lockheed Martin document entitled "FORWARD PRICED SCHEDULE" for Phase I from its 13 January 1988 proposal. (R4, tab 168 at attach. 5; tr. 966)

35. Attachment 5 shows that, in calculating its fixed fee at 10 percent, Lockheed Martin deducted from its costs ($18,280,045), Unisys' costs for both the antenna ($6,319,061) and the transmitter ($4,593,271). As shown by the following footnote computation, Lockheed Martin calculated its fee strictly from its costs less Unisys' costs:

**TOTAL RCA COST (LESS COM)	18,280,045
LESS UNISYS COST-ANTENNA	(6,319,061)
LESS UNISYS COST-TRANSMITTER	(4,593,271)
TOTAL RCA COST (LESS UNISYS COST)	7,367,713
FIXED FEE @ 10.0%	736,771

(R4, tab 168 at attach. 5) According to PCO Levitas, this calculation from Lockheed Martin was totally consistent with what SP H-36 provided with respect to eliminating from Lockheed Martin's cost base, from which fee would be determined, the costs of all Unisys subcontractor effort (tr. 968).

36. When asked what the exclusion limitation of "solely on the initial definitized price of the subcontracts" referred to, PCO Levitas explained that the phrase was inserted as a compromise during negotiations so that the exclusion would not apply "if there were any major modifications issued after this contract" (tr. 977-78). He agreed that the reference to "definitized price of the subcontract" meant that Lockheed Martin would not get fee on the Schedule (Section) B prices in the subcontracts, and once that was accomplished, SP H-36 had no other application (tr. 982). PCO Levitas did not recall discussing or negotiating with Lockheed Martin whether SP H-36 would apply in a termination for convenience situation (tr. 984).

First-Tier Antenna Subcontract Between Lockheed Martin and Unisys

37. Pursuant to its prime contract with NAVSEA, Lockheed Martin issued Purchase Order No. 672D123059 to Unisys on 15 April 1988 for work on the second source qualification of the AEGIS antenna (R4, tab 215 at C-000285). The definitized price of the Lockheed Martin/Unisys antenna subcontract was $38,019,500 (*id.* at C-000293).

38. Because it was a FFP contract, the Lockheed Martin/Unisys first-tier antenna subcontract included a termination for convenience clause for fixed-price contracts. Supplement A, RCA [Lockheed Martin] 656 (3-87), Clause 3, Termination, provided:

> . . . The clause entitled "Termination for the Convenience of the Government (Fixed-Price)" set forth in FAR Section 52.249-2 [(APR 1984)] is made a part hereof, but the title is changed to "Termination"; "Government" and "Contracting Officer" mean "RCA [Lockheed Martin]"; paragraph (c) is deleted; in paragraph (d) "1 year" at each appearance is changed to "6

> months"; and on paragraph (k) "90 days" is changed to "45 days." Nothing in that clause, however, shall affect or limit the rights of RCA [Lockheed Martin] under any other provision of this Purchase Order or provided by law in the event of default or breach by Seller.

(R4, tab 215 at C-000334, 336)

39. SECTION B, SUPPLIES OR SERVICES of the Lockheed Martin/Unisys antenna subcontract included nine CLINs. CLIN 0001 through CLIN 0004 were priced as follows:

Item	Supplies/Services	FFP
0001	Second Source Manufacturer Qualification Program Planning	$ 6,215,394.00
0002	Data and Documentation for Item 0001 (see SOW TB-1301, Attachment 4)	$ 188,372.00
0003	Antenna, Phased Array Assembly (one face)	$31,430,459.00
0004	Data and Documentation for Item 0003 (see SOW TB-1301, Attachment 4)	$ 185,275.00

(R4, tab 215 at C-000293)

40. SECTION C - DESCRIPTION/SPECIFICATIONS/STATEMENT OF WORK of the Lockheed Martin/Unisys antenna subcontract defined Phase I to include CLIN 0001 (Second Source Manufacturer Qualification Program Planning) and CLIN 0002 (Data and Documentation for CLIN 0001). Phase II was defined to include CLINs 0003, 0004 and 0005, and other CLINs if the option for them was exercised. Paragraph 2.0 of Item 0001 stated that "[a]uthorization to proceed with Phase II is not to be contingent upon satisfactory completion of Phase I." Item 0004 required the Data and Documentation required to be furnished under CLIN 0004 to be "prepared and submitted in accordance with the Subcontract Data Requirements List DD Form 1423 as set forth in Attachment 4 of SOW TB 1301." (R4, tab 215 at C-000295-297)

41. SECTION F - DELIVERIES AND PERFORMANCE of the Lockheed Martin/Unisys antenna subcontract required Phase I to be completed within seven months after subcontract award. For the antenna assembly (CLIN 0003), delivery was required "36 months ARO [After Receipt of Order]," and major performance milestones were required to be accomplished in accordance with Attachment 1 of SOW TB-1301. Data and

documentation were required to be delivered at times specified in Attachment 4 of SOW TB-1301. (R4, tab 215 at C-000300)

42. As in the prime contract, the Lockheed Martin/Unisys antenna subcontract contains a SECTION H, but it is entitled "SPECIAL SUBCONTRACT PROVISIONS/REQUIREMENTS." SP H-19 of the prime contract, "AEGIS SECOND SOURCE WORK BREAKDOWN STRUCTURE," was "flowed down" as SP H-34, "AEGIS WEAPON SYSTEM PRODUCTION WORK BREAKDOWN STRUCTURE" in the Lockheed Martin/Unisys subcontract. This provision required Unisys to collect costs under its contract in accordance with the WBS set forth in Attachment 3. (R4, tab 215 at C-000302, 322)

43. In addition, SOW TB-1301 required Unisys to deliver all SDRL (Subcontract Data Requirements List) items in accordance with Attachment 4 (R4, tab 215 at C-000369, ¶ 1.2.6). Unisys was required to submit to Lockheed Martin "the current cost and current and projected budget information in accordance with the established WBS on the Cost Performance Report, SDRL E001 . . . at the WBS designated levels. Cost of Work Data report, SDRL E002, and Variance Analysis Report, SDRL E004, shall also be provided" (R4, tab 215 at C-000368, ¶ 1.2.4.2).

44. Attachment 4 of SOW TB-1301 listed the SDRLs required for Phase I and Phase II. Phase I required 28 SDRLs; Phase II 50. Some SDRLs, such as the Cost Performance Reports (E001), the Cost of Work Data (E002), the Variance Analysis Report (E004), and Network, Diagram/Gantt Charts (E005), were required to be submitted during Phase I and continuing through Phase II (R4, tab 215 at C-000409-413). Others were uniquely Phase II deliverables, such as Test Procedures (E036), Test Reports (E037) and Material Specifications (E058) (R4, tab 215 at C-000412-413).

Second-Tier Antenna Subcontract between Unisys And Westinghouse

45. On 21 April 1988, Unisys issued Purchase Order No. SW 12001-HM to Westinghouse. This purchase order, in the amount of $4,057,040.00, was initially for two items only. Item No. 1 was for "AEGIS Second Source Manufacturer Qualification Program Planning (Phase I) in accordance with conditions set forth in Section B items 0001 and 0002." Item No. 2 was for "Data and Documentation for Item 1 in accordance with SDRL List Attachment 4 to SOW-TB-1301." (R4, tab 216 at C-000565)

46. Westinghouse's prices for CLIN 0001 through CLIN 0004, as shown in SECTION B, were as follows:

Item	Supplies/Services	Firm Fixed-Price
0001	Second Source Manufacturer Qualification Program Planning	$ 3,984,261

0001AA	. . . .	
0002	Data and Documentation for Item 0001 (see SOW TB-1301, Attachment 4)	$ 72,739
0003	Antenna, Phased Array Assembly (one face)	$22,604,103
0003AA	. . . .	
0004	Data and Documentation for Item 0003 (see SOW TB-1301, Attachment 4)	$ 338,897

The Unisys/Westinghouse antenna subcontract was definitized at $27,000,000 (R4, tab 216 at C-000664).

47. Because the Unisys/Westinghouse second-tier antenna subcontract was a FFP contract, it contained the termination for convenience clause for fixed-price contracts. Section I - GENERAL PROVISIONS, Clause 24, TERMINATION, provided:

> The clause entitled "Termination for Convenience of the Government" set forth in . . . FAR 52.249-2 [(APR 1984)] . . . and any successor clause is hereby incorporated herein except that the references to Government and Contracting Officer, where applicable, shall be references to Sperry [Unisys] . . . .

(R4, tab 216 at C-000637)

48. The Unisys/Westinghouse antenna purchase order required Phase I to be completed within seven months after subcontract award, the antenna assembly to be delivered "36 months ARO," and the "Data and Documentation shall be delivered at time specified in Attachment 4 SOW-TB1301" (R4, tab 216 at C-000666).

49. Flowed down as a part of SECTION H - SPECIAL PURCHASE ORDER PROVISIONS/REQUIREMENTS was SP H-34, AEGIS WEAPON SYSTEM PRODUCTION WORK BREAKDOWN STRUCTURE, which required Westinghouse to collect costs under the contract in accordance with the WBS set forth in the SOW at Attachment 3 (R4, tab 215 at C-000605), and SP H-56, SUBCONTRACT DATA REQUIREMENTS LISTS (SDRL) which required Westinghouse to "deliver all reports and other data set forth in the 'SDRL' DD Form 1423. . ." (R4, tab 216 at C-000615).

50. On 2 August 1988, Unisys issued Change Order No. 1 to its subcontract with Westinghouse. This change increased the Government's liability to $4,932,209.00. (R4, tab 215 at C-000652) On 24 March 1989, Unisys issued Change Order No. 2. This change order, among other things, provided authorization to proceed with CLINs 0003 and 0004 (Phase II), and established a firm fixed-price of $27,000,000.00 for CLINs 0001 through 0004 (R4, tab 216 at C-000660).

First-Tier Transmitter Subcontract Between Lockheed Martin and Raytheon

51. On 14 April 1988, Lockheed Martin issued Purchase Order No. 672E123061 to Raytheon Company (Raytheon) for the transmitter. SECTION I - SUPPLIES AND SERVICES, included nine CLINs. The relevant CLINs are listed below:

ITEM No.	SUPPLIES/SERVICES
0001	Second Source Manufacturer Qualification Program Planning
0001AA	Raytheon Level of Effort
0001AB	Unisys Subcontract
. . . .	
0004	Transmitter Group, (one station) OT-146/SPY-1D
. . . .	
0007	Data for Items 0001, 0004, 0008 and 0009 (See Exhibits A and A1, attached hereto)

(R4, tab 214 at C-000992, 996)

52. The UNIT PRICE column of CLIN 0007 provided "NSP - Price to be included in price of Items 0001, 0004, 0008 and 0009" (R4, tab 214 at C-000996). The Raytheon transmitter subcontract's estimated cost plus fixed fee after definitization was $49,715,065 (*id.* at C-001278).

53. Because the Lockheed Martin/Raytheon first-tier transmitter subcontract was a CPFF contract, Supplement CR of the subcontract contained Paragraph 32, Termination, which provided:

> The clause set forth in FAR 52.249-6 [TERMINATION (COST-REIMBURSEMENT) (MAY 1986)] is made a part hereof . . . .

(R4, tab 214 at C-001075)

54. SECTION V - DELIVERIES OR PERFORMANCE, required Raytheon to provide the effort set out in Item 0001 of Section I (Second Source Manufacturer Qualification Program Planning) within six months after subcontract award. Data under Item 0007 were required to be delivered to destinations and at the times specified in Exhibits A and A1. (R4, tab 214 at C-001003)

55. SECTION VI - SPECIAL PROVISIONS, included a number of provisions "flowed down" from the prime contract, among them, Provision 40, "AEGIS WEAPON SYSTEM WORK BREAKDOWN STRUCTURE" which required Raytheon to collect costs under its contract in accordance with the WBS set forth in Raytheon's proposal and Attachment E (R4, tab 214 at C-001025).

56. Attachment A6 of the Lockheed Martin/Raytheon subcontract set out the major performance milestones, including the Producibility Study Review, the PMRR, the CMRR, and the Mission Readiness Review Board Event (R4, tab 214 at C-001139-141).

57. The Lockheed Martin/Raytheon transmitter subcontract not only listed the SDRLs Raytheon was required to submit, but also the SDRLs Unisys, as the second tier subcontractor, was required to submit to Raytheon. Those SDRLs (G series) Unisys was required to submit to Raytheon were specified on the DD Form 1423s attached to the subcontract as Exhibit A. Those SDRLs (H series) Raytheon was required to submit to Lockheed Martin were specified on the DD Form 1423s attached to the subcontract as Exhibit A1. (R4, tab 214 at C-001161-210)

58. Examples of some of the 43 SDRLs Unisys was required to submit to Raytheon included: (1) Cost Performance Report (G001); (2) Cost of Work Data (G002); (3) Variance Analysis Report (G003); (4) Network Diagrams/Gantt Charts (G005); (5) Agenda, Program Meetings (G009); and (6) Presentation Material (G010) (R4, tab 214 at C-001164-189). Examples of some of the 14 SDRLs Raytheon was required to submit to Lockheed Martin included: (1) Cost Performance Report (H001); (2) Cost of Work Data (H002); (3) Variance Analysis Report (H003); (4) Network Diagram/Gantt Charts (H005); (5) Agenda, Program Meetings (H009); and (6) Presentation Material (H010) (R4, tab 214 at C-001198-206).

Second-Tier Transmitter Subcontract Between Raytheon and Unisys

59. On 29 April 1988, Unisys accepted Purchase Order No. 53-D570-EX-93000 issued by Raytheon on 8 March 1988 with certain modifications for the Not-To-Exceed price of $29,910,774 (R4, tab 217 at C-000731-739). Subsequently, Raytheon and Unisys negotiated a total FFP subcontract price of $30,238,000 (*id.* at C-000959). Of this amount, $4,138,000 was for Phase I work, and $26,100,000 for Phase II work (*id.* at C-0009700).

60. The Raytheon/Unisys transmitter subcontract contained a number of CLINs. CLINs 0001(a) and 0001(b) pertained to Phase I, and CLINs 0004 to 0012 pertained to Phase II. CLIN 0001(a) required Unisys to conduct a detailed analysis of the TDP and other referenced data in accordance with the SOW. CLIN 0001(b) required Unisys to develop, document and submit a number of specified Phase I plans for review, comment and approval. CLIN 0004 required Unisys to provide one string of the AEGIS Transmitter. CLIN 0007 required Unisys to prepare for submission, comments and approval the data and documentation required by the DD Form 1423s. (R4, tab 217 at C-000740-742)

61. The Raytheon/Unisys subcontract required CLINs 0001(a) and (b) to be completed within six months after receipt of the subcontract. It required CLIN 0004 to be delivered 31 months after release of Phase II. It also required the data under CLIN 0007 to be delivered at times specified in the DD Form 1423s. (R4, tab 217 at C-000746)

62. SECTION I, GENERAL PROVISIONS, of the Raytheon/Unisys subcontract incorporated by reference a number of FAR clauses, among them, FAR 52.212-13 STOP-WORK ORDER (APR 1984) - ALTERNATE I (APR 1984), and, since it was a FFP contract, FAR 52.249-2 TERMINATION FOR THE CONVENIENCE OF THE GOVERNMENT (FIXED-PRICE) (APR 1984) (R4, tab 217 at C-000772, 775).

63. SECTION H - SPECIAL PROVISIONS included H-19, AEGIS SECOND SOURCE WORK BREAKDOWN STRUCTURE, which required Unisys to collect costs under the subcontract in accordance with the WBS set forth in Attachment E (R4, tab 217 at C-000748, 757). Attachment E showed that for Phase II data, cost was required to be collected at Level 02, "Data," and at Level 03, "SDRL ITEMS" (R4, tab 217 at C-000915, fig. 1-L).

64. The SOW of the Raytheon/Unisys subcontract at Attachment A required Unisys to deliver all SDRL items in accordance with Exhibit A (¶ 1.2.2), and implement a Cost Control System designated in Attachment A8, through the period of subcontract performance employing MIL-STD-881A of 25 April 1975 ("Work Breakdown Structure for Defense Material Items") at Attachment E (¶ 3.3) (R4, tab 217 at C-000831, 839).

65. Attachment A6 of the Raytheon/Unisys subcontract identified as a part of the major performance milestones, Producibility Study Review, PMRR, CMRR, and Mission Readiness Review Board Event (R4, tab 217 at C-000886-888). Attached to Exhibit A1 were the same 43 SDRLs as contained in Exhibit A of the next higher tier Lockheed Martin/Raytheon transmitter subcontract (*id*. at C-000917-945).

66. The complex contractual relationship the various participants entered into to execute the Navy's AEGIS Second Source Radar Qualification Program is reflected in Exhibit 1001. To summarize, NAVSEA entered into a CPFF prime contract with Lockheed Martin. On the antenna side, Lockheed Martin, as the antenna leader, entered into a first-tier FFP subcontract with Unisys as the antenna follower. Unisys then entered into a second-tier FFP subcontract with Westinghouse, also an antenna follower. On the transmitter side, Lockheed Martin entered into a first-tier CPFF subcontract with Raytheon, the transmitter leader. Raytheon then entered into a second-tier FFP subcontract with Unisys as the transmitter follower. (Ex. 1001; tr. 54)

67. Under the contractual arrangement set up above, Lockheed Martin played two roles: as the prime contractor overseeing the entire AEGIS Second Source Radar Qualification Program for NAVSEA, and as leader of the antenna because it was its OEM. Since Raytheon was the OEM of the transmitter, it became the leader on the transmitter. Unisys also played two roles: as the follower of both the antenna and the transmitter, and as the team leader of Team B, consisting of itself and Westinghouse, which if qualified, would ultimately compete with Team A, consisting of Lockheed Martin and Raytheon.

68. Phase I was not completed until June 1989, 15 months after award of the 5175 Contract (tr. 281-82). On 14 December 1988, NAVSEA issued Modification No. P00003 authorizing Lockheed Martin to proceed with Phase II (R4, tab 213 at C-012368-369; tr. 1304). Because a funding problem was not cleared up until late January 1989 however, Phase II did not officially begin until 1 February 1989 (tr. 1334). For about six months, Phase I and Phase II ran concurrently (tr. 60-61, 1305).

Definitization Not Accomplished

69. By letter dated 30 May 1989 to NAVSEA, Lockheed Martin confirmed the parties' agreement reached on 24 May 1989 to definitize the 5175 Contract as follows:

Estimated Cost	$109,670,200
Cost of Money	800,000
Fixed Fee	3,729,800
	$114,200,000

(R4, tab 171). According to Daniel B. Lear, the PCO who negotiated the definitized amount (PCO Lear), the $3,729,800 fee was derived "utilizing H-36," without including the Unisys

subcontracts in the fee base (tr. 999-1000). PCO Lear testified that Lockheed Martin's proposal came in applying SP H-36, and there was no issue on "whether . . . the Unisys-directed subcontract costs would be removed in calculating the fee" (tr. 1001).

70. Subsequent to its 30 May 1989 confirmation letter, Lockheed Martin forwarded its Certificate of Current Cost and Pricing Data. PCO Lear then wrote a post-negotiation BCM which was approved by the Assistant Secretary of the Navy. In July 1989, PCO Lear forwarded to Lockheed Martin a modification which incorporated the terms of the agreement reached on 24 May 1989. (Tr. 1001)

71. In a letter dated 2 March 1990, less than a month prior to issuance of the Stop Work Order, Lockheed Martin advised NAVSEA that the negotiated agreement reached on 24 May 1989 "has not been definitized primarily because of the Navy's continuing review[[3]]" (ex. 2000). According to PCO Lear, "there was never any issue with either the cost or fee that had been negotiated" (tr. 1002). The parties' 24 May 1989 agreement to definitize the letter contract was never formally finalized by way of a bilateral modification.

Termination For Convenience

72. On 30 March 1990, NAVSEA's CO issued Modification No. P00016. It directed Lockheed Martin and its subcontractors to stop work to the degree specifically directed effective 30 March 1990. As a part of the Stop Work Order, Lockheed Martin was instructed to prepare an assessment of the completion status of each CLIN, and of the cost of completing each CLIN. The assessment report was required to be submitted to the CO not later than 30 days from 30 March 1990. (R4, tab 17)

73. When the Stop Work Order was issued, Unisys and Westinghouse had just received materials and were in the process of providing them to the technicians on the assembly floor to begin assembling the antenna (tr. 554).

74. Lockheed Martin's Final Program Assessment Report, dated 30 April 1990, provided the following assessment on the antenna:

> As a general assessment of the critical assemblies (parts) we estimate that 15% of the Phase Shifters and 20% of the Combiners have been assembled with an additional 35% of the Phase Shifters and 50% of the Combiners in some phase of assembly. Without Navy approval of RFD/W4-0011-R3 for

[3] In late Summer of 1989, there were on-going discussions within the Navy on whether the program would ever be cost-beneficial, and whether the 5175 Contract should be terminated. Also, there were questions on whether Unisys was linked to the Ill-Wind investigations. (Tr. 1005)

> the use of Dupont gold paste, none of the ISEM's [Improved Standard Electronic Module] built under the Navy to Westinghouse Standard Test Equipment (STE) contract are usable, and no ISEM's have been built on the qualification contract. The completed power supply prototype has yet to be tested, and none of the 31 production units have been started. None of the critical assemblies built to date have been tested to Attachment 8 or Attachment 13 of SOW-TB-1301 of our P.O. 672D123059, nor has DCAS approved any of them.
>
> The task team strongly recommends that the Unisys/WEC critical assemblies not be accepted for use on GESD [Lockheed Martin] AEGIS production programs, or by GESD [Lockheed Martin] to complete the array face for the 5175 contract.

(R4, tab 190 at AP-000006)

75. With respect to the CDRL data Lockheed Martin was required to furnish to NAVSEA, Lockheed Martin reported:

> This CLIN was not separately priced. The costs associated with this CLIN are included in CLINs 0001 through 0004, 0008, and 0009. All CDRL Plans were initially submitted December 1988 and were in process of revision.

(R4, tab 190 at AP-000007) Because Unisys did not submit an assessment report, Lockheed Martin did not provide an assessment of the SDRL data items delivered by Unisys and Westinghouse on the antenna.

76. Lockheed Martin's 30 April 1990 assessment report also attached Raytheon's preliminary assessment on the transmitter (R4, tab 190 at AP-000244). It stated:

> The SPY-1D transmitter assemblies built to date by Unisys are an unknown entity when compared to current production hardware. It is not recommended that the Unisys subassemblies be used on the AEGIS Production Program.

(R4, tab 182 at TP-006780)

77. According to NAVSEA's Second Source Qualification Officer, at the time the Stop Work Order was issued, Phase II was "about 10 percent, maybe 15 percent" complete (tr. 575), and Lockheed Martin was about six months late on the entire project (tr. 557).

The parties have not provided an assessment of the overall percentage of completion based on both phases. The record does not reflect that percentage of completion of the entire contract was used as a basis for settlement in the termination settlement discussions.

78. With respect to the transmitter SDRLs it had to furnish to Lockheed Martin, and the SDRLs its subcontractor Unisys had to furnish, Raytheon provided the following assessment:

> Raytheon SDRL Status:
>
> | | |
> |---|---|
> | 10 | Complete & Approved |
> | 2 | Continuing (ie updates) |
> | 2 | Requiring GESD [Lockheed Martin] Approval |
> | 43[4] | Total Raytheon data items |
>
> Unisys SDRL Status:
>
> | | |
> |---|---|
> | 17 | Complete & Approved |
> | 6 | Initial submissions not Approved |
> | 6 | Continuing (*i.e.* monthly reports) |
> | 11 | Not yet required |
> | 3 | Complete (requires GESD [Lockheed Martin] approval) |
> | 43 | Total data items |

(R4, tab 182 at TP-006784)

79. On 21 June 1990, NAVSEA issued Modification No. P00018, terminating the 5175 Contract for convenience. The termination was effective 21 June 1990. Paragraph 3(a) of the termination notice required Lockheed Martin to transfer title and deliver to the Government at the Naval Weapon Station (NWSC), Crane, Indiana, all termination inventory and "all data including, but not limited to, CDRL/SDRL requirements . . . which were to be delivered to the Government." Paragraph 3(b) told Lockheed Martin that "[t]o settle your proposal, it will be necessary to establish that all prime and subcontractor termination inventory has been properly accounted for." Lockheed Martin was told it remained liable to its subcontractors and suppliers, and to settle with them as promptly as possible. (R4, tab 19) At the time of the termination, the prime contract had not been definitized, but its undefinitized amount had been raised to $127,070,904 (R4, tab 65 at 2). After the termination, settlement of the termination was assigned to Defense Contract Management Agency in Philadelphia (DCMA-Philadelphia). In January 1993, Sharon R. Lyman (TCO Lyman or the TCO) was assigned to administer the termination of the 5175 Contract (tr. 710).

[4] The SDRLs do not add up to 43. This may be a typographic error.

80. After the termination, the parts that were assembled at Westinghouse's Sikesville, Maryland facility (on the antenna), and at Unisys' plant in Great Neck, New York (on the transmitter), were packaged and sent to NWSC for storage. Because the hardware parts were not qualified, they could not be used. (Tr. 625-26, 654) The Government had paid for the direct labor and material costs incurred on the hardware delivered to NWSC (tr. 732, 837).

81. Not all of the SDRLs submitted could be found. Just before the hearing, Lockheed Martin supplemented the Rule 4 file by including all of the Phase II SDRLs it could locate. For those SDRLs it could not locate, Lockheed Martin relied on its internal computerized correspondence tracking database to demonstrate that the missing SDRLs were delivered (tr. 1298). Had any of the required SDRLs and CDRLs not been delivered, the Government would have complained. Nothing in the record indicates that the required SDRLs and CDRLs were not delivered. No Government witness testified to the contrary. We find that all Phase II SDRLs and CDRLs were delivered up to the time NAVSEA issued the Stop Work Order. No new SDRLs were submitted after issuance of the Stop Work Order on 30 March 1990 (tr. 1328).

82. Over the 14 months (February 1989 through March 1990) Phase II was in effect, a massive amount of SDRLs were submitted. Documentary evidence in the record shows the following antenna SDRLs were submitted by Unisys and Westinghouse jointly to Lockheed Martin: SDRL E001, Cost Performance Reports (03/89-08/89; 11/89-03/90; 08/90) (R4, tab 301); SDRL E002, Cost of Work Data (04/89-08/89; 11/89-03/90) (R4, tab 302); SDRL E004, Variance Analysis Reports (04/89-08/89; 11/89-03/90) (R4, tab 303); SDRL E005, Network Diagram/Gantt Charts (02/89-03/90) (R4, tab 304); SDRL E008, Program Status Report Letters (02/89; 04/89-09/89; 10/13/89; 11/89-03/90) (R4, tab 305); SDRL E010, Presentation Materials (06/27-29/89; 12/07/89; 01/11/90) (R4, tab 306); and SDRL E022, Quality Assurance Production Inspection Reports (03/89-07/89; 10/89; 01/90-03/90) (R4, tab 307).

83. Documentary evidence in the record shows the following transmitter SDRLs were submitted by Unisys to Raytheon: SDRL G001, Cost Performance Reports (03/89-12/89; 01/90-02/90) (R4, tab 401); SDRL G002, Cost of Work Data (04/89-12/89; 01/90-02/90) (R4, tab 402); SDRL G003, Variance Analysis Report (04/89-12/89; 01/90-02/90) (R4, tab 403); SDRL G005, Network Diagrams/Gantt Charts (03/89; 05/89; 07/89-10/89; 12/89; 01/90-02/90) (R4, tab 404); SDRL G009, Program Meeting Agenda (06/29/89) (R4, tab 405); SDRL G010, Presentation Materials (02/07/89; 03/15/89; 04/04/89; 04/26-28/89; 06/16/89; 07/06/89; 09/06-08/89; 11/01/89; 12/05/89; 02/06/90) (R4, tab 406); SDRL G011, Meeting Minutes (02/07/89; 03/28/89; 04/24/89; 08/03/89; 11/21/89; 01/03/90; 03/20/90; 03/29/90) (R4, tab 407); SDRL G014, GFP Status Reports (06/21/89; 08/02/89; 09/20/89; 10/19/89; 11/20/89; 01/03/90; 01/19/90; 03/01/90; 03/29/90) (R4, tab 408); SDRL G016, ILS Plan (04/18/89) (R4, tab 409); SDRL G018,

Production/Delivery Plan (08/02/89; 09/89; 03/29/90) (R4, tab 410); SDRL G019, Quality Assurance Program Plan (06/09/89; 01/09/90; 03/30/90) (R4, tab 411); SDRL G020, Quality Assurance Production Inspection Plan (04/18/89) (R4, tab 412); SDRL G021, Quality Assurance Production Inspection Procedures (08/08/89; 09/25/89; 12/14/89; 03/20/90) (R4, tab 413); SDRL G022, Quality Assurance Production Inspection Reports (02-03/90) (R4, tab 414); SRDL G023, R/M Program Plan (02/90) (R4, tab 415); SDRL G026, Deviation/Waiver Requests (08/02/89; 01/18/90; 02/26/90; 03/20/90) (R4, tab 416); SDRL G027, Nonstandard Part Approval Requests (11/01/89; 03/01/90) (R4, tab 417); SDRL G029, Special Tools and Test Equipment List (03/90) (R4, tab 418); SDRL G035, Program Test Plan (04/89; 02/90) (R4, tab 419); SDRL G036, Element/Subelement Test Procedure (03/29/90) (R4, tab 420); SDRL G038, Factory/Production Acceptance Test Procedure (03/90) (R4, tab 421); and SDRL G040, ESS Test Plan (03/90) (R4, tab 422).

84. The TCO testified at the hearing that if Lockheed Martin could show there were "actual SDRL deliveries" during Phase II, that would provide a basis for higher-tier profit and fee (tr. 883). She testified that to allow higher-tier profit and fee, she needed to see "a listing of what was in fact delivered . . . [and] prices associated with those particular SDRLs" (tr. 869).

Lower-Tier Settlements

a. Westinghouse/Unisys Settlement (Second-Tier, Antenna)

85. Westinghouse's termination settlement with Unisys is summarized in Rule 4, tab 198, page 5. According to this summary, Westinghouse proposed a "Gross Settlement" of $32,166,515. This amount was made up of (1) $4,057,000 in Phase I work and (2) $28,109,515 in Phase II work. On 16 February 1993, Westinghouse and Unisys settled for $26,170,065. Of this amount, $4,057,000 was for Phase I work and $22,113,065 was for Phase II work. The TCO believed the "Gross Settlement" should be $25,906,660. She took no exception to the Phase I amount; she believed Phase II should cost $21,849,660. (R4, tab 198 at 5) She disapproved the Westinghouse/Unisys Second-Tier Subcontract Settlement of $22,113,065 for Phase II (R4, tab 134 at 5).

b. Unisys/Lockheed Martin Settlement (First-Tier, Antenna)

86. Unisys' termination settlement with Lockheed Martin is summarized in Rule 4, tab 198, page 4. Unisys proposed $22,011,452 in "Direct Material," and $4,512,895 in "Profit." "Settlement/Subs" was proposed at $4,897,605. It proposed a "Gross Settlement" of $37,323,212. Of this amount, $6,403,765 was for Phase I work and $30,919,447 was for Phase II work. On 10 September 1993, Unisys and Lockheed Martin settled for the "Gross Settlement" amount of $35,600,000. The TCO took no exception to the Phase I

settlement proposal of $6,403,765 and took the position that Phase II costs should be $27,697,085. (R4, tab 198 at 4)

87. In its proposal to Lockheed Martin, Unisys included its settlement amount with Westinghouse in two places: (1) "Direct Material," and (2) "Settlement/Subs." By placing a significant portion of the cost of its settlement with Westinghouse "above the profit line," Unisys rendered Westinghouse's cost profit-bearing. In her computation, TCO Lyman reduced the "Direct Material" cost from $22,011,452 to $5,425,954 and increased the "Settlement/Subs" category from $4,897,605 to $21,849,660, thus rendering Westinghouse's cost non profit-bearing. (R4, tab 198 at 4; tr. 766)

c. Unisys/Raytheon Settlement (Second-Tier, Transmitter)

88. Unisys' termination settlement with Raytheon is summarized at Rule 4, tab 198, page 3. According to this summary, Unisys proposed a "Gross Settlement" of $29,608,783. This amount was made up of (1) $4,138,000 in Phase I work and (2) $25,470,783 in Phase II work. On 2 November 1992, Unisys and Raytheon settled for $26,014,156. Of this amount, $4,138,000 was for Phase I work and $21,876,156 was for Phase II work. The TCO believed the "Gross Settlement" should be $25,926,237. She took no exception to the Phase I amount of $4,138,000; she believed Phase II should cost $21,788,237. (R4, tab 198 at 3) Accordingly, she disapproved the Unisys/Raytheon Second-Tier Subcontract Settlement of $21,876,156 for Phase II. (R4, tab 148 at 6)

d. Raytheon/Lockheed Martin Settlement (First-Tier, Transmitter)

89. Raytheon's termination settlement with Lockheed Martin is summarized in Rule 4, tab 198 at 2. Raytheon proposed $24,125,471 in "Direct Material" and $3,052,680 in "Fee." "Settlement/Subs" was proposed at $1,855,461. It proposed a "Gross Settlement" of $36,593,256. On 24 July 1996, Raytheon and Lockheed Martin settled for a "Gross Settlement" amount of $36,469,426. The TCO took the position that the "Gross Settlement" amount should be $34,536,111. (R4, tab 198 at 2)

90. In its proposal to Lockheed Martin, Raytheon included its settlement amount with Unisys as "Direct Material." By placing the cost of its settlement with Unisys "above the fee line," Raytheon rendered Unisys' cost fee-bearing. In her computation, TCO Lyman reduced the "Direct Material" from $24,125,471 to $4,170,412 and increased "Settlement/Subs" from $1,855,461 to $21,788,331, thus rendering Unisys' cost non fee-bearing. (R4, tab 198 at 2; tr. 801)

Events Leading to the TCO's Final Decision

91. By letter dated 20 October 1993, Lockheed Martin's contract manager, James Bland (Bland) submitted to TCO Lyman an interim termination settlement proposal

on Standard Form (SF) 1437.[5] The proposal sought a net payment of $14,869,257.64 (line 15, SF 1437). This amount was derived by deducting prior payments of $76,498,703.36 (line 14, SF 1437) from the net proposed settlement of $91,367,961 (line 13, SF 1437). The net proposed settlement included $2,257,478 in fee (line 8, SF 1437). The fee was roughly 2.5 percent of the total costs incurred ($89,110,483). (R4, tab 100)

92. In the October 1993 proposal, Lockheed Martin accounted for "Settlements With Subcontractors" in the amount of $73,823,212 (line 10, SF 1437) "below the fee line" (R4, tab 100; tr. 1023). In response to Defense Contract Audit Agency's (DCAA) inquiry, Lockheed Martin furnished a computation showing that it applied an 86 percent decrement deducting $5,713,916 in subcontractor fee (R4, tab 189; tr. 1026). When asked why Lockheed Martin applied an 86 percent decrement to the "Settlement With Subcontractors" amount ($73,823,212), Bland faxed to DCAA on 22 October 1993 a page out of the 5175 Contract containing SP H-36 (R4, tab 192; tr. 1028). The Government argues that this indicates Lockheed Martin interpreted SP H-36 to apply not only to the initial definitization of the letter contract but to the termination for convenience as well.

93. At the hearing, Bland explained that after the 5175 Contract was terminated, he became the sole Lockheed Martin representative responsible for closing out the contract. In the course of assembling all of the costs for submission, he consulted with Lockheed Martin's finance manager who advised that subcontractor fee "was handled a certain way in May 1989." Because he was not familiar with the program, Bland decided to follow the same approach in Lockheed Martin's settlement proposal. (Tr. 1049, 1069) We find in May 1989, Lockheed Martin and the Navy were negotiating to definitize the letter contract, and SP H-36 by its terms applied to that situation. In 1993, however, Lockheed Martin and DCMA - Philadelphia were in the process of negotiating a termination settlement. On the record before us, we cannot find Bland or Lockheed Martin's finance manager was aware at the time that SP H-36 was limited to "the initial definitized price of the Subcontracts placed with UNISYS" (*see* finding 30).

94. In response to the TCO's request to provide cost information in a format more conducive to audit, Lockheed Martin forwarded by letter dated 25 January 1994 another interim settlement proposal--SF 1437--with column (b) filled in. This proposal requested a net payment of $7,352,992.64 derived by deducting prior payments of $81,870,329.36 (line 14, SF 1437) from the net proposed settlement of $89,223,322.00 (line 13, SF 1437). This net proposed amount included $2,204,277.00 in fee (line 8, SF 1437). (R4, tab 101 at TE-001371-373)

95. FAR Part 49 pertains to "TERMINATION OF CONTRACTS." FAR 49.000 **Scope of part**, provides:

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[5] SF 1437 is prescribed by FAR 49.602-1(c). *See also* FAR 53.249(a)(4).

> This part establishes policies and procedures relating to the complete or partial termination of contracts for the convenience of the Government or for default. It prescribes contract clauses relating to termination and excusable delay and includes instructions for using termination and settlement forms.

FAR 49.108 deals with **Settlement of subcontract settlement proposals**. FAR 49.108-1 makes clear that "[a] subcontractor has no contractual rights against the Government upon the termination of a prime contract." FAR 49.108-3 **Settlement procedure**, provides, in part:

> (a) Contractors shall settle with subcontractors in general conformity with the policies and principles relating to settlement of prime contracts in this subpart and Subparts 49.2 or 49.3. . . . Each Settlement must be supported by accounting data and other information sufficient for adequate review by the Government. . . .
>
> (b) Except as provided in 49.108-4, the TCO shall require that . . . (2) the prime contractor submit, for approval or ratification, all termination settlements with subcontractors. . . .
>
> (c) The TCO shall promptly examine each subcontract settlement received to determine that the subcontract termination was made necessary by the termination of the prime contract . . . The TCO will also determine if the settlement . . . is reasonable in amount, and is allocable to the terminated portion of the contract . . . . In considering the reasonableness of any subcontract settlement, the TCO shall generally be guided by the provisions of this part relating to the settlement of prime contracts, and shall comply with any applicable requirements of 49.107 [relating to audit] and 49.111 [relating to procedure for administrative review] . . . . After the examination, the TCO shall notify the contractor in writing of (1) approval or ratification, or (2) the reasons for disapproval.

Thus, the procedure for settlement of subcontract termination for convenience proposals is highly structured. In this case, both parties followed the procedure set out above during the

course of settlement discussions from inception in 1993 up to the time the TCO issued her final decision in June 2000.

96. In reviewing the subcontractors' termination proposals, TCO Lyman applied both FAR 49.202(a) and FAR 49.315-1(a) (tr. 714). FAR 49.2 deals with "ADDITIONAL PRINCIPLES FOR FIXED-PRICE CONTRACTS TERMINATED FOR CONVENIENCE." FAR 49.202(a), **Profit**, applicable to FFP contracts provides, in part:

> The TCO shall allow profit on preparations made and work done by the contractor for the terminated portion of the contract but not on the settlement expenses. . . . Profit for the contractor's efforts in settling subcontractor proposals shall not be based on the dollar amount of the subcontract settlement agreements but the contractor's efforts will be considered in determining the overall rate of profit allowed the contractor. *Profit shall not be allowed the contractor for material or services that, as of the effective date of termination, have not been delivered by a subcontractor, regardless of the percentage of completion.*

(Emphasis added) Since the NAVSEA/Lockheed Martin prime contract is a CPFF contract, this FAR provision is inapplicable to the contract between them.

97. FAR 52.249-2 TERMINATION FOR CONVENIENCE OF THE GOVERNMENT (FIXED-PRICE) (APR 1984) requires at subparagraph (f)(2)(iii) that profit under a fixed-price contract be determined under FAR 49.202. As noted earlier, a modified version of FAR 52.249-2 was a part of the Lockheed/Unisys first-tier antenna subcontract (finding 38).

98. FAR 49.305, **Adjustment of fee**, applicable to cost-reimbursement contracts, provides in part:

> **49.305-1 General**
>
> (a) The TCO shall determine the adjusted fee to be paid, if any, in the manner provided by the contract. The determination is generally based on a percentage of completion of the contract or of the terminated portion. . . . *The contractor's adjusted fee shall not include an allowance for fee for subcontract effort included in subcontractors' settlement proposals.*

(Emphasis added)

99. Because of disagreement as to the application of FAR 49.202(a) and FAR 49.305-1(a), the TCO did not approve the settlements between Lockheed Martin and Raytheon (transmitter) and between Lockheed Martin and Unisys (antenna) (R4, tab 59 at 2).

100. In her 29 October 1996 letter, TCO Lyman notified Lockheed Martin that based on their prior meeting, she "takes exception to the negotiated Raytheon fee in the amount of $2,972,831" on the transmitter subcontract. She stated that her position was predicated upon FAR 49.305-1(a) which she interpreted to require Raytheon to "exclude from its fee calculation the Raytheon/Loral [Unisys] second-tier subcontract settlement . . . in the amount of $25,926,237." TCO Lyman wrote that her preliminary review indicated that Lockheed Martin/Raytheon "failed to exclude the Raytheon/Loral [Unisys] settlement from its fee calculation," and, as a result, Lockheed Martin's fee was "substantially overstated." In addition, TCO Lyman took the position that SP H-36 also "precludes Raytheon from including the Raytheon/Loral [Unisys] settlement . . . in Raytheon's fee calculation." Lockheed Martin was asked to respond on or before 30 November 1996. (R4, tab 56)

101. TCO Lyman wrote a similar letter dated 29 October 1996 to Lockheed Martin on the antenna, taking exception to the negotiated Loral [Unisys] profit in the amount of $2,213,437. She relied on FAR 49.202(a) which she interpreted to require Unisys to "exclude from its profit calculation the Loral [Unisys]/Westinghouse second-tier subcontract settlement . . . in the amount of $21,849,660. Lockheed Martin was asked to respond on or before 30 November 1996. (R4, tab 55)

102. Located in Philadelphia, and not having participated in the administration of the 5175 Contract, TCO Lyman was apparently unaware at the time of the SDRLs that had been delivered by Unisys/Westinghouse on the antenna, and by Unisys on the transmitter. She testified that she was concerned that Lockheed Martin was including in its fee base costs associated with undelivered Phase II work (tr. 724-25).

103. By letter dated 10 March 1997, TCO Lyman reminded Bland that notwithstanding numerous reminders, no response to her October 1996 letters had been received. TCO Lyman's letter established 31 March 1997 as the deadline for receipt of a response and advised Lockheed Martin that lacking a response by that date she would disapprove the negotiated subcontract settlements and decide on a settlement amount the Government found reasonable. (R4, tab 58)

104. Lockheed Martin's 2 April 1997 response framed the dispute between the parties as "whether first-tier subcontractors Raytheon and Loral [Unisys] can recover fee or profit on the terminated Phase II costs incurred for work performed by second-tier subcontractors Loral [Unisys] and Westinghouse." Lockheed Martin argued that FAR 49.305-1(a) did not preclude the transmitter costs already incurred from being a part of the

fee-bearing cost base. It made a similar argument with respect to the application of FAR 49.202(a) to the antenna cost base. With respect to SP H-36, Lockheed Martin raised two arguments: first, it only applied to Raytheon's prime contract with NAVSEA; and second, it did not address fee on subcontractor costs when there had been a termination for convenience. (R4, tab 60)

105. Lockheed Martin first broached the notion that meeting milestones and delivering SDRLs should be considered making deliverables under the contract for which it was entitled to fee in a meeting with the TCO in June 1997. Despite her request for supporting information, Lockheed Martin furnished no such information until June 2002, two years after the TCO issued her final decision. (Tr. 727-29)

106. Lockheed Martin submitted its final termination settlement proposal dated 15 April 1999 by letter dated 16 April 1999. In response to the Government's contention that no delivery of materials and services was made prior to the termination, Lockheed Martin argued that "[t]he fact that Phase II was not completed is not determinative of whether profit/fee should be paid by the Government." It explained its theory for recovery as follows:

> The program was implemented through the engineering, technical, manufacturing, process, and management personnel of the four companies. . . . This resulted in a continuous transfer and absorption of know-how for each phase of the program, evidenced through an incremental process of meetings and documentary exchanges, based on established Program Reviews and Milestone Reviews, reports and evaluations, CDRL/SDRL submissions, manufacturing readiness reviews and quality control reviews, and manufacturing process demonstrations, all supported by Leader oversight and technical assistance.
>
> These efforts are, by their very nature, completed when performed on a daily, weekly, or monthly basis during the program and were, therefore, completed and delivered services when provided, as under any services-based program.

Lockheed Martin took the position that "costs incurred for services rendered to the date of termination by the first-tier subcontractors are fee/profit-bearing costs," and that it was entitled to fee on its costs for services rendered to the date of termination, including such costs from its first and second tier subcontractors. (R4, tab 65 at 4-5)

107. DCAA's Report No. 6501-99C17100001 of 15 July 1999 on Lockheed Martin's 15 April 1999 final termination settlement proposal found that Lockheed Martin's

"proposed fee represents 9.9% of total claimed costs excluding cost of money." Explanatory note 4 of the report provided the following details:

> It should be noted the contractor changed the basis and percentage of proposed fee between the termination proposal submitted on 25 January 1994 and the subsequent revision on 15 April 1999. The contractor, in the 25 January 1994 proposal inserted almost all their material costs on line 10 "Settlements with Subcontractor." This line is below the fee line, therefore, there was no fee applied to these costs. On the revision on 15 April 1999, the contractor transferred most of the subcontractor costs to line 1 "Direct Material," and applied fee. The fee was increased as a result of the transfer from $2,204,277 to $7,763,889. The contractor declined to comment as to why they transferred the costs between lines.

(R4, tab 104 at 6)

108. Lockheed Martin updated its 15 April 1999 final settlement proposal by a proposal dated 15 September 1999.[6] This proposal requested a net payment of $11,650,410.64 (line 15, SF 1437). The amount was derived from deducting $81,870,329.36 in prior payments (line 14, SF 1437) from $93,520,740.00 in net proposed settlement (line 13, SF 1437). The net proposed settlement of $93,520,740 was made up of four elements: (1) $78,146,458 in total cost (line 7, SF 1437); (2) $7,765,056 in fee (line 8, SF 1437); (3) $262,866 in settlement expenses (line 9, SF 1437) and (4) $7,346,360 in settlements with subcontractors (line 10, SF 1437). (R4, tab 39)

109. Lockheed Martin's explanation accompanying the 15 September 1999 update shows how it calculated its fee:

Item 7 Total Costs (Items 1 through 6)		$78,146,458
Less FCCOM		(495,901)
Fee-bearing costs		$77,650,557
		x10%
Fee		$ 7,765,056

Lockheed Martin provided the following explanation for this calculation:

[6] At the time Lockheed Martin submitted its 15 September 1999 updated final proposal, it had settled with its first-tier transmitter subcontractor, Raytheon, and its first-tier antenna subcontractor, Unisys, and they had settled with their second-tier transmitter subcontractor Unisys and second-tier antenna subcontractor Westinghouse (tr. 1177).

> [Lockheed Martin] is now including the . . . subcontracts in the base for [Lockheed Martin] prime contract fee. The rationale for this approach is more fully addressed in [Lockheed Martin] letter . . . dated 16 April 1999, which provided the Final [Lockheed Martin] Termination Settlement Proposal, and in the Introduction to Book 1 of Enclosure (1) to that Letter.

Lockheed Martin noted that fee had increased by $1,167 from $7,763,889. (R4, tab 39 at 15-16)

110. Negotiations between the parties commenced on 12 January 2000. On 14 February 2000, the TCO increased the Government's position by $197,917 from $85,118,831 to $85,316,748 to allow additional costs associated with the first-tier subcontract agreement reached between Lockheed Martin and Unisys. Beyond this issue, however, the parties reached an impasse. (R4, tab 43 at 2)

111. By letter dated 21 March 2000, TCO Lyman advised Lockheed Martin that based on the information she had, she considered $85,316,748 "fair compensation for performance and settlement expenses for this terminated contract." Lockheed Martin was advised that it had 15 days from the date of receipt of the notice to submit any additional written evidence to support the amounts previously claimed. It was told that at the end of the 15 days, the TCO would determine the amount due[7], and Lockheed Martin could appeal a final decision setting forth her unilateral determination. The TCO identified $8,203,992 ($93,520,740 claimed less $85,316,748 found due) as being in dispute. (R4, tab 40 at 1, 2)

112. Of the $7,763,889 in proposed fee (as of 15 April 1999), *i.e.*, 10 percent of incurred costs less FCCOM, the TCO took no exception to the 10 percent fee rate but took exception to the base costs to which fee was applied. She explained:

> FAR is very clear in its prohibition of fee on uncompleted subcontract work. In accordance with FAR 49.202(a), Lockheed Martin cannot recover fee against uncompleted Phase II costs associated with the Firm Fixed Price lower-tier Loral [Unisys] subcontracts (i.e. the First-Tier Loral [Unisys] subcontract for the Antenna; the second-tier Loral [Unisys] subcontract awarded by Raytheon for the Transmitter). Lockheed Martin can legitimately recover fee on costs of $6,403,666 representing completed Phase I work invoiced and paid under the FFP First-Tier Loral [Unisys] subcontract.

[7] The 15-day notice of determination of amount due when a termination settlement cannot be agreed upon was required by FAR 49.109-7(b).

> Lockheed Martin can also recover fee on Raytheon's incurred costs and fee totaling $12,392,719 for the First-Tier Cost Plus Fixed Fee Raytheon subcontract. The latter amount excludes costs associated with uncompleted Phase II work on the Second-Tier subcontract awarded by Raytheon to Loral [Unisys].

(R4, tab 40 at 2)

113. TCO Lyman rejected Lockheed Martin's argument that delivery of hardware was "incidental to the knowledge transfer and qualification process" inherent in a Leader/Follower program. She also rejected the argument that meeting various milestones should be considered making deliverables. (R4, tab 40 at 2) She drew a distinction and defended her position in allowing higher-tier fee on lower-tier work on Phase I:

> The prime contract and subcontracts are divided into Phase I and II deliverables. Phase I calls for detailed analyses of requirements and the development of plans and procedures; Phase II, the production, qualification, and delivery of hardware. Phase I of the prime and subcontracts was completed, delivered, and invoiced. Phase II was not completed or delivered at the time of termination. Hence, the Government position, in accordance with FAR, properly applies fee/profit to completed Phase I work and disallows fee/profit on uncompleted, undelivered Phase II work.

(R4, tab 40 at 3)

114. At the time TCO Lyman sent her 15-day notice, Lockheed Martin had not provided information as to the various SDRLs and CDRLs that had been submitted during Phase II as deliverables. Information with respect to what SDRLs and CDRLs were delivered, and the value of the delivered SDRLs and CDRLs, was not furnished to the TCO by Lockheed Martin until June 2002, two years after she issued her final decision. (Tr. 838)

115. Lockheed Martin responded to the TCO's 15-day notice by letter dated 3 April 2000. It rearranged the $8,203,992 the TCO identified as being in dispute into three categories: (1) settlement expenses ($96,114); (2) disputed amount attributable to the Raytheon subcontract (transmitter) ($5,108,135); and (3) disputed amount attributable to the Unisys subcontract (antenna) ($2,999,743). On the settlement expenses, Lockheed Martin simply argued that "[t]he Government has allowed less than the actual expenses incurred." On the antenna and transmitter subcontracts, Lockheed Martin argued that the TCO improperly applied the FAR regulations, that work performed prior to the termination

should be fee-bearing and paid on the basis of "percentage of completion" plus loading, pursuant to FAR 49.305-(1)(a). Lockheed Martin's letter concluded by stating that given the differences between the parties, it would be appropriate for the TCO to issue her final decision so that the matter could be resolved through the disputes process. (R4, tab 41)

116. By letter dated 15 May 2000, Lockheed Martin submitted a certified claim for a net payment in the amount of $11,636,874.64 (R4, tab 42). We find the TCO received the claim on 18 May 2000.

117. On 19 June 2000, TCO Lyman issued her final decision by way of Administrative Modification No. A00015 to the 5175 Contract. The decision denied Lockheed Martin's claim in total to the extent it exceeded her determination as set forth in her 21 March 2000 15-day notice ($85,316,748). The decision stated:

> . . . It is my final decision that Lockheed Martin is entitled to costs plus fee in the amount of $85,316,748 under the terminated contract of which $81,870,329 has previously been paid. Hence the net payment to which Lockheed Martin is entitled is $3,446,419.

(R4, tab 43)

118. Lockheed Martin's 15 September 1999 updated final settlement proposal sought a net termination for convenience payment of $11,650,410.64 (finding 108). Its certified claim of 15 May 2000 sought a net termination for convenience payment of $11,636.874.64 (finding 116). There is a reduction of $13,563, and we cannot determine from Lockheed Martin's certified claim the reason for the reduction. In discussing the termination settlement amount to which Lockheed Martin is entitled, the parties have since 1993 consistently used SF 1437 (*see* finding 91) culminating in the 15 September 1999 proposal as Lockheed Martin's last update. Since the TCO's final decision was based on a comparison of her position with Lockheed Martin's 15 September 1999 updated proposal, and since the Government's litigation position is also based upon such a comparison (*see* R4, tab 198 at 1), and, as we find below, after litigation commenced, Martin focused almost exclusively on the two "flow up" theories of recovery developed by its expert, making no further revisions to its latest proposal, we use Lockheed Martin's 15 September 1999 updated proposal as opposed to its certified claim as the starting point for our analysis. Based on a comparison of what Lockheed Martin sought in its 15 September 1999 updated final settlement proposal and the amount the TCO allowed in her final decision, there was a dispute of $8,203,992 ($93,520,740 - $85,316,748).

119. In coming up with her numbers, the TCO testified there were no disputes between the parties on indirect cost rates, material handling rates, general and administrative (G&A) rates and overhead (tr. 1177). According to TCO Lyman, the

$8,203,992 difference was attributable solely to "the costs that would be included in the base for computing Lockheed Martin fee." In other words, the TCO "excluded undelivered Phase 2 cost from the cost base for the application of fee" (tr. 1178).

120. In conjunction with her review of Lockheed Martin's termination proposals, TCO Lyman came across SP H-36. Her initial interpretation was that "[t]here is no fee to Lockheed Martin on the Unisys subcontracts." She was, however, not quite sure of what was meant by the phrase "initial definitized price of the Unisys subcontracts." Because she believed that SP H-36 was ambiguous, and because she believed that FAR 49.202(a) and FAR 49.305-1(a) were clear, TCO Lyman ultimately did not rely on SP H-36 in denying Lockheed Martin's higher-tier fee/profit on lower-tier work. (Tr. 1014-15)

121. Lockheed Martin filed a timely notice of appeal dated 8 September 2000. The Board docketed the appeal as ASBCA No. 53032.

Events Leading to the TCO's Second Final Decision

122. Phase I work has been invoiced and paid for (tr. 113). According to TCO Lyman, since the FAR contains no prohibition against paying fee for "delivered" subcontract work, she allowed fee on Phase I subcontract work. (Tr. 1016)

123. When representatives of the parties met in June 1997, Lockheed Martin was alerted to the fact that the Government was going to have problems with fee at the first-tier level in connection with undelivered Phase II work. At that time, Lockheed Martin took the position that accomplishing the milestones constituted deliveries under the contracts. Even though the TCO sought pricing information on the CDRLs and SDRLs, no such information was provided prior to issuance of her final decision on 19 June 2000. (Tr. 727-28, 1016) At the time TCO Lyman issued her 15-day notice of intent to unilaterally determine the termination amount, she understood Lockheed Martin to have taken the position that Phase II deliveries had taken place in the context of knowledge transfer, whose value was the costs incurred by the followers up to the time of termination. She did not have a specific allocation of that knowledge to the SDRLs. (Tr. 839-40)

124. On 17 June 2002, after the hearing on its appeal had already been scheduled, Lockheed Martin submitted to the TCO a quantification of higher-tier profit and fee, together with appropriate loadings, on what it considered to be the "fair value" of the Phase II SDRLs delivered by lower-tier subcontractors prior to termination (*see* TCO's final decision of 8 January 2003 at 2, ¶ (d)). The Phase II SDRLs identified were the same ones Lockheed Martin subsequently included in the Rule 4 file at tabs 301 to 307 (antenna), and 401 to 422 (transmitter) (*see* findings 81-83).

125. Lockheed Martin's 25 October 2002 update of its 17 June 2002 submission determined that the "fair value" of the Phase II antenna SDRLs delivered by Unisys and

Westinghouse prior to termination was $14,025,421, and the value of the Phase II transmitter SDRLs delivered by Unisys was $13,627,072. Based on these values, Lockheed Martin alternatively claimed entitlement to profit, fee and loadings on the delivered Phase II data items in the amount of $5,524,466. (*See* TCO's final decision of 8 January 2003 at 2-3, ¶¶ (e) and (f))

126. As the evidence unfolded during the course of the hearing in November 2002, the Board became concerned that the TCO had not seen, and therefore had not considered a case based on SDRLs and CDRLs as Phase II deliverables and using Cost Performance Reports (CPRs), a monthly SDRL deliverable, to establish their value. To avert what might become a jurisdictional issue, the Board urged Lockheed Martin to submit during an upcoming scheduled break in the hearing (13 November 2002 to 20 January 2003) what it submitted to the TCO in June and October 2002 as a certified claim and to obtain from her an expedited decision.

127. Lockheed Martin submitted a certified "protective claim" dated 20 November 2002 to the TCO. The claim was submitted with the following reservations:

> (1) "Lockheed Martin believes there are substantial factual and legal bases on which to find the 17 June 2002 submittal and its 25 October 2002 update do not constitute a new claim."
>
> (2) "This claim is filed solely to satisfy the ASBCA's concern that it, or an appellate court, might later find there was no jurisdiction over the 17 June 2002 quantification and the 25 October 2002 update because they constituted a new claim," and
>
> (3) "This 'protective claim' is in addition to and does not supplant the claim which is the subject of ASBCA 53032."

(*See* TCO's 8 January 2003 final decision at 3, ¶ (h))

128. On 8 January 2003, TCO Lyman issued her final decision on the "protective claim." She explained that she considered Lockheed Martin's 17 June 2002 submission and 25 October 2002 update as a "new claim" because its final termination proposal and its update were based on certified cost and pricing data traceable to the company's books and records. That cost and pricing data was audited by DCAA, and the TCO's 19 June 2000 decision was based largely on the DCAA findings and recommendations. TCO Lyman asserted that Lockheed Martin's "protective claim"—based on the 17 June 2002 and 25 October 2002 submissions—was based on cost data contained in the CPRs submitted by Unisys. TCO Lyman contended that Lockheed Martin did not provide her with CPR cost data in support of its final termination proposal nor in response to her 15-day notice. She

contended that the CPR data did not surface until 17 June 2002, two years after she issued her June 2000 final decision. (TCO's 8 January 2003 final decision at 4)

129. The decision went on to say that "Lockheed Martin may be entitled to additional fee, profit, and loadings on the reasonable cost of Phase II data items actually delivered prior to termination . . . provided Lockheed Martin is able to substantiate its entitlement." In this connection, the TCO found that Lockheed Martin had "failed to adequately substantiate alleged data deliveries made prior to termination." The TCO observed that the data items (CLIN 0004) of the antenna subcontracts were priced at $185,275 (Unisys) and $338,897 (Westinghouse), and even if the unpriced data item of the Unisys transmitter subcontract were priced at $338,897,[8] Lockheed Martin would only be entitled to $863,069 ($185,275+$338,897+$338,897) plus $196,000 in additional fee, profit, and loadings for a total of $1,059,069 had it delivered 100 percent of the data items prior to termination. In comparing this amount with Lockheed Martin's alternate claim of $5,524,466, the TCO found the claim overstated. (TCO's 8 January 2003 final decision at 5-6)

130. Lockheed Martin timely appealed the TCO's 8 January 2003 decision by notice dated 9 January 2003. The Board docketed this appeal on 9 January 2003 as ASBCA No. 54064, before resuming the second segment of the hearing on 21 January 2003.

Quantum—Based on Lockheed Martin's Theory that the 5175 Contract is Exempt From that Part of the Regulation Excluding Fee Based on Subcontract Effort

131. Lockheed Martin's primary theory is that it is entitled to receive higher-tier profit loadings and fee on lower-tier subcontractor work based on actual costs incurred without regard to whether there were deliveries of data items (tr. 1080; ex. 1007 at 5). This theory is based on its belief that the 5175 Contract is exempt from the prohibitions of FAR 49.202(a) and FAR 49.305-1(a).

132. To prove quantum under this theory, Lockheed Martin called as its expert Charles R. Long (Long). Long, a certified public accountant (CPA), was qualified as an expert in Government cost accounting (tr. 1082), and his pre-filed written testimony was received into evidence (ex. 1007). With the help of CPRs, Unisys' termination settlement

[8] The Phase II data item in the Unisys transmitter subcontract was not separately priced. TCO Lyman used a price of $338,897 based on the PCO's advice that "the data items required under this subcontract are identical to data items contained in the Westinghouse subcontract" (TCO's 8 January 2003 final decision at 6). While most of the SDRLs required from Unisys on the antenna and the transmitter were the same, there were differences. For example, on the antenna, several SDRLs were required on the near-field antenna test, and "there [were] some other transmitter ones that [were] required that [were] not required on the antenna" (tr. 1399).

proposals, and the TCO's approval letters, Long determined that Westinghouse incurred $18,014,263 for the antenna during Phase II. Using this amount as the base, Long "flowed up" the profit, loadings and fee as follows:

Second Tier	
Westinghouse Cost	$18,014,263 (A1)
First Tier	
Westinghouse Cost	$18,014,263 (A1)
Unisys Profit on A1	**2,341,854 (A2)**
Unisys Loadings on A1	601,830 (A3)
Unisys Unique Costs	3,141,354 (A4)
Unisys Profit on A3 & A4	486,614 (A5)
Prime	
Westinghouse Cost	$18,014,263 (A1)
Unisys Profit on A1	2,341,854 (A2)
Unisys Loadings on A1	601,830 (A3)
Unisys Unique Costs	3,141,354 (A4)
Unisys Profit on A3 & A4	486,614 (A5)
Lockheed Martin Loadings on A2	**327,860 (A6)**
Lockheed Martin Fee on A1-A6	**2,491,378 (A7)**

(Ex. 1007, attach. C at 3; tr. 1151) According to Lockheed Martin, the only amounts in dispute are A2, A6, and A7, which add up to $5,161,092.

133. Using the same method, Long determined Lockheed Martin was entitled to Phase II profit, loadings and fee on the Phase II transmitter in the amount of $4,410,166 (ex. 1007, attach. D at 3). Thus, under its theory that it is entitled to profit, loadings and fee on actual costs incurred without regard to any Phase II deliveries, Lockheed Martin seeks recovery of $9,571,258 ($5,161,092 + $4,410,166) (ex. 1007, attach. E).

Quantum—Based on Establishing a Value for the SDRLs Delivered

134. Lockheed Martin's alternate theory of recovery is based on allocating the actual costs incurred during Phase II to the various SDRLs delivered on the basis of their relative difficulty as measured by a weighting system. To determine what costs were incurred during Phase II, Lockheed Martin located all of the CPRs on that phase it could find. These CPRs were a part of the SDRLs its subcontractors were required to submit. (Tr. 1194-95) The CPRs reported actual costs incurred by phases, by month, and on a cumulative-to-date basis. Costs reported were by WBS elements. Thus, the CPRs for the antenna reported costs for (1) Program Management; (2) Engineering Support; (3) Technical Support Build/Test; (4) Manufacturing; (5) Material Management; (6) Westinghouse Subcontract; (7) Trainee Expense; and (8) Data. (R4, tab 301 at AP-004083) Similarly, the CPRs for the transmitter reported costs for (1) Program

Support; (2) Technical Support Build/Test; (3) First Article Certification; (4) Environmental Stress Screening; (5) System (String) Test; (6) Data Summary; (7) Major Subcontracts; and (8) Manufacturing (R4, tab 401 at AP-004062). In allocating costs from each of these WBS elements to the data items (SDRLs) delivered, Lockheed Martin theorized that "some or all of these various activities are going to contribute to performing . . . or completing that particular deliverable" (tr. 1197).

135. To determine what SDRLs were delivered, Lockheed Martin reviewed the subcontracts involved and checked its internal computerized correspondence tracking data base (tr. 1200-03, 1208-09). It demonstrated at the hearing that the SDRL submissions could be traced to the data base (tr. 1329).

136. To determine how much cost to assign to the various Phase II SDRLs, Lockheed Martin came up with a weighting system which converted the CPR "functional loading WBS structure" into "a product WBS structure" (tr. 1196). Lockheed Martin then developed a matrix listing on the left hand column all of the SDRLs Delivered and Non-Delivered Items. A weighting of one to a maximum of six was assigned to each SDRL as well as the Non-Delivered Items over the 14-month (February 1989 to March 1990) Phase II period. Based on their familiarity with the program, Lawrence Bigaj (Bigaj) assigned the weightings for the antenna, and Paul Bledsoe (Bledsoe), Raytheon's AEGIS Program Manager, assigned the weightings for the transmitter. One matrix was created for each WBS element. (Ex. 1024, attach. F, schedule F-E-W, F-G; tr. 1208, 1272-74; Bledsoe dep. at 133-34) What weighting to assign depended on Bigaj's and Bledsoe's subjective, though educated, belief of the difficulty or complexity of each SDRL (tr. 1275; Bledsoe dep. at 133-34).

137. Once the matrices were populated, Long used the CPRs and allocated "a dollar value to each one of these weighted entries." As Bigaj explained:

> . . . [T]his way we could identify out of all of the dollars that had been spent in a particular month what was tied to a deliverable, what was tied to a nondeliverable. This way we could account for it all, and that way a reasonable approach would be made.

(Tr. 1277)

138. This method boils down to spreading the cost of each WBS element over the SDRLs delivered[9] during Phase II to form a cost base on which to apply higher-tier profit, loadings and fee (tr. 1371, 1487-88). We find this method of allocating WBS element costs to value the SDRLs delivered contrary to the accounting requirement of DODINST

[9] The "Non-Delivered Items" in the matrices were subtracted out in arriving at the profit base (tr. 1391).

7000.2 which prohibits the allocation of one single WBS cost account to two or more WBS elements[10].

139. Using the same flow-up method it used in its other theory (exempt from regulation), Lockheed Martin seeks recovery of $5,524,466 ($2,799,881 + $2,724,585) under its alternate theory (based on delivery of SDRLs) (ex. 1027).

Quantum Based on SF 1437

140. Standard Forms 1437 are used for settlement proposals for cost-reimbursement type contracts. Lockheed Martin's termination settlement proposals were submitted on this form. We summarize Lockheed Martin's final termination proposal as updated 15 September 1999, and the TCO's position culminating in her 19 June 2000 final decision in the table[11] below:

ITEM	09/15/99 Proposal	TCO Final Decision
1. DIRECT MATERIAL	$64,298,692	$18,736,094
2. DIRECT LABOR	$1,604,594	$1,604,594
3. INDIRECT FACTORY EXPENSE	$2,000,002	$2,000,002
4. SPECIAL TOOLING & TEST EQPT.	-------	-------
5. OTHER COSTS	$3,286,682	$3,149,596
6. GEN. & ADMN. EXPENSE	$6,956,488	$6,654,359
7. TOTAL COSTS (ITEMS 1 thru 6)	$78,146,458	$32,144,645

[10] DODINST 7000.2 required the use of COST/SCHEDULE CONTROL SYSTEM (C/SCS). Among the accounting requirements was that a contractor must "[s]ummarize direct costs from cost accounts into the WBS without allocation of a single cost account to two or more WBS elements" (ex. 2003, encl. 1 at 6; tr. 1602-03). This requirement prohibits capturing one WBS cost—such as data item cost—in other WBS items. Similarly, it prohibits capturing costs relating to other WBS elements in the data WBS element. This is consistent with the underlying purpose of requiring WBS, *i.e*., to keep track of costs by WBS functions (tr. 1603). At the time the 5175 Contract was awarded, Lockheed Martin, Unisys and Westinghouse were using the DODINST 7000.2 accounting system (tr. 1189-90). Lockheed Martin's C/SCS established pursuant to DODINST 7000.2 collected actual costs from time sheets, purchasing systems, "against the proper WBS structure, contract, charge number" (tr. 1191). In the absence of evidence to the contrary, we find that Raytheon also had in place a DODINST 7000.2 accounting system.

[11] The table follows the format set out in SF 1437.

8. FEE	$7,765,056	$3,164,874
9. SETTLEMENT EXPENSES	$262,866	$166,752
10. SETTLEMENTS WITH SUBS.	$7,346,360	$49,840,477
11. GROSS PROPOSED SETTLEMENT	$93,520,740	$85,316,748
12. DISPOSAL & OTHER CREDITS	-------	-------
13. NET PROPOSED SETTLEMENT	-------	-------
14. PRIOR PAYMENTS TO CON.	($81,870,329)	($81,870,329)
15. NET PAYMENT REQUESTED	$11,650,411	$3,446,419

(R4, tab 198 at 1)

141. According to the TCO, her analysis of the parties' positions above was based on Lockheed Martin's 15 September 1999 updated final termination settlement proposal which included total incurred costs for Phase I and Phase II, "as reflected in the contractor's books and records, which were audited by DCAA" (tr. 1176). We find the amounts reflected in the table the TCO put together reliable for purposes of determining a gross settlement to which Lockheed Martin is entitled.

142. Even though the TCO testified there was no dispute between the parties with regard to indirect cost rates, material handling rates, G&A, and overhead (tr. 1177), differences did exist as to some items, as indicated in the above table. Other than challenging the TCO's determination that subcontractor costs are non fee-bearing, and coming up with its own "bottoms up" approach in determining fee, Lockheed Martin has not challenged the TCO's calculation on each of the SF 1437 cost elements. We have, nonetheless, reviewed each line of the SF 1437 in detail. However, in the interest of brevity, we make findings below only as to those SF 1437 line items whose validity Lockheed Martin challenged during the appeal process. It is not necessary for us to address those SF 1437 line items as to which either no dispute exists, or as to which Lockheed Martin has provided no evidence that the TCO's adjustment is incorrect.

Direct Material (Line 1, SF 1437)

143. In its 15 September 1999 updated final termination proposal, Lockheed Martin claimed $64,298,692 for "Direct Material." The TCO allowed $18,736,094 in her 19 June 2000 final decision. (R4, tab 198 at 1)

144. The $64,298,692 proposed consisted of the following: (1) $624,488 for Lockheed Martin computer equipment required for configuration management; (2) $64,359,083 for Raytheon and Unisys first-tier subcontract costs reimbursed by Lockheed Martin; and (3) a credit of $684,879 for Miscellaneous Material Pooling and material costs included under Settlement Expenses (line 9, SF 1437). (R4, tab 105 at 3)

145. The TCO determined that Lockheed Martin could recover fee and costs of $6,403,766[12] representing completed Phase I work invoiced and paid under the FFP first-tier Unisys antenna subcontract, and that Lockheed Martin could recover fee on vouchered base costs totaling $12,392,719 on the first-tier CPFF Raytheon transmitter subcontract, representing Raytheon's own incurred costs plus fee on those costs. Thus, she determined that Lockheed Martin could recover fee against total first-tier subcontract costs in the amount of $18,796,485 ($6,403,766 + $12,392,719). (R4, tab 105 at 4)

146. Of the $64,298,692 "Direct Material" proposed, the TCO allowed $18,736,094 to remain in line 1, SF 1437, and transferred the balance ($45,562,598) to line 10, SF 1437, "Settlements With Subcontractors," "below the fee line," as non fee-bearing. The $18,736,094 in "Direct Material" was calculated as follows:

Transferred computer equipment:	$ 624,488
Fee-Bearing 1st Tier Sub-K costs:	$18,796,485
MMP and material credit:	($ 684,879)
	$18,736,094

(R4, tab 105 at 4-5)

147. Other than disagreeing in principle that the transferred amount should be fee-bearing, Lockheed Martin has not challenged the TCO's calculation.

Settlements With Subcontractors (Line 10, SF 1437)

148. Lockheed Martin's 15 September 1999 updated final termination proposal proposed $7,346,360. This is the amount of costs remaining that Lockheed Martin did not transfer to the "Direct Material" cost element (line 1, SF 1437). The TCO's 19 June 2000 final decision proposed $49,840,477 in "Settlements With Subcontractors" (line 10, SF 1437) as non fee-bearing. (R4, tab 198 at 1, tab 105 at 11)

149. The $7,346,360 settlement cost Lockheed Martin proposed was calculated as follows:

[12] This amount is $1 more than what is reflected in Rule 4, tab 198, page 4 (finding 86). The 30 November 1999 DCAA audit report upon which the TCO relied used $6,403,766 (*see* R4, tab 105 at 4).

Negotiated Settlement with Raytheon	$36,469,426
Negotiated Settlement with Unisys	$35,600,000
TCO Reductions with which Unisys Concurs	($ 363,983)
Subtotal	$71,705,443
1st Tier Sub Costs included in Direct Material category	($64,359,083)
Settlements with Subcontractors	$ 7,346,360

(R4, tab 105 at 12)

150. The TCO's final decision amount on "Settlements With Subcontractors" is calculated as follows:

TCO Recognized Raytheon Settlement	$34,536,111
TCO Recognized Unisys Settlement	$34,100,851
Subtotal	$68,636,962
Raytheon Cost In Direct Mat'l	($12,392,719)
Unisys Cost In Direct Mat'l	($ 6,403,766)
Settlements With Subcontractors	$49,840,477

(R4, tab 106 at 6)

151. We address next whether Unisys, as the first-tier FFP subcontractor on the antenna was entitled to recover profit with respect to the Westinghouse subcontract. Even if Lockheed Martin may not itself recover fee pursuant to FAR 49.305-1(a) and FAR 52.249-6, the remaining question is whether the TCO improperly disallowed a part of the Lockheed Martin/Unisys gross settlement and thus improperly reduced the amount Lockheed Martin could recover on line 10, SF 1437. As far as the second-tier FFP antenna subcontract between Unisys and Westinghouse was concerned, we find based on DCAA's Audit Report No. 6521-93A17100512 dated 30 August 1993 that "the subcontractor (Westinghouse) would have been in a loss position had the subcontract not been terminated" (R4, tab 132, ex. A at 5).

152. As indicated in a November 1993 Memorandum of Negotiations, Lockheed Martin and Unisys negotiated a termination settlement in the amount of $35,600,000 (R4, tab 109 at 10; tab 198 at 4).

153. Of the $35,600,000, the TCO recognized $34,100,850 (R4, tab 198 at 4). From her 14 February 2000 memorandum, we find that she derived her position as follows:

Incurred Costs	$10,184,792
Profit (13%)	$ 1,324,023
Subtotal	$11,508,815
Settlement Expenses	$ 742,376
Settlement With Subcontractors	$21,849,660
Gross Settlement	$34,100,851[13]

(R4, tab 106 at 2)

154. Although the TCO accepted a gross settlement of $34,100,851 at the time of her final decision, she accepted a lesser amount earlier. In her 25 November 1998 letter to Lockheed Martin, she stated:

> After careful consideration, the TCO disapproves the agreement reached. The TCO accepts a Gross Settlement amount of $33,778,059.00. This amount includes $6,403,765 for completed Phase I product delivered and invoiced prior to termination.
>
> The TCO position is predicated upon the audit findings of DCAA. The primary exception taken by the TCO was to the negotiated profit amount of $2,213,437. As discussed between the TCO and Lockheed Martin in the meeting of June 26, 1997 and numerous other occasions, the TCO removed uncompleted Phase II subcontract costs from the profit base in accordance with FAR 49.202(a). As a result, the TCO has taken exception to negotiated profit in the amount of $926,550, thereby reducing the amount of acceptable profit from $2,213,437 to $1,286,887.

(R4, tab 114)

155. As indicated in Rule 4, tab 198 at 4, the TCO subsequently increased the profit allowance to $1,324,023 from $1,286,887 (R4, tab 198 at 4). We are not certain as to why the $37,136 ($1,324,023 - $1,286,887) adjustment was made, but we assume that it had nothing to do with the parties' dispute relating to whether any Phase II SDRL deliveries were made since that dispute remained unresolved.

156. We find that the TCO disallowed $926,550 because she believed, at that time, that Lockheed Martin had not demonstrated what Phase II SDRLs had been delivered. The

[13] We do not know why the TCO used $34,100,850, $1 less, in R4, tab 198 at 4.

TCO has since acknowledged that if Lockheed Martin could show there were "actual SDRL deliveries" during Phase II, that would provide a basis for recovery of profit (finding 84).

157. Although Lockheed Martin did not do so initially, it demonstrated at the hearing that a massive amount of antenna SDRLs – included at Rule 4, tabs 301 to 307 – were submitted by Unisys and Westinghouse jointly to Lockheed Martin (finding 82). Since FAR 49.202(a) allows profit for material and services delivered as of the effective date of termination, we find that there is no longer a justification for disallowing $926,550 in profit. We therefore restore $926,550 to the profit line in Rule 4, tab 198 at 4, yielding a profit allowance of $2,250,573 ($1,324,023 + $926,550). This in turn, would increase the "Gross Settlement" line of Rule 4, tab 198 at 4 by $926,550 to $35,027,400 ($34,100,850 + $926,550).

158. In her final decision concerning the overall termination for convenience adjustment, the TCO's position on line 10, SF 1437 (Settlement With Subcontractors) is in the amount of $49,840,477 (R4, tab 198 at 1). This amount was derived as indicated in Finding 150. By increasing the amount of "TCO Recognized Settlement" with Unisys from $34,100,851 to $35,027,400 with the restoration of $926,550 in profit, line 10, SF 1437 would increase from $49,840,477 to $50,766,026:

TCO Recognized Raytheon Settlement	$34,536,111
TCO Recognized Unisys Settlement	**$35,027,400**
Subtotal	**$69,563,511**
Raytheon Cost In Direct Mat'l	($12,392,719)
Unisys Cost In Direct Mat'l	($ 6,403,766)
Settlement With Subcontractors	$50,767,026

159. This adjustment would in turn result in the following adjustments to the TCO's final decision numbers on the overall termination for convenience settlement:

ITEM	TCO Final Decision
1. DIRECT MATERIAL	$18,736,094
2. DIRECT LABOR	$1,604,594
3. INDIRECT FACTORY EXPENSE	$2,000,002
4. SPECIAL TOOLING & TEST EQPT.	-------
5. OTHER COSTS	$3,149,596
6. GEN. & ADM. EXPENSE	$6,654,359
7. TOTAL COSTS (1 thru 6)	$32,144,645
8. FEE	$3,164,874
9. SETTLEMENT EXPENSES	$166,752
10. SETTLEMENTS WITH SUBS.	**$50,767,026**
11. GROSS SETTLEMENT	**$86,243,297**

12. DISPOSAL & OTHER CREDITS	-------
13. NET SETTLEMENT	-------
14. PRIOR PAYMENTS	($81,870,329)
15. NET PAYMENT	**$4,372,968**

DECISION

Entitlement

Lockheed Martin's CPFF contract with NAVSEA to qualify Unisys and Westinghouse as a second source team to compete and supply the AEGIS SPY-1D antenna and transmitter was terminated for convenience. The contract consisted of two phases. At the time of the termination, Phase I was completed. Phase II, which involved mainly the qualification and assembly of hardware (one face of the antenna and one string of the transmitter) had been proceeding for 14 months. Although a massive amount of SDRLs had been delivered, assembly of the demonstration hardware had barely begun, was incomplete, and the hardware had not been delivered.

The Government has paid for all of the costs involved in Phase I (findings 112, 122). The parties were unable to reach a settlement on the overall termination. The primary issue separating the parties centers around whether Lockheed Martin is entitled to fee based on subcontractor effort.

Relying on FAR 49.202(a) and FAR 49.305-1(a), the TCO initially took the position that in the absence of delivery of completed hardware, Lockheed Martin was not entitled to higher-tier profit and fee on lower-tier subcontractor work. In response, Lockheed Martin took the position that the parts of FAR 49.202(a) and FAR 49.305-1(a) relied upon by the TCO do not apply to Leader company contracting because it is an "extraordinary acquisition technique."

Based on its theory that it is exempt from those parts of the regulations the TCO applied, and using a three-tier "bottoms up" approach, Lockheed Martin calculates that it is entitled to profit, loadings and fee in the amount of $5,161,092 on the antenna, and loadings and fees in the amount of $4,410,166 on the transmitter, for a total termination for convenience adjustment of $9,571,258. (Finding 133)

After the TCO issued her first final decision (19 June 2000) and while an appeal from that decision was pending before the Board (ASBCA No. 53032), Lockheed Martin forwarded to the TCO the SDRLs generated by its subcontractors during Phase II, and argued that they constituted delivered data items, the cost of which should be included in the base for determining higher-tier profit and fee.

Based on this contention, and using the same three-tier "bottoms up" approach, Lockheed Martin calculates that it is entitled to profit, loadings, and fee in the amount of $2,799,881 for the antenna, and loadings and fees in the amount of $2,724,585 on the transmitter, for a total termination for convenience adjustment of $5,524,466. (Finding 139)

FAR 49.202(a) and FAR 49.305-1(a) do not provide the same recovery in terms of profit and fee based on subcontractor work. In the case of FAR 49.202(a), which applies to fixed-price contracts terminated for convenience, profit is not allowed for "material or services that, as of the effective date of termination, have not been delivered by a subcontractor" (finding 96). Thus, to the extent material and services had been delivered prior to the effective date of termination, their costs can be included in the base for determining higher-tier profit. In contrast, FAR 49.305-1(a), which applies to cost-reimbursement contracts terminated for convenience, flatly provides that the contractor's adjusted fee "shall not include an allowance for fee for subcontractors' effort included in subcontractors' settlement proposals" (finding 98).

The only contract before the Board is the prime contract between NAVSEA and Lockheed Martin – a CPFF contract. Hence, the dispute here must be resolved through the application of (1) FAR 52.249-6 TERMINATION (COST-REIMBURSEMENT) (MAY 1986) and (2) FAR 49.305-1(a). As for FAR 49.305-1(a), Lockheed Martin is presumed to have constructive knowledge of federal procurement regulations. *General Builders Supply Co. v. United States*, 409 F.2d 246, 250-251 (Ct. Cl. 1969); *General Engineering & Machine Works v. O'Keefe*, 991 F.2d 775, 780 (Fed. Cir. 1993).

In terms of adjustment of fee of the CPFF contract between NAVSEA and Lockheed Martin, FAR 49.305-1(a) provides that "[t]he TCO shall determine the adjusted fee to be paid . . . in the manner provided by the contract" (finding 98). The contract termination clause, FAR 52.249-6(g)(4)(i), provides that if the contract is terminated for the convenience of the Government, the settlement shall include a percentage of the fee equal to the percentage completion of work contemplated under the contract "but excluding subcontract effort included in subcontractors' termination proposals" (finding 20). There is no ambiguity in this contract language. In contract interpretation, the plain and unambiguous meaning of a written agreement controls. *Craft Machine Works, Inc. v. United States*, 926 F.2d 1110, 1113 (Fed. Cir. 1991) In arguing their respective positions before the Board, both sides seem to have overlooked FAR 52.249-6.

Lockheed Martin does not argue that FAR 49.305-1(a) is unclear. It argues that it is exempt from the exclusion of fee based on the subcontract effort part of the regulation by virtue of the fact that its contract with NAVSEA is a Leader company contract. We note that Lockheed Martin does not contend that the entire FAR 49.305-1(a) is inapplicable but only "*[t]he portions of the FAR provisions limiting higher-tier fee and profit on lower-tier subcontractor work"* (emphasis added) (app. br. at 2, *see also* at 50, 52-53) We are

not persuaded by this argument. First, FAR Part 17.4 which authorizes Leader company contracting does not exempt contracts entered into pursuant to that regulation from the principles found in FAR Part 49, including Subpart 49.3, applicable to cost-reimbursement contracts terminated for convenience. Second, there is nothing in FAR Subpart 49.3 that singles out contracts entered into pursuant to the Leader company contracting technique (FAR Part 17) for special treatment. In this regard, FAR 49.305-1(a) itself offers perhaps the best example of how a regulation accomplishes exclusion from coverage. When it wants to exclude fee based on subcontract effort, it says so specifically. Exclusion from coverage of contracts entered into under the Leader company contracting technique is nowhere stated in FAR Subpart 49.3. Third, excluding a contractor's fee based on subcontract effort as provided in FAR 49.305-1(a), is totally consistent with the contract termination clause, FAR 52.249-6(g)(4)(i). Prior to initiating the AEGIS Second Source Radar Qualification Program, the parties entered into "[v]ery vigorous, robust" and "intense" discussions (finding 31) and there is no evidence that the parties intended the contract termination clause (FAR 52.249-6) to apply any other way but as written.

In arguing their respective interpretations of FAR 49.305-1(a) and FAR 49.202(a), both sides rely on what they consider to be the regulatory history of the earlier version of these regulations (*see* app. br. at 39-40; Gov't br. at 54-59). Lockheed Martin contends that "[t[here is no indication in the regulatory history of either of the two FAR provisions that either was intended to apply to what the FAR and its predecessors called the 'extraordinary' leader-follower contracting technique" (app. br. at 41, ¶ 165). The so-called regulatory history in the Rule 4 file consists mainly of recommendations from various members of the Armed Services Procurement Regulation Committee members, and correspondence between the committee and an industry representative known as Council of Defense and Space Industry Associations on the merits or lack of merits in allowing profit on subcontractor settlements.

In *Alaskan Arctic Gas Pipeline Co. v. United States*, 831 F.2d 1043, 1046 (Fed. Cir. 1987), the court stated:

> It is well established, in cases involving statutory construction, that the statutory language itself is the best indication of congressional intent [footnote omitted]. However, if the bare language of the statute fails to provide adequate guidance or if a literal interpretation of the statute would lead to an incongruous result, the court must resort to the purpose and legislative history of the statute to determine the intent of Congress in enacting the statute [footnote omitted]. Notwithstanding the guidance provided by the statutory language itself or by its legislative history, this court is bound, in performing statutory construction, by case law

> precedent developed by it and by its predecessor courts [footnote omitted].

Where the language of the FAR provision (FAR 49.305-1(a)) is clear, as here, we do not look to its regulatory history for interpretation. In this regard, the canons of statutory interpretation "apply equally to any legal text." *Smith v. Brown*, 35 F.3d 1516, 1523 (Fed. Cir. 1994).

The appeals before us are controlled by *Kollmorgen Corp., Electro-Optical Division*, ASBCA No. 28480, 86-2 BCA ¶ 18,919. *Kollmorgen* involved the interpretation of the earlier version of FAR 52.249-6 (DAR 7-203.10 TERMINATION (APR 1973)) which required fee to be determined "exclusive of subcontract effort included in subcontractors' termination claims," and FAR 49.305-1(a) (DAR 8-406) which provided that "[t]he prime contractor's adjusted fee shall not include an allowance for fee for subcontract effort included in subcontractors' termination claims." 86-2 BCA at 95,411. As in this case, Kollmorgen was awarded a CPFF contract. The contract was terminated for convenience about six months after award. The contractor claimed fee on the basis that it had completed 80 percent of the work—55 percent for itself and 25 percent for its subcontractor, Westinghouse. In denying fee based on Kollmorgen's settlement with Westinghouse, we said at 86-2 BCA at 95,411:

> *The termination clause and the regulations are very clear* that the prime contractor . . . may not include a fee on subcontractor cost or effort included in the subcontractor's termination claim. . . . Kollmorgen may not collect a fee on the amount of the settlement with Westinghouse.

(Emphasis added)

By shifting subcontractor costs from the non fee-bearing cost element of "Settlements With Subcontractors" (line 10, SF 1437) to the fee-bearing cost element of "Direct Material" (line 1, SF 1437) in its final termination settlement proposal, Lockheed Martin sought to avoid the application of FAR 52.249-6 (finding 107). To allow this is to read the prohibition of FAR 52.249-6 out of the contract. Such a reading is impermissible. *See Fortec Constructors v. United States*, 760 F.2d 1288, 1292 (Fed. Cir. 1985). In the same vein, Lockheed Martin's "bottoms up" approach, advanced by its expert, cannot be accepted because it too disregarded FAR 52.249-6 and FAR 49.305-1(a) by including subcontract effort in the base for calculating higher-tier fee (findings 132, 133).

For its alternate theory of recovery based on deliveries of SDRLs, Lockheed Martin relies on *TRW Inc.*, ASBCA No. 51003, 00-2 BCA ¶ 30,992 (app. br. at 55, 59, 78). In that case, we granted TRW's motion for summary judgment as to its entitlement to profit on

data items that were delivered, if a reasonable value could be placed on the data-items. The portions of the prime contract relevant to that appeal were on a fixed-price-incentive-fee basis, and the contract incorporated FAR 52.249-2, the 1984 termination for convenience clause applicable to fixed-price contracts. Moreover, the principle involved there was FAR 49.202(a). *TRW* is consistent with Board precedents that have recognized delivery of drawings and supporting calculations, schedules, engineering advice and data items as deliverables and have held that contractors were entitled to profit on such items delivered in termination for convenience cases involving FFP contracts. *Industrial Pump & Compressor, Inc.*, ASBCA No. 39003, 93-2 BCA ¶ 25,757 at 128,167 (applying FAR 52.249-2, Board allowed profit on subcontract performance costs for delivered material and services such as drawings, meeting attendance, and provision of schedules); *cf. Metadure Corp.*, ASBCA No. 21183, 83-1 BCA ¶ 16,208 (after termination for convenience of a FFP contract, claim for profit denied because subcontractor had not delivered technical manual and related data). These precedents do not apply to the appeals before us. What apply are FAR 52.249-6, FAR 49.305-1(a), and *Kollmorgen*.

Had the prime contract and all subcontracts in this case been FFP contracts, the SDRLs delivered might provide a basis for higher-tier profit. Had the prime contract and all subcontracts been cost-reimbursement contracts, all subcontract effort would have to be excluded from determining prime contractor fee. Given the language of FAR 52.249-6 and FAR 49.305-1(a), subcontract effort, delivered SDRLs or otherwise, must be excluded in determining prime contractor fee so long as the prime contract is CPFF. This was a foreseeable result because different contract types and different contract clauses and regulations were involved in the complex contract structure the parties themselves created.

In its brief, Government counsel seeks repayment of "approximately $1 million in additional fee due to the conciliatory approach taken by Ms. Lyman in not applying Special Provision H-36" (Gov't br. at 98-99). Due to the clear and unambiguous language of SP H-36 limiting its application to "*the initial definitized price of the Subcontracts placed with UNISYS*" (emphasis added) (finding 30), we are unable to conclude that SP-36 applies to the termination for convenience situation we face here. Where the "provisions are clear and unambiguous, they must be given their plain and ordinary meaning." *Alaska Lumber & Pulp Co. v. Madigan*, 2 F.3d 389, 392 (Fed. Cir. 1993). We have found to the extent Lockheed Martin invoked SP H-36, it was either in connection with forward pricing the 5175 Contract (finding 34-35), or where those involved in Lockheed Martin simply lacked an understanding of the limitation prescribed in SP H-36 (findings 92-93).

Because FAR 52.249-6 and FAR 49.305-1(a) are clear in excluding contractor fee based on subcontract effort included in subcontractors' settlement proposals, and because we are not persuaded that contracts entered into pursuant to the Leader company contracting technique are exempt from the exclusion provisions of FAR 49.305-1(a) and FAR 52.249-6, we hold that Lockheed Martin is not entitled to the $9,571,258 claimed.

Because FAR 49.202(a) upon which it relies for its claim for fee associated with the delivery of SDRLs applies to fixed-price contracts terminated for convenience, and because its contract with NAVSEA is a cost-reimbursement contract not subject to FAR 49.202(a), we hold that Lockheed Martin is not entitled to the $5,524,466 claimed.

Because SP H-36 clearly provides that fee was excludable "solely on the initial definitized price of the Subcontracts placed with UNISYS," we hold that the Government is not entitled to recoup the money paid in settlement of Phase I convenience termination costs on the basis of SP H-36.

This leaves for consideration whether any other adjustments to the termination settlement as determined by the TCO are required. Determining Lockheed Martin may not itself recover fee does not settle whether the TCO improperly disallowed a part of the Lockheed Martin/Unisys gross settlement and thus improperly reduced the amount Lockheed Martin could recover on line 10, SF 1437.

On the antenna side, both Lockheed Martin's first-tier subcontract with Unisys, and Unisys' second-tier subcontract with Westinghouse are FPP contracts. The Lockheed Martin/Unisys first-tier subcontract settlement is governed by Clause 3, Termination, which is a modified version of FAR 52.249-2 TERMINATION FOR CONVENIENCE OF THE GOVERNMENT (FIXED-PRICE) (APR 1984), and FAR 49.202 (findings 38, 97). In this regard, FAR 49.202(a) allows profit for material and services delivered as of the effective date of termination. *TRW,* 00-2 BCA at 153,028.

Because Lockheed Martin demonstrated at the hearing that a massive amount of Phase II antenna SDRLs were submitted by Unisys and Westinghouse jointly to Lockheed Martin, we hold that Lockheed Martin was entitled to include these delivered SDRLs in the base for determining its subcontractor's profit in computing its termination for convenience costs.

Quantum

Lockheed Martin bears the burden of proving that it is entitled to a settlement amount in excess of that determined by the TCO. *Nicon, Inc. v. United* States, 331 F.3d 878, 885 (Fed. Cir. 2003); General *Dynamics Land Systems, Inc.*, ASBCA No. 52283, 02-1 BCA ¶ 31,659 at 156,411; *North-East Plumbing*, 88-2 BCA ¶ 20,736 at 104,781; *Systems & Computer Information, Inc.*, ASBCA No. 18458, 78-1 BCA ¶ 12,946 at 63,069.

The parties have attempted to reach a termination settlement since 1993. They have consistently done so using SF 1437, the prescribed form for settlement proposals used for termination for convenience of a cost-reimbursement contract. Only after litigation began did Lockheed Martin come up with the three-tier "bottoms up" approach in calculating the fee it claims is due.

Lockheed Martin's quantum calculations based on its theory that the 5175 Contract was exempt from excluding subcontract effort in calculating fee cannot be accepted because it disregarded FAR 52.249-6 and FAR 49.305-1(a). Its calculations based on placing a value on the SDRLs delivered also cannot be accepted because it is based on FAR 49.202(a) which we have held is not applicable to the NAVSEA/Lockheed Martin contract.

This leaves SF 1437. The TCO summarized the parties' positions in a table in Rule 4, tab 198, page 1. We have reproduced a concise version of the table in finding 140. The TCO's summary of the parties' positions on various SF 1437 cost elements was based on total incurred costs as reflected in the contractor's books and records which were audited by DCAA. For this reason, we have found the summary to be reliable for determining a gross settlement to which Lockheed Martin is entitled (finding 141).

Determining that Lockheed Martin may not itself recover fee does not settle whether the TCO improperly disallowed a part of the Lockheed Martin/Unisys gross settlement on the first-tier antenna subcontract, and thus improperly reduced the amount Lockheed Martin could recover on line 10 of SF 1437 (Settlement With Subcontractors). We have found Lockheed Martin is entitled to $926,550 in disallowed profit in the Lockheed Martin/Unisys gross settlement because Lockheed Martin has demonstrated that a massive amount of Phase II antenna SDRLs were delivered by Unisys and Westinghouse jointly to Lockheed Martin as of the effect date of the termination of the 5175 Contract (findings 81-82, 156-59).

We decline to follow Lockheed Martin's "bottoms up" method for valuing the SDRLs delivered based on allocating WBS element costs to the SDRLs delivered. This method is contrary to the contract accounting requirement of DODINST 7000.2 which prohibits the allocation of one single WBS cost account to two or more WBS elements (finding 138). Moreover, since the inception of settlement discussions in 1993, the parties have followed the settlement procedure set out in the FAR. The costs set out in SF 1437 were discussed, audited, and revised as a result of discussions and audits on numerous occasions. Lockheed Martin has provided no persuasive reasons to now deviate from the prescribed FAR termination for convenience settlement procedure.

We conclude that payment of profit on the Westinghouse Phase II costs to the extent of $926,550 most fairly reflects the parties' agreed upon procedure (c*f. Worsham Construction Co., Inc.*, ASBCA No. 25907, 85-2 BCA ¶ 18,016 at 90,368). Restoring the $926,550 in disallowed profit would increase the Lockheed Martin/Unisys first-tier gross settlement by $926,550 to $35,027,400. This adjustment would, in turn, increase line 10, SF 1437 of the NAVSEA/Lockheed Martin gross settlement at the prime contractor level to $50,767,026, resulting in a NAVSEA/Lockheed Martin gross settlement, line 11, SF 1437, of $86,243,297. (Findings 151-159)

CONCLUSION

For the reasons stated, we sustain the appeals in part, holding that Lockheed Martin is entitled to a gross settlement of $86,243,297 (line 11, SF 1437). Interest on the amount found due (unpaid) is to run from 18 May 2000 (finding 116). 41 U.S.C. § 611. In all other respects, the appeals are denied.

Dated: 15 October 2003

PETER D. TING
Administrative Judge
Armed Services Board
of Contract Appeals

I concur

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

I concur

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

I certify that the foregoing is a true copy of the Opinion and Decision of the Armed Services Board of Contract Appeals in ASBCA Nos. 53032, 54064, Appeals of Lockheed Martin Corporation, Naval Electronics & Surveillance Systems - Surface Systems, rendered in conformance with the Board's Charter.

Dated:

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