

ARMED SERVICES BOARD OF CONTRACT APPEALS

Appeal of --)
)
Southwest Marine, Inc.) ASBCA No. 54550
)
Under Contract No. N00024-85-C-8506)

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OPINION BY ADMINISTRATIVE JUDGE THOMAS ON CROSS-MOTIONS
RELATING TO SECTION III.E OF APPELLANT'S RESPONSE

This is the quantum phase of ASBCA No. 47621. Southwest Marine, Inc. (SWM) appealed under the Contract Disputes Act (CDA), 41 U.S.C. §§ 601-613, from a contracting officer's final decision (COFD) asserting a government claim that the Navy had overpaid SWM's predecessor in interest, Northwest Marine Iron Works (NMIW), \$2,161,287 as a result of debt concessions by its subcontractors and other creditors subsequent to confirmation of its Chapter 11 reorganization plan. As more fully set forth in *Southwest Marine, Inc.*, ASBCA No. 54550, 08-1 BCA ¶ 33,786 ("SWM II"), the Board sustained ASBCA No. 47621 as to entitlement, concluding that the bankruptcy proceedings precluded recovery. That decision was reversed, however, by the United States District Court for the Southern District of California which remanded the appeal for determination of quantum. The United States Court of Appeals for the Ninth Circuit affirmed the decision of the District Court. *Southwest Marine, Inc.*, ASBCA No. 47621, 96-2 BCA ¶ 28,601 (*SWM I*), *rev'd, Dalton v. Southwest Marine, Inc.*, No. 97-1488-IEG (LSP), Third Amended Order (S.D. Cal. Oct. 7, 1998) (hereinafter District Court

opinion), *aff'd*, 217 F.3d 1128 (9th Cir. 2000) (hereinafter Circuit opinion), *cert. denied*, 532 U.S. 1007 (2001).

In the quantum proceedings, the Navy has filed Respondent's Statement of Costs (SOC) dated 21 May 2004 and SWM has filed Appellant's Response to the Government's Statement of Costs (Response) dated 23 July 2004. The current amount of the Navy's claim is \$1,204,155 less retention of \$10,003. This opinion decides motions filed by the parties relating to Section III.E of the Response. *SWM II* decided motions relating to Sections III.A, III.B and III.C of the Response. We assume familiarity with *SWM II*, which contains a more complete statement of the underlying facts and prior proceedings.

The pending motions consist of "Respondent's Motion For Partial Summary Judgment Addressing Section III.E Of Appellant's Response" (gov't mot.), dated 2 April 2008, and "Appellant's Cross-Motion for Order In Limine Determining the Claim Allowed by and to be Quantified in Compliance with the Mandate of the Appellate Court," dated 29 April 2008. In Section III.E of the Response, SWM argues, based upon quotations from the court opinions and the Navy's brief to the Ninth Circuit, that the claim as sustained by the District Court is more limited in scope than the claim as quantified by the contracting officer in the COFD. For example, the Navy's claim included debt concessions not only by subcontractors but also by creditors such as the Port of Portland. The District Court stated that the Navy contends that the claim related to "debts which NMIW owed its subcontractors" (District Court opinion at 8). SWM argues based on this language that the claim is limited for purposes of quantum to debt concessions by "subcontractors." The Navy responds that the District Court sustained the claim as to entitlement without limitation.

STATEMENT OF FACTS FOR PURPOSES OF THE MOTIONS

1. On 19 August 1985, the Navy awarded NMIW the captioned fixed-price incentive contract for overhaul of the USS DULUTH. The contract included Federal Acquisition Regulation (FAR) 52.216-16, INCENTIVE PRICE REVISION-FIRM TARGET (APR 1984) (the IPR clause). This clause defines "Costs" as "allowable costs in accordance with Part 31 of the [FAR] in effect on the date of this contract" (FAR 52.216-16(b)). (R4, tab 1 at 1-2, 46-49 of 53)

2. FAR 31.201-5, sometimes referred to as the Credits Provision clause, provided at the relevant time:

The applicable portion of any income, rebate,
allowance, or other credit relating to any allowable cost and

received by or accruing to the contractor shall be credited to the Government either as a cost reduction or by cash refund.

3. During performance, NMIW's subcontractors included Crosby & Overton and PacOrd. NMIW obtained worker's compensation insurance from the Oregon State Accident Insurance Fund (SAIF). The Port of Portland provided facilities for which it charged fees and tariffs. (SOC at 24-27)

4. On 29 October 1986, NMIW filed a Chapter 11 petition. On 20 March 1987, the bankruptcy court confirmed NMIW's reorganization plan under Chapter 11. The plan provided that unsecured claims in excess of \$1,000 would be converted into interest bearing debentures of the reorganized company in a principal amount equal to the allowed unsecured claim. Amongst the debenture holders were subcontractors who had worked on the DULUTH and not been paid. (Circuit opinion, 217 F.3d at 1132, 1140)

5. On 5 April 1989, NMIW submitted an invoice for \$2,811,077. On or about 7 April 1989, the Navy paid that invoice. (District Court opinion at 3, 8)

6. On 17 April 1989, SWM purchased NMIW. As one of the conditions for the purchase, NMIW received debt concessions from its debenture holders. (Circuit opinion, 217 F.3d at 1133)

7. The COFD dated 11 March 1994 claimed that NMIW had received debt concessions from subcontractors and other creditors in the amount of \$3,238,248, as follows:

Direct Costs:	
Port of Portland	\$ 381,757
PACCORD [PacOrd]	113,679
Other	59,031
Allocable Costs:	
First Interstate Bank	917,620
Willamette Savings & Loan	260,882
SAIF	319,264
Other (Some May Be Direct)	<u>1,186,015</u>
Total	\$3,238,248

Working the amount of \$3,238,248 through the formula in the IPR clause as interpreted by the Navy, the COFD demanded reimbursement of \$2,161,287 pursuant to the Credits Provision clause. (R4, tab 26 at 5-6)

8. SWM appealed the COFD to the Board. As noted above, the District and Circuit courts ultimately sustained the Navy’s claim as to entitlement and remanded the appeal for determination of quantum.

9. In the SOC, the Navy quantified the debt concessions at a total of \$1,857,192, as follows:

	<u>Direct</u>	<u>Indirect</u>	<u>Total</u>
Crosby & Overton	\$ 105,161	\$ 7,243	\$ 112,404
PacOrd	113,679		113,679
Port of Portland	539,097	55,464	594,561
SAIF		607,456	607,456
Other Creditors At Least \$10,000	363,136	40,767	403,903
Other Creditors Under \$10,000	<u>20,314</u>	<u>4,875</u>	<u>25,189</u>
Total	\$1,141,387	\$ 715,805	\$1,857,192

(SOC at 11, indirect costs as totaled by the Board) Working the amount of \$1,857,192 through the IPR clause formula as interpreted by the Navy, the SOC arrives at a claim of \$1,204,551. (SOC at 11, ex. D)

DISTRICT COURT AND CIRCUIT COURT PROCEEDINGS

We quote the District Court opinion at some length since SWM relies upon the description of the Navy’s arguments in that opinion for purposes of Section III.E of the Response. We italicize the language SWM emphasizes in its Response and its memorandum in opposition to the government’s motion for summary judgment and in support of its cross-motion *in limine* (Response at 22; app. memo. at 3). The District Court stated:

DISCUSSION

A. Did ASBCA Err as Matter of Law in Determining that NMIW’s Bankruptcy Proceedings Precluded the Navy’s Recovery for Overpayment?

The first issue raised by the instant appeal is whether the ASBCA erred in determining that the Navy’s right to recovery was barred by operation of bankruptcy law....

The Navy advances two principal arguments in support of the instant appeal with respect to [the] ASBCA analysis. First, the Navy contends that the operation of bankruptcy

principles is inapposite in relation to its claims of overpayment and, therefore, the ASBCA's analysis is irrelevant. The Navy argues that, regardless of whether the NMIW's pre-petition debts were wiped out by the 1987 bankruptcy reorganization, the Navy's efforts to recover costs relates to the creditor's voluntary post-petition actions in April of 1989. The Navy contends that (a) the post-petition obligations replaced the original pre-petition ones; (b) these "new" obligations represented, at least in part, debts which NMIW *owed its subcontractors* for Duluth work; (c) *NMIW sought reimbursement on [sic] these costs to the subcontractors when it certified, post-petition, the April 5, 1989 invoice*; and, (d) therefore, when the creditors (including *the subcontractors*) voluntarily agreed to compromise their claims, the Navy was entitled, pursuant to the contract, to share in the reduction of costs.

...Essentially, the Navy argues that unless it is allowed to seek recovery of funds, NMIW will recover a windfall because it will have obtained post-petition payments (April 7, 1989) from the Navy *for subcontractor work* on the Duluth project *which the subcontractors subsequently excused*.

Second, having distinguished the ASBCA's reliance on bankruptcy principles, the Navy argues that the ASBCA's analysis of the Navy's overpayment challenge to the post-petition actions is inadequate....

....

Having reviewed the arguments, the Court agrees with the Navy. First, the Court notes that both the ASBCA and SWM erroneously focus on NMIW's pre-petition debts. Although these debts were discharged in bankruptcy, the Court notes that the Navy correctly focuses on the voluntary post-petition activities of NMIW's creditors.... Accordingly, as a matter of law, the ASBCA erred when it determined that the bankruptcy discharge precluded the Navy from seeking reimbursement for overpayment.

B. Did the ASBCA Err in Construing the Contract's Provisions?

Having determined that bankruptcy law does not preclude the Navy from seeking reimbursement for overpayment on the contract, the Court now examines the ASBCA's analysis of the contract provisions. The Navy contends that the ASBCA erred in construing the two contract provisions which authorize recovery in this case. In its decision, the ASBCA indicated that the bankruptcy discharge prevented the Navy's recovery under the contract. However, as previously discussed, the discharge does not preclude recovery for overpayment where the overpayment relates to voluntary post-petition debt concessions by NMIW's creditors. As a matter of law, the ASBCA erred in concluding that the Navy could not recover under the contract for these concessions. The Navy is entitled to reimbursement under the Credit Provision Clause, FAR 31.201-5, and the IPR Clause, FAR 52.216-16.

CONCLUSION

Based on the preceding discussion, the Court finds that the ASBCA committed two legal errors in addressing the parties' cross-motions for summary judgment. First, the ASBCA erred as a matter of law in finding that NMIW's bankruptcy discharge prevented the Navy from seeking recovery for overpayment on the Duluth contract. Second, the ASBCA erred as a matter of law in finding that the Navy could not recover for overpayment under the terms of the contract. Accordingly, the judgment of the ASBCA is **REVERSED**. As the instant appeal resolves the issue of the Navy's *entitlement to overpaid contract costs*, the Court hereby **REMANDS** the matter to the ASBCA for a determination on the merits of quantum.

(District Court opinion at 7-10, emphasis supplied, footnotes omitted)

In its brief on SWM's appeal to the Ninth Circuit, the Navy argued *inter alia* that the FAR Credits Provision applied "...because NMIW performed the DULUTH contract work but did not pay all of its creditors for their work... The confirmed Plan created new post-petition debts in the form of debentures whereby NMIW still owed monies to those

_____” (emphasis as supplied in the Response at 23).

The Court of Appeals explained in its opinion affirming the District Court’s order (217 F.3d at 1140, emphasis as supplied in the Response at 24):

Under the Credits Provision Clause, Southwest was required to credit back to the Navy any income, rebate, allowance or other credit related to an allowable cost, which was received by or accrued to the contractor. The debenture holder’s [sic] agreement to forego collection of the debentures satisfied this definition. It was related to the claimed cost—*there would have been no debentures had NMIW actually paid its subcontractors for the Duluth work*—and it accrued to the contractor since Southwest no longer had to pay them their full principle [sic].

APPELLANT’S RESPONSE AND THE PARTIES’ MOTIONS

Section III.E of the Response is entitled “Limitation Of Claim To Items Consistent with Government Representations To Courts (i.e. Direct Costs Of Subcontractors Who Received Debentures And ‘Voluntarily’ Conceded Portions Of Those Obligations).” SWM argues: “In the courts that decided appeals of this case, the Government consistently and repeatedly argued that the credits it sought were debts voluntarily excused (or ‘conceded’ or ‘compromised’ or ‘forgiven’) by subcontractors.” (Response at 22) SWM continues:

For each item of its claimed concession amounts, the Government should be required to prove its representations that NMIW included debenture debts in its costs, that NMIW sought reimbursement of those costs (or any costs) in its April 1989 invoice and that the debenture holder voluntarily agreed to forego collection of his debenture. The Government cannot prove any of those representations. In addition, at minimum, it is clear that the Navy and the courts focused exclusively on DULUTH subcontractors who received debentures.... Subcontract costs are direct costs.... Notwithstanding those Navy representations to the courts, the [SOC] now claims credits to indirect costs totaling \$715,805.... The Navy’s credits should be limited to the credits addressed and allowed by the District Court: credits to debts to DULUTH subcontractors.

(Response at 24-25)

In its motion for summary judgment as to Section III.E, the Navy argues:

Section III.E of SWM's Response asks that the Board correct alleged errors in the appellate courts' entitlement decisions leading to this quantum appeal. Appellant contends the Government led the appellate courts to make these alleged errors through misrepresentations, and Appellant requests that the Board require the Government to support these alleged misrepresentations through evidence presented in the present proceedings on quantum. According to Appellant, should the Board act as Appellant requests, the results would be "zero" recovery on quantum for Respondent.

(Gov't mot. at 1-2) The Navy concludes its memorandum in support of the motion as follows:

SWM's arguments at Section III.E of its Response improperly ask the Board to circumvent or effectively overrule the appellate courts' ruling of entitlement in favor of the Government. The Board is without authority to do so and must, therefore, reject Appellant's arguments at Section III.E as a matter of law.

(Gov't mot. at 9) The Navy does not argue that it is entitled to recovery of any specific cost on summary judgment. Rather, it objects to SWM's general contentions in Section III.E.

SWM opposes the motion. It points out that the Navy mischaracterized the Response:

Specifically, Respondent's motion asserts that "SWM's response asks that the Board correct alleged errors in the appellate courts' entitlement decisions" and alleges that Appellant asserts "misrepresentations" by the Government to those courts.

Appellant's Response asserts no such thing.

To the contrary, Appellant's Response, Section III.E., argues that the Board should carry out the mandate of the appellate District Court exactly in accordance with its terms

by quantifying the “overpaid contract costs” to which that Court, in its own words held the Navy entitled.

(App. opp’n and cross-mot. at 1-2). In its cross-motion, SWM requests an order *in limine* “identifying the Government claim and the costs to be proved to and quantified by the Board.” SWM states that the claim consists of:

- “Costs to the subcontractors” which were unpaid and were “represented” by post-petition obligations of NMIW,
- of which “NMIW sought reimbursement...when it certified...[its] April 5, 1989 invoice”
- for which “NMIW...obtained post-petition payments [on] April 7, 1989 from the Navy for subcontractor work on the DULUTH”
- which debts “the subcontractors subsequently excused.”

(App. cross-mot. at 2-3, quoting from the District Court opinion at 8)

In its reply, the Navy argues *inter alia* that the District Court opinion did not contain a checklist such as that suggested by SWM. Rather, the District Court simply remanded “for a determination on the merits of quantum.” The District Court did not indicate any intent “to limit the Government’s claim to something short of what is presented in the contracting officer’s final decision and described and addressed in [SWM I].” (Gov’t reply at 3, 8)

In a subsequent rejoinder, SWM argues that the District Court’s mandate includes a recitation of the Navy’s contentions to the court, as listed in the motion *in limine*. SWM states: “[i]t is the Navy’s contentions to the Court—not its previous claims—which the District Court found to be meritorious: ‘Having reviewed the arguments, the Court agrees with the Navy.’” (App. rejoinder at 2, quoting the District Court opinion at 9)

DECISION

The Navy’s Motion for Summary Judgment as to Section III.E of the Response

Although the Navy styled its motion as a motion for summary judgment, we view it as more in the nature of a motion to strike. Section III.E asserts that the claim, for purposes of quantum, must be limited to “Items Consistent with Government

Representations To Courts.” As indicated in its rejoinder, SWM argues in this section of the Response that the District Court sustained something less than the whole of the Navy’s claim as to entitlement. Thus, SWM argues that “[i]t is the Navy’s contentions to the Court—not its previous claims—which the District Court found to be meritorious” (app. rejoinder at 2).

We are unable to find any merit in SWM’s interpretation. The appeal to the Board, and subsequently the courts, was taken from the Navy’s claim set forth in the COFD. The District Court denied the appeal and remanded it for determination of quantum. The Court’s mandate did not use words of limitation. In the mandate, the Court stated: “As the instant appeal resolves the issue of the Navy’s entitlement to overpaid contract costs, the Court hereby **REMANDS** the matter to the ASBCA for a determination on the merits of quantum” (District Court opinion at 10). The Ninth Circuit affirmed the District Court’s decision without disturbing the mandate.

SWM argues that the Board must look beyond the language of the mandate itself to “the full text” of the order (app. rejoinder at 2). SWM has not, however, pointed to words of limitation in the text. In its opinion, the District Court outlined the Navy’s arguments as to entitlement. The Court nowhere stated that its outline was intended to limit the scope of the claim. It did not, for example, state that it was only recognizing entitlement insofar as the claim related to subcontractors as opposed to other creditors or to direct costs as opposed to indirect costs. On the contrary, it sustained entitlement to “overpaid contract costs” pursuant to the Credits Provision clause, which refers generally to “any...credit relating to any allowable cost,” and the IPR clause (SOF ¶¶ 1, 2). Similarly, the Ninth Circuit did not state that it was limiting the claim as set forth in the COFD. We are not prepared to infer a limitation where none was expressed.

Accordingly, we grant the government’s motion to strike Section III.E of the Response.

SWM’s Cross-Motion for an Order *in Limine*

SWM moves for an order *in limine* “identifying the Government claim and the costs to be proved to and quantified by the Board,” as more particularly described above. SWM’s proposed order intermingles elements which may have some merit with those which don’t. For example, the Navy presumably will have to prove as part of its quantum case that a particular cost was “subsequently excused.” On the other hand, we have rejected above the interpretation that the costs must be “Costs to the subcontractors,” as opposed to other creditors. We do not think it would be useful to pick and choose among SWM’s proposed criteria. Accordingly, we deny the motion *in limine*. Any evidentiary questions which remain will be resolved as necessary at the hearing.

CONCLUSION

The Navy's motion for summary judgment as to Section III.E of the Response, which we view as a motion to strike, is granted. Appellant's cross-motion for an order *in limine* identifying the scope of the claim to be quantified is denied.

Dated: 25 September 2008

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

I concur

I concur

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

RICHARD SHACKLEFORD
Administrative Judge
Armed Services Board
of Contract Appeals

I certify that the foregoing is a true copy of the Opinion and Decision of the Armed Services Board of Contract Appeals in ASBCA No. 54550, Appeal of Southwest Marine, Inc., rendered in conformance with the Board's Charter.

Dated:

CATHERINE A. STANTON
Recorder, Armed Services
Board of Contract Appeals