Developments in Federal Contracts and Construction Law, 1985-86

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Tax Proposals Restrict Completed Contract Accounting Method

The House Tax Bill and the Senate Finance Committee Chairman's latest proposal both impose significant restrictions on the use of the completed contract method of accounting. Under the House Bill, "long—term contracts," meaning those with performance periods longer than one year, must be reported under the percentage completion method. An exception is provided for construction contracts to be completed within 2 years of the contract date, if performed by a taxpayer whose average annual gross receipts do not exceed $10 million. Senator Packwood's proposal provides that all long—term contracts would be subject to uniform capitalization rules under the completed contract method, but would retain present law for real property construction contracts not requiring more than 2 years to complete, if performed by a taxpayer with average annual gross receipts of $10 million or less, It's too early to tell how or if the Senate will modify the House action. The Senate may repeal the method, follow the House version, increase the $10 million gross receipt figure, or some combination of these or other alternatives.

DOD Revises Certification Requirement

DOD revised the rules on overhead certification after issuing what the industry viewed as conflicting policies. Prior to the final version, DOD suggested that the contractor certify that claimed costs would be finally allowed. Under the final rule, however, as set out in a public memorandum from the Undersecretary of Defense, a contractor must certify only that the claimed overhead costs are allowable.

Attorneys Fees Now Recoverable in Contract Appeals Board Cases

Some prevailing contractors in disputes before Agency Appeals Boards may now be awarded attorneys fees under the reauthorized Equal Access to Justice Act ("EAJA"). Language in the reauthorization bill signed on August 5, 1985 reversed a prior court ruling which prohibited Agency Boards from awarding attorney fees under the EAJA. The new legislation not only made the EAJA permanent, but also expanded its coverage to make the government responsible for fees unless the underlying Agency action *i.e.* default termination, delay claim etc. or the government's litigation position is substantially justified. The government may also avoid liability for fees if "special circumstances" would make the award unjust. In addition to other minor changes, eligibility for fees was expanded to include individuals with a net worth of two million dollars or less, and to businesses with a net worth of less than seven million dollars.

Eichleay Method Finally Adopted by the ASBCA

After years of sidestepping, The Armed Services Board finally recognized the validity of the Eichleay formula in a 1985 decision on overhead costs. In *Savoy Construction Company, Inc.*, ASBCA Nos. 21218, 21925 et al., 85—2 BCA ¶18,073, a contractor, using the Eichleay Method, claimed for extended overhead costs resulting from numerous government issued change orders. The Board first rejected the Eichleay calculation, but then reversed itself after the Claims Court directed the issue to be reconsidered in light of its holding in the *Capital Electric* case. The Board ruled that the Eichleay method was a fair method to calculate the extended or unabsorbed overhead costs of a construction contractor delayed as a result of changes.

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In concluding, the Board cited the often quoted but seldom invoked language in the *Shirley Contracting* case: "We see no reason why the government should not be required to bear a fair share of appellant's extended home office overhead."

Contractor's Duty to Clarify Bid Ambiguities Extended

The U.S. Court of Appeals for the Federal Circuit extended the patent ambiguity rule" to apply to industry specifications incorporated by reference in bid documents. The doctrine requires a contractor to seek clarification of any obvious ambiguities in bid documents, or risk the cost of an error.

In *Fortec Constructors v. U.S.. 760 F.2d 1288* (Fed. Cir. 1985), a contractor sought an equitable adjustment for the costs of demolishing and rebuilding concrete rebar joints. Footnotes to the contract drawings incorporated industry standards for rebar construction, however, the standards included two different design methods. Before the contractor completed cementing the last rebar, the government claimed that the contractor used the wrong of the two methods. The court ruled that the two designs presented a patent ambiguity, triggering a duty to seek clarification. Upon failure to gain clarification, the contractor was found to have assumed the risk of error, and was denied an adjustment.

Courts Continue Strict Enforcement of No Damage for Delay Clauses

Courts have continued the recent trend of strict enforcement of the increasingly common "No damage for delay" clause. The provision, included in many private and state construction contracts but so far not adopted on the Federal level, provides that a contractor's only remedy for delay is a time extension, In *Bates & Rogers Construction Corp. et al v. Greeley & Hansen,* 486 N.E. 2d 902 (Ill. 1985) for example, a municipal contractor claimed for damages resulting from the owner's late material deliveries. The court, relying on the no delay damage clause in the contract, rejected the contractor's attempt to characterize delay costs as general impact and disruption damages. The court ruled that the contractor was barred from recovery because the essence of his claim sought delay damages, which were bargained away by signing a contract containing the "no damage" clause.

Appeals Boards Clarify Deductive Modification Formula

The Armed Services and Veterans Appeals Boards clarified the costing method to be used in pricing deductive change orders. These orders, which generally involve deletions of a phase or portion of the contract work, are sometimes identified as a line item in the bid or cost schedule, but sometimes impact on less clear contract tasks.

Cost disputes often arise over the method for pricing deductive change orders because the contractor's credit proposal is usually less than the line item bid or schedule price In clarifying the pricing method, the Boards ruled that the equitable adjustment for a reduction—of—work is what the deleted work would have cost, and government has the burden of proving the amount of the reduction.

As the decisions suggest, contractors should not use pricing schedules or bid abstracts to calculate change proposals. Rather, in preparing the proposal, contractors should segregate the deleted item and apportion and allocate attributable costs to the removed work. *Glover Construction Co., Inc.*, ASBCA No. 29194 85-2 BCA ¶18,093; *R&E Electronics, Inc.*, VABCA Nos. 2227, 2299, 2300, 85-3 BCA ¶18.316.

Postal Service Appeals Board Recognizes Total Cost Claim

In a departure from recent precedent, the Postal Service Contract Appeals Board ruled that a contractor could recover interest on a claim presented in a total cost format. *Regan/Nager Construction Co.*, PSBCA No. 1070, 85-1 BCA ¶17,778. The Board rejected the government's contention that the Contract Disputes Act prohibits submission of total cost claims.

Except for limited advantages in reduced preparation time, however, the total cost method is not a desirable approach for costing a claim. The better approach is to submit a detailed claim showing the cause and effect relationship between owner acts and increased costs. The extra time involved in the preparation of a thorough claim is often rewarded by earlier and more favorable settlements.

GAO's Authority to Enjoin Contract Performance Survives Administration Challenge

The recently enacted Competition in Contracting Act gave the General Accounting Office highly controversial authority to halt performance of contracts for which bid protests were filed. The administration contested this authority, and, in a highly unusual order, advised the executive agencies not to comply with the law on the grounds of unconstitutionality. After losing a court battle, however, the Executive reversed itself, and advised agencies to honor the law pending further appeal to the courts.