

**Eichleay And The Recovery of Unabsorbed Home Office Overhead: The Redheaded Step-Child Among The Various Elements of Compensable Damages In Government Contract Claims  
- Further Complicated By -  
Government Tricks, Traps, Delays And Audit Flaws, Interlaced With Confusion At The Appeals Tribunals, the Boards And Courts**

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Putting A Small Contractor's Home Office Overhead In Perspective

Of all the major elements of contractors' damage claims (alternatively, cost recovery elements in a contractor's proposal in his request to the government for equitable contract adjustment ["REA"]), e.g. extra labor, material, equipment & small tool, field overhead, insurance, surety bond, interest, claim preparation costs, and, yes, even profit on these extra costs, unabsorbed home office overhead (a.k.a. general and administrative or "G&A" cost) is by far the least understood and most contentious cost element of them all.

Often, like the parent of the aforementioned redheaded step-child, a contractor, particularly early in its life, and in highly competitive tight markets as well, may tend to ignore its G&A cost.<sup>1</sup> For example, a less experienced contractor in need of new work may "bid the competition" to an extreme. He tends to figure his direct costs down to a fine line, put on some figure, say 10%, for indirect field cost, supervision, field office, etc., then, in an attempt to best the competition and without much thought to the fact his G&A cost record actually is based on his previous fiscal year-end financial statements, adds on another say 7% for "margin." Margin, by necessity then must cover profit *and* G&A. Under these circumstances, any major government disruption or suspension prolonging the contract's performance can burn down the margin between cost and contract income such that there ultimately remains nothing for profit ....or worse.

Home Office Overhead – A "Dead Horse" Which Must Be Carried

G&A costs are those generated exclusively by a contractor's home office and that office's staff, for the use and benefit of all of the contractor's contracts. Since the home office, unlike the projects, has no income, the contractor is obliged to charge each project its appropriate share of this "rent," properly done by means of addressing this cost as a separate cost element in the project's bid estimate.<sup>2</sup> Ideally the contractor will know and recognize, by way of previous financial statements, exactly how much his G&A is running annually. He will then divide the figure thus determined by all other costs of contracting, over the same time period from which he determined the G&A figure, the result being a percentage. This is the percentage he must multiply the total estimated cost of the project being bid by, the result being the home office overhead (G&A) cost

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<sup>1</sup> He does so at his own great peril. "Overhead for many contractors is a completely nebulous item that is felt rather than seen and measured. It should not be so because overhead alone may well run up to 10 percent of a contractor's annual business volume." *Contractor's Management Handbook*, James J. O'Brien and Robert G. Zilly, 1-17.

<sup>2</sup> Thus a project running on schedule and developing monthly cash flow is able to "absorb" the "rent" cost it must "pay" to the home office for its services. In the event of a government suspension of work, the project, suddenly deprived of income, becomes unable to pay that fee and "unabsorbed" home office costs accrue, resulting in over-absorption of these costs by the contractor's other projects.

element of doing business. This is by no means perfect,<sup>3</sup> but far, far better than a low ball guess to try to beat the competition.

### The Government Gauntlet A Contractor Faces In An Unabsorbed Overhead Recovery Attempt

Returning to the step-child analogy and addressing the other side of that coin, a bit like the public with respect to its view of the proverbial child's legitimacy, when asserting a claim to recover unabsorbed G&A, the contractor will be faced with a host of government actors ready and anxious to test with great skill and passion the legal and factual veracity of the contractor's damages recovery claim for unabsorbed G&A. They include the contract's administrative contracting officer, the contracting officer ("CO") and her consultants and handlers, including the agency's staff lawyers; if denied at the CO level, the board of contract appeals judges (or the Federal Court of Claims judges), and if further appealed, the judges of the Federal Circuit Court of Appeals. This is not to forget the Department of Justice attorneys if the contractor appeals to the Claims Court rather than the board, nor the government auditors of the Defense Contract Audit Agency ("DCAA")<sup>4</sup> who will undoubtedly make their appearance sooner rather than later.

Before jumping into the government claims ring to challenge this cast of government actors, one had best gird his loins for combat. Knowing exactly what you are claiming, and the support for it, is indispensable. Having a rock-hard, air-tight case factually and legally will help.<sup>5</sup> Otherwise you will waste your time and money.

### Eichleay Explained

The Federal Circuit has held that the *Eichleay* formula is the *exclusive* means available for calculating unabsorbed overhead costs on a federal construction contract.<sup>6</sup> *Wickham Contracting Co. v. Fischer*, 12 F.3d 1574, 13 FPD 1, 18 C.C.121 (Fed. Cir. 1994). It is not possible to state the *Eichleay* recovery proposition better than the Newsletter of a leading construction law firm did:<sup>7</sup>

"Over 40 years ago, in *Eichleay Corporation*, ASBCA No. 5183, 60-2 BCA ¶ 2688, affirmed on reconsideration, 61-1 BCA ¶ 2894, the Armed Services Board of Contract Appeals ("ASBCA") recognized that there is no exact method to determine the amount of home office overhead expenses to be allocated to any particular contract. In *Eichleay*, the board utilized the following formula for allocating extended home office overhead costs to a contract that has been delayed:

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<sup>3</sup> For example, it assumes simple projects next door to the home office bear the same G&A costs as risky ones two states away.

<sup>4</sup> Those genuine wizards of the government bean-counting autocracy – said with an appropriate amount of actual seriousness and respect.

<sup>5</sup> To say the least. It will be indispensable.

<sup>6</sup> I believe this is true only if you have presented a Contract Disputes Act ("CDA")-certified "claim" to the CO for a determination, NOT if you are presenting a cost proposal for an REA to the contracting officer. The former elevates the issue to legal standards imposed in federal litigation while the latter does not.

<sup>7</sup> *Common Sense Contracting*, #421, Vol 16, No. 1, Smith, Currie & Hancock LLP.

$$(1) \frac{\text{Contract Billings}}{\text{Total Billings for Full Contract Period}} \times \text{Total Overhead for Contract Period} = \text{Overhead Allocable to Contract}$$

$$(2) \frac{\text{Overhead Allocable to Contract}}{\text{Total Days of Performance (including Delay Period)}} = \text{Daily Contract Overhead}$$

$$(3) \text{Daily Contract Overhead} \times \text{Number of Days of Delay} = \text{Extended Overhead}$$

This formula for calculating extended home office overhead damages is commonly called the "*Eichleay Formula*." The Federal Circuit has approved the use of the *Eichleay Formula* to calculate extended home office overhead ... "provided that compensable delay occurred, and that the contractor could not have taken on any other jobs during the contract period." *C.B.C. Enterprises, Inc. v. United States*, 978 F.2d 669, 673-4 (Fed. Cir. 1992)."

### Eichleay – A “Resilient Means”

To understand fully the approved identification of the Formula’s elements and its operation I refer to the following construction legal experts:<sup>8</sup>

“The mathematical operation of the *Eichleay* formula is best understood by reviewing its application in a relatively uncomplicated case. In *A.A. Beiro Construction, Co., Inc.*, the contractor claimed entitlement to compensation for extended home office overhead, profit, and interest on behalf of its subcontractor, Westlind. Westlind calculated its damages according to the *Eichleay* formula. The Government contended that it had properly compensated Westlind for home office overhead according to "a percentage of direct cost method." At trial, Westlind introduced evidence of the following figures: \$552,492.12 in contract billings for the project; \$2,003,047.69 in total billings for the contract period; \$339,195.52 in total overhead for the contract period; 322 calendar days of actual performance; and 118 days of government-caused delay. Westlind calculated its unabsorbed overhead, as follows:”

$$(1) \frac{\$552,492.12}{\$2,003,047.69} \times \$339,195.52 = \$93,558.86$$

$$(2) \frac{\$93,558.86}{322} = \$290.56$$

$$(3) \$290.56 \times 118 = \$34,285.54$$

<sup>8</sup> III. The *Eichleay Formula*: A Resilient Means For Recovering Unabsorbed Overhead, 322 Public Contract Law Journal, Vol. 24, No. 2, Winter, 1995. [Footnotes omitted.]

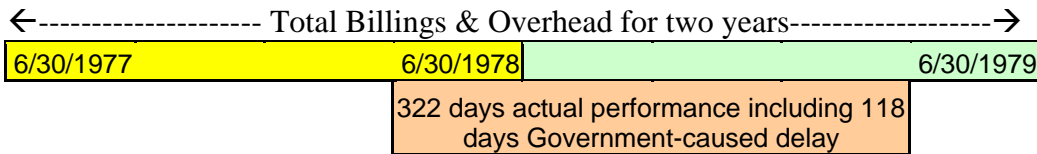
A Creative Way To Maintain “Apples-To-Apples” In Eichleay

It is important to note carefully exactly how the Board<sup>10</sup> permitted the contractor to define and identify essential elements of the formula to maintain strict “apples to apples” comparison:

“99. Westlind calculated its total billings by determining a per diem rate of total billings for the fiscal years ending June 30, 1978 and June 30, 1979 (the years during which it performed the contract.) 91-3 BCA at 120,841.

100. Westlind calculated its total overhead by determining a per diem rate of total overhead for the fiscal years ended June 30, 1978 and June 30, 1979 (the years during which it performed the contract). *Id.* at 120,842. The per diem rate was then multiplied by number of days in the contract period. *Id.* Westlind's total overhead pool included: officers' salaries; group and key-man insurance; repairs and maintenance; depreciation; dues and subscriptions; office supplies and expense; office salaries; indirect salaries; telephone, taxes; truck and auto expense; travel and entertainment; legal and accounting; contributions; interest; licenses; retirement plans; yard maintenance; consulting and placement fees; employee welfare; utilities; and miscellaneous items. *Id.*”

A chart of this creative approach might be helpful to visualize how this method nullifies the dispute potential which would be natural in the identification of exactly where the start and stop points for the correct total overhead figure actually occur in the contractor’s financial statements:



Note that the Board’s only apparent criteria for the contractor in this regard was that the actual performance start and stop within “*the [fiscal] years during which it performed the contract*”.

The DCAA Watchdog Watching Eichleay

I have before mentioned the DCAA. Its life mission is to sharp-shoot, nullify and/or minimize every contractor advantage (perceived or actual) possible in the claim – more often than not before the CO makes her formal determination. While the CO’s own federal “warrant” requires absolute fairness and independence in such determinations, there is no one drawing a federal paycheck who will find for a contractor in utter contradiction of the DCAA. It is therefore well to note and be prepared for the positions taken by the DCAA before you decide to use the *A.A. Berio* period determination

<sup>9</sup> This is an exact calculation based on the root figures in *...A Resilient Means...*, which showed \$34,307.32 as the final result, a probable rounding error or typo by the writers or the Board.

<sup>10</sup> This was a Corps of Engineers Board of Contract Appeals case, ENG BCA No. 5103, 91-3 BCA ¶24,149.

method, as characteristically DCAA will most likely dispute your right to use this approach, whether it knows about *Berio* or not:<sup>11</sup>

“The actual contract performance period represents the actual days of performance (including the extension period). It is the period from the start date of the contract until the date of contract completion. Note that the contract billings, total billings, the total fixed overhead and the performance days should be for the same time interval, i.e., the delayed contract’s actual total performance period.”

At least part of the reason why the DCAA auditors’ findings sometimes seem unreasonable is because their own Manual has flaws. For example, a serious auditor, an astute student of his DCAA Manual,<sup>12</sup> might demand that the contractor produce proof that he could take on no other work while standing by during the government-ordered suspension of contract work:<sup>13</sup>

“Entitlement to Unabsorbed Overhead Damages. The U.S. Court of Appeals of the Federal Circuit (CAFC) (*West v. All State Boiler*, 146 F.3d 1368 (Fed. Cir. 1998) “All State”) ruled that the elements of the claim (legal tests) **that a contractor must show** to recover unabsorbed overhead include:

- (1) The delay/suspension was Government caused [when a Government caused disruption results in a delay of contract performance, Eichleay damages may be appropriate].
- (2) The Government required the contractor to standby during the delay/suspension period.
- (3) It was impractical for the contractor to take on other work.
- (4) The delay/suspension caused the contractor to be unable to complete the contract within the original contract performance period, as extended by any modifications.”  
[**Emphasis** added.]

In fact, the actual rule as to what a contractor must prove is no such thing.<sup>14</sup> (Going forward from this point, I refer from time to time to my contractor-example. See fn14.) The government had constructively admitted it was solely at fault. The suspension was sudden and the contractor was always in doubt about its duration. As a result, it was not possible to take on “replacement” work with the assets planned for use on the instant contract. Thus he was always in stand-by mode for the suspension’s duration. The contractor had a *prima facie* case for recovery of his unabsorbed G&A. Once this is

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<sup>11</sup> DCAA Contract Audit Manual December 31, 2008 1253 12-804 - .1 Eichleay Steps.

<sup>12</sup> Our DCAA auditor here is a very serious government bureaucrat, always on the lookout to squelch any contractor mischief in the bud. When he’s on the road, he reads his DCAA Manual instead of a John Grisham novel in his motel room before bedtime.

<sup>13</sup> DCAA Contract Audit Manual December 31, 2008 1253, 12.803 Auditing Unabsorbed Overhead.

<sup>14</sup> My hypothetical contractor here is from the situation description given me by a small contractor recently. Shortly after award and before any work could be accomplished, the government, without any warning, suddenly placed a work suspension order on the contract as it had lack-of-permit issues. Over the course of some eight (8) months it could give the contractor no estimate of when it could begin work. Then it just as suddenly lifted the order and demanded that the contractor submit a price proposal covering its costs for the suspension, due not later than 30 days from the date the work suspension order was lifted.

established, no proof by the contractor of items (3) and (4) above is required. They are assumed as true and shifted to the government for rebuttal proof:<sup>15</sup>

“Therefore, when a contractor can show that the government required a contractor to remain on "standby" and [show that] the government-imposed delay was "uncertain," the contractor has established a prima facie case of entitlement to Eichleay formula damages. The burden then shifts to the government to present rebuttal evidence or argument showing that the contractor did not suffer or should not have suffered any loss because it was able to either reduce its overhead or take on other work during the delay.”

### Key Issues For Our Suspended Small Contractor

There are two important issues we should address on behalf of our beleaguered hypothetical contractor. a.) Why is he getting the “bum’s rush” from the government owner to submit his price proposal in such an unreasonably short time – considering the complications involved in an unabsorbed G&A claim? And b.), since the suspension went into effect before any appreciable work could be accomplished and no billings were generated as a result, there is no numerator (“total contract billings”) to install into Step (1) in the Eichleay formula, how is it possible for the contractor to use Eichleay – said by the court to be the *exclusive* means available for calculating unabsorbed overhead costs on a federal construction contract?<sup>16</sup>

### The Exception To The Federal Circuit’s Eichleay Exclusivity Rule

Taking the second issue first, the contractor has met the exception to the Federal Circuit’s Eichleay-as-the-exclusive-means rule. In a ruling a decade after *Wickham*,<sup>16</sup> the Circuit said that a contractor, otherwise fully entitled to recover unabsorbed G&A as a result of government-caused suspension, but faced with the unique situation where the suspension has prevented any contract billings, may not use the Eichleay formula.<sup>17</sup> *Nicon*, the contractor in that case, computed its "daily contract overhead" by substituting the contract price for "contract billings" and the contract performance time for the actual "days of performance" into the *Eichleay* formula. No one could say, in the total absence of actual cost and total contract duration figures, this was not a reasonable estimate under the circumstances.<sup>18</sup> However, "constructive figures may not be substituted into the *Eichleay* formula," said the Circuit in response.<sup>17</sup>

The Federal Circuit did note, however, that the contractor nevertheless might be able to recover unabsorbed overhead through "some other method of allocation,"<sup>17</sup> making *Eichleay* off limits for any contractor so unlucky as to be the winning bidder on any contract on which the government has unknown (or concealed) design or site access issues which must be fixed before a formal Notice to Proceed (“NTP”) can be issued, and/or before any actual work can be accomplished.

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<sup>15</sup> *Mech-Con Corp. v. West*, 61 F.3d 883, 14 FPD \_ 65, 19 C.C. \_ 395 (Fed. Cir. 1995).

<sup>16</sup> *Wickham Contracting Co. v. Fischer*, 12 F.3d 1574, 13 FPD 1, 18 C.C.121 (Fed. Cir. 1994).

<sup>17</sup> *Nicon, Inc. v. United States*, 331 F.3d 878 (Fed. Cir. 2003).

<sup>18</sup> After award to *Nicon*, there apparently ensued a bid protest by another contractor which, after 288 days had elapsed the government resolved by terminating *Nicon*’s contract.

## The Government's Abrupt Demand For Unreasonably Rapid REA Submittal Turnaround

As for the initial problem our contractor faced right out of the gate, after eight months of little or no information, it suddenly received the formal NTP, and in the same order received notice to produce and submit its REA not later than 20 days from the date of the order. Our contractor held an \$8,000,000 subcontract under a mega-prime contractor, who's own government contract was in the multi-millions. As for the requirement for the absurdly short 20-day submittal period, the prime contractor's management said it was required by the government to produce its own REA within 30 days from the government order's date.<sup>19</sup> As its own REA had to include all of its own costs as well as the REA's of all its subcontractors in all other trades, it required at least 10 days for its own coordination and review prior to submittal to the government.

Our contractor's contract is on a Department of Defense agency contract. His claim will by definition be a Contract Disputes Act ("CDA") claim, the statute of limitations for the submittal of which is six (6) years from the date of its accrual, provided in the interim he declines to accept any government offer of "final contract payment" and release of claims.<sup>20</sup>

A simple explanation of why the government is being just a bit disingenuous with its demand for a rush-to-submittal may be that it wishes to unfairly minimize its unabsorbed overhead damages exposure.<sup>21</sup> Contractor blunders made in producing REAs in an unreasonably constricted time frame will facilitate this, as such blunders are broader targets for the CO's claim defense-savvy technical and legal helpers to aim at. Nothing discredits a claim like money damages generated by contractor overreaching – done innocently or not. Taken to the extreme, the government has a penchant to threaten, and sometimes actually file, counterclaims alleging contractor fraud, many of which are withdrawn upon the contractor's agreement of claim forfeiture.

## Does Government Bias Exist In Contract Administration?

Finally to this aspect, a few COs and their helpers have biased opinions about contractors,<sup>22</sup> particularly so with regard to claims.<sup>23</sup> Unfortunately, in some instances this stems from an anti-contractor culture created at the agencies' various departments. The example below is from a chat room-blog spot sort of "club" of current and former

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<sup>19</sup> Mega-prime government contractors, and other primes as well, are not noted for sharing with their subs inside correspondence or information passed between them and the government.

<sup>20</sup> 41 U.S.C. § 605(A). "Accrual" occurs when the contractor properly certifies his REA as a CDA claim, if and when mutual agreement on the REA is declined by the government.

<sup>21</sup> No contractor wants to inordinately delay its damages recovery process, but the smart ones want time enough to "get it right".

<sup>22</sup> *Penner Installation Corp. v. United States*, 116 Ct. Cl. at 564, 89 P. Supp. 545 (1950): (Some contracting officers regard themselves as representatives of [the Government], charged with the duty of protecting its interests and of exacting of the contractor everything that may be in the interest of the Government, even though no reasonable basis therefore can be found in the contract documents; but the Supreme Court has said that in settling disputes this is not his function; his function, on the other hand, is to act impartially.)

<sup>23</sup> There is no argument here that contractors have flawless integrity.

government CO types out of various agencies, who are predominately all very professional and smart about government regulations and contracting procedures. This excerpt is the decided exception, far, far in the minority, we hope:

FAR 52.242-14 states:<sup>24</sup>

(a) The Contracting Officer may order the Contractor, in writing, to suspend, delay, or interrupt all or any part of the work of this contract for the period of time that the Contracting Officer determines appropriate for the convenience of the Government.

(b) If the performance of all or any part of the work is, for an unreasonable period of time, suspended, delayed, or interrupted (1) by an act of the Contracting Officer in the administration of this contract, or (2) by the Contracting Officer's failure to act within the time specified in this contract (or within a reasonable time if not specified), **an adjustment shall be made for any increase in the cost of performance of this contract** (excluding profit) **necessarily caused by the unreasonable suspension, delay, or interruption, and the contract modified in writing accordingly.** However, no adjustment shall be made under this clause for any suspension, delay, or interruption to the extent that performance would have been so suspended, delayed, or interrupted by any other cause, including the fault or negligence of the Contractor, or for which an equitable adjustment is provided for or excluded under any other term or condition of this contract.

Question #1 - If it has been determined that the delay is both excusable (Defaults clause) and compensable (Suspension of Work clause), what is the best way to isolate the costs that should be considered for providing relief of actual costs for FOOH, Design and/or HOOH as a result of the delay? **Typically contractors try to load up a cost pool to come up with a daily rate** and then multiply times the number of days of delay. However, if there is no idle equipment and only very limited labor costs as a result of suspension, **is there anything due the contractor?**

Question #2 - **What would be the reasons to NOT issue a suspension of work, if you know there is going to be a delay in giving NTP** or allowing some part of critical path works to commence? Isn't the contractor already on notice about suspension at the convenience of the Gov't, by virtue of the clause being in the contract? **[Highlights and footnote added.]**

This bureaucrat is clearly biased; they “try to load up a cost pool”, says he, seeking to maximize their home office overhead (“HOOH”) recovery. This is next to impossible. Because the allocable pool will have to be stripped out of the contractor’s existing financial statements prepared by his accountant at either the “review” or “audit” level, challenged and further stripped of non-FAR-compliant entries by the contractor’s consultant; and finally thoroughly challenged by the DCAA auditors, padding the pool would be folly and might even bring down a fraudulent claim case from the government. He has the contractor-biased bright idea that when essentially no work has been performed, and the government can show essentially no direct costs have been expended by the contractor; and (probably also) when no billings have thus been generated as a result to install into the Eichleay formula, he wants to know if the government can’t simply go into denial by failing to issue the Suspension of Work Order. He believes this would nullify the contractor’s key element to its prima facie entitlement case, i.e., that government-caused suspension even exists. He is looking for some peer-blogger to support this.

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<sup>24</sup> FAR: Federal Acquisition Regulation.

## More Government Contract Administrators Than Not Aim At Professionalism

One of his more professional peer-COs answered him thus:

Regarding "design costs," what are you referring to? Not enough information to formulate any opinion or advice.

"Question #2 - What would be the reasons to NOT issue a suspension of work, if you know there is going to be a delay in giving NTP or allowing some part of critical path works to commence? Isn't the contractor already on notice about suspension at the convenience of the Gov't, by virtue of the clause being in the contract?"

From the clause and the above discussion, you should be able to see that:

1) You don't have to direct a suspension of work for the contractor to request an adjustment as a constructive suspension of work and:

2) It is potentially worse if you allow the contractor to be constructively suspended from performance of work for an indeterminate period than if you issue a formal suspension for a determinate period.

If the period is indeterminate and the contractor is in limbo, it will more than likely be entitled to unabsorbed daily home office overhead, calculated using the Eichleay formula. If you issue a suspension for a determinate period, you might only be liable for any increased cost impacts, such as inflation or the like. If the period is indeterminate, you might be liable for both that and unabsorbed OH costs. You can issue a definite delay notice and if it needs to be extended, extend it. If the delay will certainly be resolved early, you can contact the contractor and ask if it could mobilize or remobilize earlier than the original suspended delay period.

## Government Contracting In The Real World – The Stunning Negative Impact Of Major Contract Suspension On Small Contractors

Our contractor began as a family business 40 years ago. Client, banking and surety relationships have always been strong. Before taking on this contract, the contractor's maximum work backlog had never exceeded \$9,000,000, more often, \$6MM to \$8MM, all private or non-federal government public work. Since the suspension of work order eight months prior, the contractor had shifted underutilized extra key supervision and other extra personnel from job to job at other sites in order to have them available at a moment's notice for when the government might lift the suspension.

Meanwhile, a pre-government contract work program which had been steadily throwing off about six to eight million cash income each year, had wilted to a mere dwarf of its previous self, the \$8MM government contract part paralyzed for eight (8) months. This much stifled income for this long translates directly to drastically reduced corporate retained earnings, which will not be transparently apparent until the next fiscal year-end financial report. This is when, at the latest, working capital and surety bond lines will be reviewed by his banking and bonding support.

Retained earnings on his new financial statement will have melted from the previous report to smaller than Al Gore's prediction of the polar ice caps in the worst case global warming scenario. Unless these contractor supporters are beyond exceptional, the bond company will demand a major personal cash infusion into the corporation by the

principals - just to *maintain* the current bond level. Next, the bank will want more property pledged as working capital collateral. As for what the government cares about this unfair situation, he could interview all the government bureaucrat authorities<sup>25</sup> all the way up to the department secretary, present them with this unjust situation, and in return get only blank stares.

There is no hope that any recovery of contract damages he may ultimately prove and eventually receive will completely make whole the final corporate damages which will result. He has no choice but to march on, completing the government contract while essentially financing it in the process, meanwhile vigorously pursuing the REA – and/or ultimately, the CDA-certified unabsorbed overhead claim – and financing that as well.

### Never Forget – In Government Contracting It Is The Government Who Is In Control Of The Small Contractor’s Business Continuity, NOT The Contractor

Perhaps the most unjust element of all in this and similar government contractor claim situations is the total government control of the time lapse between contractor identification and proof of the cost of, and entitlement to, damages for a government-caused contract problem - and the contractor’s actual receipt of the funds, if any.

To illustrate, both Nikon<sup>17</sup> and our contractor were small contractors. Both were awarded Government contracts. Both contracts were suspended by the government before any work could start. Both suspensions were for the better part of a year, ours for eight months, Nikon’s for 288 days. Both were placed in a standby position by the government. Both being small contractors, the instant government contract of each was a major financial element in its overall surety bonded work program. Both had (have) a prima facie case for entitlement to unabsorbed overhead.<sup>26</sup> Failure of reasonably prompt, fair, recovery of resulting damages by either may well be critical to its contracting business continuity.<sup>27</sup>

### Further To The *Nicon* Saga

Seeking fairness and justice, more than five (5) years after award and then near-immediate government suspension of its contract, Nikon found itself at its second Federal court.<sup>28</sup> That court ordered the case back to the lower Federal court instructing that court, which had summarily dismissed the case (the reason Nikon had to appeal to the instant court), with the instructions for it to seek to determine whether, given the unique case facts, there was not some other way besides Eichleay to allocate unabsorbed overhead to the suspended contract.

Meanwhile over this course of time, two different construction claims consulting firms had been applying their considerable expertise to the case on Nikon’s behalf. Both claim in their current advertising they made positive contribution to the case, one apparently

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<sup>25</sup> If they could be found.

<sup>26</sup> My own view in respect to our subject contractor.

<sup>27</sup> Nikon does not appear in the Federal Business Opportunities archives as having received any of the 20,800 some government construction contract awards since the earliest archive, April 6, 1999.

<sup>28</sup> <http://www.ll.georgetown.edu/FEDERAL/judicial/fed/opinions/02opinions/02-5097.html>

consulting with Nikon's attorney to negotiate \$184,757 in direct field costs and "related overhead" at the lower court in 2001, while the other directed its service to cooperation with Nikon's attorney in pursuit of the \$387,513 in unabsorbed home office overhead before the second, appeals, court.<sup>29</sup>

As of June 2003, after over five (5) years of negotiations supported by the not inexpensive services of three (or four) claims and legal advisors, Nikon was now faced with seeking fairness and justice before the same lower court which had on summary judgment<sup>30</sup> dismissed the case two years earlier.

Nikon was now facing another year at least before briefing could be completed and the court would produce a ruling. Since I can find no record of Nikon's appearance before the lower court again, I reasonably conclude that Nikon cut its losses and made some final deal with the government for enough to perhaps cover its legal and consulting costs, and together they petitioned the court for dismissal, ending the issue.

### Some Layman's Insight Into The Contradictions Within The Federal Claims Tribunals

This of course left hanging for lack of authoritative decision exactly how a contractor is to calculate unabsorbed overhead damages when Eichleay does not apply, i.e., when the government suspends a contract when the contract billings remain at zero. But does it? Hold on.

Since early in the previous decade, the various boards of contract appeals have been re-charted by Congress as being peer tribunals with the current U.S. Court of Federal Claims ("Claims Court"), the lower court to which Nikon initially brought its claim. Contractors, even before the time Congress made the change, had a choice; they could, and can now, bring appeals from a CO's decision to either the Claims Court or to the appropriate board of contract appeals. Since the time Congress made this change, the appeals of contractors whose claims are denied at either the boards or at the Claims Court must make their final appeal to the Federal Circuit Court of Appeals. Before that time, contractors with rejected claims at the boards made their appeals to the Claims Court (under its various earlier names).

It has been said by various legal writers that this situation has been non-conducive to almost any cross proliferation of case law after the Congressional change of court-board peer standing. The boards generally ignore the precedents set by the Claims Court and vice versa.

This lengthy explanation sets the stage for analysis of the following hypothetical scenario. Suppose Nikon had chosen to appeal its CO's decision to the Armed Services Board of Contract Appeals (ASBCA"), not the Claims Court. Had it done so, there is a

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<sup>29</sup> The appearance of two different consulting firms at two different courts addressing the same or related issues, in the same case usually indicates the involvement of two different law firms.

<sup>30</sup> Dismissal on government motion without a hearing.

strong likelihood the ASBCA would have found for Nikon, not summarily dismissed the case as did the Claims Court.<sup>31</sup>

In *The Appeal of – Genisco Technology Corporation*, ASBCA No 49664, April 7, 1999,<sup>32</sup> ASBCA emphatically found that estimates of elements of an Eichleay formula, ***when actual figures were not available, were permissible***. The contractor had met a situation like Nikon's; there had evidently been an award protest, and the contractor had calculated unabsorbed overhead by other means, avoiding Eichleay on the excuse, exactly like in *Nikon*, and our contractor's situation, there were no billings as the contract had been suspended by the government before any could be generated:

Appellant seeks reconsideration of our decision denying its appeal. In *Genisco Technology Corporation*, ASBCA No. 49664, 99-1 BCA ¶ 30,145 (*Genisco*), we denied appellant's claim for unabsorbed overhead because it had not been computed using the + formula, and we concluded that use of the Eichleay formula was mandatory, citing *West v. All State Boiler, Inc.*, 146 F.3d 1368 (Fed. Cir. 1998) and *Libby Corporation*, ASBCA No. 40765, 96-1 BCA ¶ 28,255. *Genisco* also rejected the modified Eichleay computation appellant presented at the hearing because we found the computation to be based on financial data that was seriously incomplete. Appellant alternatively requests that we reopen the record to receive additional financial data and a revised Eichleay computation. Respondent opposes both reconsideration and the reopening of the record. The parties have submitted a considerable quantity of additional material with the motions and opposition.

#### THE MOTION FOR RECONSIDERATION

Appellant essentially raises the same arguments we rejected in *Genisco*. Appellant first argues that respondent is estopped from asserting that use of the Eichleay formula is mandatory here because the governing clause, FAR 52.233-3, Protest After Award (AUG 1989) makes use of the Eichleay formula impossible. That clause provides for filing a claim within 30 days after the work stoppage ends, although "the Contracting Officer may receive and act upon a proposal submitted at any time before final payment under [the] contract." We rejected that argument, pointing out that an Eichleay claim can be filed using estimates and that appellant's claim as submitted without using Eichleay did, in fact, use estimates. *Genisco* at 149,128. As respondent argues, we have held that claims based on estimates are proper under the Contract Disputes Act (CDA), 41 U.S.C. §§ 601-613, as amended. See, e.g., *Allied Signal Aerospace Co.*, ASBCA No. 46890, 94-3 BCA ¶ 27,089. Indeed, even DCAA recognizes that complete financial data may not be available when an unabsorbed overhead claim is filed and sanctions the use of estimates in formulating an Eichleay claim. See DCAA Contract Audit Manual, ¶ 12-804 b., July 1997. Moreover, as respondent also points out in its opposition, the clause specifically authorizes consideration of claims filed more than 30 days after the work stoppage has ended. Respondent cites examples of cases where claims filed under FAR 52.233-3 more than 30 days after the work stoppage had ended were considered without challenge or comment on the date of filing (*Interstate General Government Contractors, Inc.*, ASBCA No. 43369, 92-2 BCA ¶ 24,956, *aff'd* 12 F.3d 1053 (Fed. Cir. 1993); *FMC Corporation, Steel Products Division*, ASBCA No. 39546, 92-3 BCA ¶ 25,025).

Appellant next argues that our decision effectively eliminates FAR 52.233-3 from the contract. As stated above, decisions of this Board and our appellate court have adjudicated claims under FAR 52.233-3 using the Eichleay formula. Other decisions of this Board and our appellate court have held that unabsorbed overhead may only be calculated by use of the Eichleay formula. Our view is that a common sense reconciliation of those decisions to FAR 52.233-3 would result either in submission of unabsorbed overhead claims thereunder by use of estimates, or with the agreement of the contracting officer that he or she will consider such claims after 30 days but before final payment, as the clause provides. We are unpersuaded by appellant's argument that, under *Genisco*, a contracting officer could never award unabsorbed overhead pursuant to FAR 52.233-3 because a contractor would never have

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<sup>31</sup> True, the same ultimate result might have occurred if the government were to have appealed a ASBCA decision made in favor of Nikon to the Federal Circuit, but far less likely due to ASBCA's own precedent and ASBCA's pointing to DCAA's recognition of estimate use in Eichleay.

<sup>32</sup> Motion for reconsideration by the contractor.

enough information to file an Eichleay claim. As pointed out above, even the DCAA Audit Manual recognizes that estimates will be used in Eichleay calculations.

Notably, twice, the ASBCA pointed to “decisions of ... our appellate court [the Federal Circuit]” as predicate for mandatory use of Eichleay for figuring unabsorbed overhead. ASBCA pointedly stated that it has held in a previous case that “claims based on estimates” are acceptable. Finally, “...even the DCAA<sup>33</sup> ....recognizes...” Eichleay calculated with estimates, said the ASBCA.<sup>34</sup>

### Government Contract Administrators' Disingenuous Behavior And Its Impact On Small Contractors

This ASBCA decision also leaves absolutely no doubt that neither the government nor its prime contractor has the authority to enforce a 30 (or 20) day turnaround from the date of the lifting of a government-ordered work suspension on its submittal of its REA or claim.

It is clear to me that our small contractor and his sub-contractor peers are about to become educated in government contract claim tactics, at considerable expense, I might add.<sup>35</sup> In contract administration, the government never does anything of major impact without planning by the CO’s “committee.” This includes using unfair tactics to nullify or disguise contractors’ claim rights of recovery. The long period of suspension with little to no information from the government or the mega-prime, coupled with the near-immediate suspension after award was, I wager, by government design. In all probability the government knew before the bid it had serious site access permit issues which could not possibly be resolved before time to issue the NTP.<sup>36</sup> Yet it proceeded to bid and award the project anyway.<sup>37</sup> You may be sure the government was acutely aware that on a suspended project with no work accomplished the contractors’ largest expense would be unabsorbed overhead. Just as surely the CO’s legal helpers knew what little chance a contractor has to prevail on recovery of those costs given the facts about *Nicon* I have described above.

### “Toto, I’ve A Feeling We’re Not In Kansas Anymore”<sup>38</sup>

Now the government will play hardball; it will stall, deny and unreasonably reject the subs’ REA’s over the coming months, driving the contractors to the CDA-certified claims stage, and on to litigation before the ASBCA or the Claims Court, smug in the knowledge

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<sup>33</sup> With obvious reverence for the weight that venerable government watchdog throws.

<sup>34</sup> This decision permitting estimates for unavailable actual elements required in Eichleay came on April 7, 1999. On December 21, 2001, without a formal hearing, with no recognition whatever of its peer tribunal, ASBCA’s, precedent decision; and with essentially the same suspended contract and no-billings fact situation, the Claims Court dismissed *Nicon*’s case, holding “that *Nicon* could not recover damages for home office overhead under the Eichleay formula because the formula could not be modified to fit a fact situation where the contractor has not yet begun to perform”.

<sup>35</sup> The contractor did not engage my advisory service. I wish him well. In business 40 years providing jobs for the skilled and unskilled as well, he deserves better than he will probably get.

<sup>36</sup> In government contract claim parlance this is called “Abuse of Superior Knowledge”. It is also “Bad Faith and Unfair Dealing”.

<sup>37</sup> Why? Budgets and end-of-fiscal-year funds commitments often play a part in such government decisions.

<sup>38</sup> *The Wizard Of OZ*, Dorothy to her dog Toto after the cyclone had subsided.

that they will spend hundreds of thousands in legal fees for attorneys and claims consultants of lesser and greater skills, where some (probably most) will exhaust themselves financially, becoming ripe for final settlement of pennies on the dollar (or nothing) – all literally years later.

How did government contract justice get to be this way? Is three courts, six years and final resolution for pennies on the dollar in “negotiations”<sup>39</sup> with the government agency which created the stalling and delaying tactics in the first place, fair?<sup>40</sup> Who will serve notice on government and its mega-prime contractors they must not use sly bullying tactics like fictitiously short submittal periods to facilitate government advantage in negotiations? What’s with this thing with the lower peer tribunals where each ignores the decisions of the other? What’s with the mighty Federal Circuit which perpetuates this ridiculous situation? Why do we even need the boards if the Claims Court is permitted to ignore their decisions as if they don’t even exist? Or vice versa? Which lower tribunal should our contractor choose if fairness can’t be found at the CO level? He will need to decide that immediately. But how could he make that decision? If he calculates the claim by estimating the financial and time elements required in the Eichleay and brought that to the ASBCA in appeal from a negative CO decision, would the board stand by its *Genisco* decision or would it immediately buckle in deference to the Federal Circuit’s current position that Eichleay cannot be used where no contract billings have been generated? If the board upheld the contractor’s use of estimates, the government would surely appeal to the Federal Circuit. Would the Circuit then do as in *Nicon* and simply run it back to the board to determine another way to make the calculation? Can anyone guess the time which would elapse in this tortured process?

These and similar questions stand starkly begging for answers. I hope and plan to address some of them or ones similar in the very near future.

Your comments are graciously invited.

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<sup>39</sup> Exactly how *Nicon* ended up is not completely clear but the documents readily available online point inexorably to this result.

<sup>40</sup> “Justice delayed is justice denied”. *William Gladstone*.