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SECOND SERIES

PRACTICAL TIGHT-KNIT BRIEFINGS INCLUDING ACTION GUIDELINES ON GOVERNMENT CONTRACT TOPICS

PREPARING TERMINATION FOR CONVENIENCE SETTLEMENT PROPOSALS FOR FIXED-PRICE CONTRACTS

By Paul J. Seidman and Robert D. Banfield

As the pace of Government downsizing continues to increase, terminations for convenience—cancellations of contracts by the Government simply because its needs change and regardless of contractor fault—have become more common as cost-saving measures.¹ These cancellations are carried out pursuant to the “Termination for Convenience of the Government” contract clause, which gives the Government broad rights to terminate a contract when termination is in the Government’s interest.² In return for this privilege, the Government agrees to reimburse the contractor for (a) all reasonable and allocable performance costs, (b) certain post-termination costs, (c) a reasonable profit on (a) and (b), and (d) settlement expenses.³

This basic formula for contractor recovery following a convenience termination was discussed in detail in an earlier BRIEFING PAPER by the authors entitled “Maximizing Termination for Convenience Settlements,” published in April 1995.⁴ That PAPER presented general strategies you can follow if you are a contractor

to maximize recovery following a termination for convenience, including claiming otherwise unallowable costs under the Federal Acquisition Regulation “fair compensation” principle, not allowing the Government improperly to disallow costs by substituting its after-the-fact business judgment for that of the contractor, not accepting cost disallowances based on impractical proof requirements imposed by the Government, claiming all allowable costs, charging normally indirect costs directly, avoiding loss adjustments, requesting a partial payment, and obtaining

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professional help. It also described steps you can take to recover costs that are frequently overlooked or are disallowed by the Government, such as the costs of contractor-caused delays and defective or nonconforming work, precontract costs, idle facilities and idle capacity costs, rental costs, facilities capital cost of money, costs of common items, costs under first article contracts, general and administrative expenses on subcontractor settlements, settlement expenses, and interest.

To protect your interests following a convenience termination, however, you must know not only *what* costs to claim but *how* to claim them. Focusing on fixed-price contracts, this BRIEFING PAPER, a companion to the previous PAPER, provides practical advice on how to prepare an effective termination for convenience settlement proposal. In addition to discussing the *time limits* for the submission of a termination settlement proposal and identifying the required *components of a settlement proposal*, the PAPER advises how to (1) choose between the *inventory* and *total cost proposal* bases, (2) prepare *Standard Form 1435, "Settlement Proposal (Inventory Basis),"* and *SF 1436, "Settlement Proposal (Total Cost Basis),"* (3) complete *inventory schedules* (SF 1426 to SF 1432), the *"Schedule of Accounting Information"* (SF 1439), and the *"Application for Partial Payment"* (SF 1440), (4) *incorporate requests for equitable adjustments* with the settlement proposal, and (5) *recover interest* on the amount of the settlement proposal under the *Contract Disputes Act*.

Time Limits

A prime contractor must submit its "final" termination settlement proposal to the Government *within one year of the effective date of the termination*.⁵ The "effective date of termination" is the date on which

the notice of termination requires the contractor to stop performance. If, however, the contractor receives the notice after the date fixed for termination, then the "effective date of termination" is when the notice of termination is first received.⁶

The deadline for a subcontractor to submit its proposal to a prime contractor (or higher-tier subcontractor) is set forth in the subcontract. The period is often six months or less than that allowed the prime contractor to submit its settlement proposal to the Government.

The period allowed for submitting a proposal can be extended by the Termination Contracting Officer, prime contractor, or higher-tier subcontractor. A prime contractor or subcontractor must request a time extension *in writing* before the deadline.⁷ Deadlines must be met at any cost even if the proposal needs to be revised at a later date. If a deadline is not met, a contractor forfeits its right to judicial review of the amount the CO determines is owed. In other words, if you fail to submit a timely "final" settlement proposal, the CO can pay whatever the CO decides, and you are without a remedy.⁸ The same forfeiture rule is incorporated in most subcontracts.

If only *part* of the contract or subcontract is terminated, a contractor is entitled to an *equitable adjustment* of the price of the continued portion of the contract or subcontract to reflect the fact that there is less work over which to spread fixed costs.⁹ The "Termination for Convenience" clause requires that a prime contractor submit any request for an equitable adjustment following a partial termination within 90 days unless this period is extended in writing by the CO.¹⁰ A subcontractor should look to its subcontract to determine the deadline for submission of a request for an equitable adjustment.

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★ Although prepared by experts, these papers are, of course, generalized and should not be considered a substitute for professional advice in specific situations. ★

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Settlement Proposal Components

■ Required Forms

At a minimum, a termination for convenience settlement proposal requesting \$10,000 or more¹¹ must include the following Standard Forms:

- (a) *Either* SF 1435, "Settlement Proposal (Inventory Basis)" *or* SF 1436, "Settlement Proposal (Total Cost Basis)."¹² (These two forms appear as appendices to this PAPER.)
- (b) The following inventory schedules (if applicable): SF 1426, "Inventory Schedule A (Metals in Mill Product Form)" (and SF 1427, "Continuation Sheet"); SF 1428, "Inventory Schedule B" (and SF 1429, "Continuation Sheet"); SF 1430, "Inventory Schedule C (Work-in-Process)" (and SF 1431, "Continuation Sheet"); SF 1432, "Inventory Schedule D (Special Tooling and Special Test Equipment)" (and SF 1433, "Continuation Sheet").¹³
- (c) SF 1439, "Schedule of Accounting Information."¹⁴

■ Description Of Cost Elements

Neither SF 1435, "Settlement Proposal (Inventory Basis)," nor SF 1436, "Settlement Proposal (Total Cost Basis)," provides sufficient space to describe adequately a contractor's claimed costs. It is therefore good advocacy to provide a "Description of Cost Elements" setting forth the factual and legal bases of your claimed costs.

A thorough explanation of your claimed costs is particularly important if your settlement proposal requests costs that would otherwise be unallowable under the FAR Part 31 cost principles. Although the FAR cost principles are used to determine the allowability of costs in a termination settlement, they are not applied strictly. Instead, when a contract is terminated for convenience, the cost principles are applied "subject to" the overriding general rule that the terminated contractor is entitled to "fair compensation."¹⁵ The FAR states that a settlement "should compensate the contractor fairly for the work done and the preparations made for the terminated portions of the contract, including

a reasonable allowance for profit," and that the "use of business judgment, as distinguished from strict accounting principles, is the heart of a settlement."¹⁶ Absent an explanation why allowance of otherwise unallowable costs is necessary to provide "fair compensation," however, the Government will perfunctorily disallow the costs. If you claim normally unallowable costs and the contract is subject to Cost Accounting Standards, you may be accused of violating CAS 405, "Accounting for Unallowable Costs."¹⁷ Even worse, you could be accused of violating the criminal or civil False Claims Acts.¹⁸ Thus, it is essential that you provide an adequate explanation in the "Description of Cost Elements" when claiming normally unallowable costs under the "fair compensation" principle.

■ Application For Partial Payment

A prompt partial payment may allow a contractor in need of immediate cash to avoid being forced to accept an unreasonably low termination settlement. You should therefore almost always submit SF 1440, "Application for Partial Payment,"¹⁹ with your termination settlement proposal and insist on prompt action.²⁰

Inventory Basis vs. Total Cost Basis

There are two methods of preparing termination settlement proposals: (1) inventory basis and (2) total cost basis.²¹ For the inventory basis, SF 1435, "Settlement Proposal (Inventory Basis)," is used. A total cost basis settlement proposal is prepared on SF 1436, "Settlement Proposal (Total Cost Basis)."

In preparing an *inventory basis* proposal on SF 1435, direct material costs, direct labor costs, and indirect factory expenses are allocated to various categories of termination inventory rather than claimed as lump sums. The categories of inventory to which direct material costs, direct labor costs, and indirect factory expenses are allocated are set forth as Items 1 through 7 in Section II of SF 1435: Item 1, "Metals"; Item 2, "Raw Materials"; Item 3, "Purchased Parts"; Item 4, "Finished Components"; Item 5, "Miscellaneous Inventory"; Item 6, "Work-in-Progress"; and Item 7, "Special Tooling and Special Test Equipment." Under the inventory basis, direct material costs, direct labor costs, and indirect factory expenses claimable as "other costs" are not

allocated to inventory but are claimed under Item 8, "Other Costs." One example of "other costs" is "initial costs," which include starting load and preparatory costs.²²

In contrast, in a *total cost basis* proposal prepared on SF 1436, direct material costs, direct labor costs, and indirect factory expenses are claimed as lump sums rather than allocated to categories of inventory, with the possible exception of the category of special tooling and special test equipment. Although, where the total cost approach is used, the FAR does not require that these costs be allocated to special tooling and special test equipment,²³ since special tooling and special test equipment appear as a separate item on SF 1436, contractors often allocate direct material costs, direct labor costs, and indirect factory expenses to this category of inventory. This approach is illustrated by the first four Items in Section II of SF 1436: Item 1, "Direct Material"; Item 2, "Direct Labor"; Item 3, "Indirect Factory Expense (from Schedule A)"; and Item 4, "Special Tooling and Special Test Equipment (SF 1432)." In addition, under the total cost approach, direct material costs, direct labor costs, and indirect factory expenses claimable as "other costs" (such as "initial costs") are not claimed under these categories but are claimed under Item 5, "Other Costs."

The use of the inventory basis (SF 1435) is preferred under the FAR²⁴ except when there is a *complete* termination of a *construction* or a *lump-sum professional services* contract. For these special situations, where there is normally little or no inventory, contractors must use the total cost basis.²⁵

You must obtain *advance permission* from the CO to use the total cost approach for other than the complete termination of a construction or a lump-sum professional services contract. The FAR permits COs to approve use of the total cost basis where use of the inventory basis is "not practicable" or "will unduly delay settlement."²⁶ The FAR lists the following nonexclusive examples of situations in which use of the total cost basis is appropriate:²⁷

(i) If production has not commenced and the accumulated costs represent planning and preproduction or "get ready" expenses.

(ii) If, under the contractor's accounting system, unit costs for work-in-process and finished products cannot readily be established.

(iii) If the contract does not specify unit prices.

(iv) If the termination is complete and involves a letter contract.

In general, you should consider requesting permission to use the total cost basis if your contract is terminated before production commences or if your unit costs cannot be readily established.

In theory, a contractor's recovery following a termination for convenience should be the same under either the inventory basis or total cost basis.²⁸ The costs are the same. The only difference is that direct material costs, direct labor costs, and indirect factory expenses are accounted for differently. However, this is not necessarily true if the Government alleges that the contract was being performed at a *loss*. When the Government terminates a loss contract, the terminated contractor is not entitled to profit and its recovery is reduced by a loss adjustment. Under a loss adjustment, the contractor's termination costs, not including settlement expenses, are reduced by the percentage of loss the contractor would have incurred had the contract been completed.²⁹

If a loss contract is alleged, you may fare better using the inventory basis. Under the inventory basis, acceptable finished product is subtracted from contractor costs in determining whether a contract is being performed at a loss. This deduction is not made where the total cost basis is used.³⁰ Examples illustrating the application of the loss adjustment under the two methods are provided in the Defense Contract Audit Agency *Contract Audit Manual*.³¹

Before deciding whether a potential loss adjustment is reason for not requesting permission to use the total cost approach, you should calculate your potential recovery under the two methods and compare the results. You should also give consideration to the techniques discussed in the earlier 1995 BRIEFING PAPER for avoiding loss adjustments. These techniques include (a) submitting equitable adjustment claims to which you are entitled to raise the contract price and (b) holding the Government to its burden of proving there would be a loss and the amount of the loss.³²

You should submit a request for permission to use the total cost approach to the CO as soon as possible. If the CO does not respond in a timely

manner, you should request a time extension before the deadline for submitting your settlement proposal citing the CO's delay in responding to your request as ground for the extension. As discussed previously in this PAPER, you should never fail to meet the deadline for submission of a "final" settlement proposal.³³ Thus, if a time extension is not forthcoming and using the total cost basis is the only way to submit a timely proposal, you should consider submitting a proposal under the total cost basis without advance approval. The Armed Services Board of Contract Appeals has indicated that a CO's right to require use of the inventory basis is not absolute.³⁴

Inventory Basis (SF 1435)

■ Background Information

SF 1435, "Settlement Proposal (Inventory Basis)," begins by requesting you to provide the following background information: (a) whether the settlement proposal is for a prime contract with the Government or for a subcontract or purchase order, (b) the name and address of the terminated contractor or subcontractor, (c) identification of the contractor or Government agency that sent the notice of termination, (d) the number of the terminated Government prime contract or of the subcontract or purchase order, (e) the name of any assignee, (f) the effective date of the termination, (g) whether this is an interim or final proposal, and (h) whether SF 1439, "Schedule of Accounting Information," is attached or an explanation why it is not attached.

A few words about the last two items are in order. First, you should consider submitting an interim proposal and, as discussed in more detail later in this PAPER, an accompanying SF 1440, "Application for Partial Payment," to facilitate a partial payment.³⁵ Second, the FAR requires that SF 1439, "Schedule of Accounting Information," always be provided in support of a settlement proposal (unless the proposal is filed on SF 1438, "Settlement Proposal (Short Form)," used for proposals under \$10,000).³⁶ However, contractors sometimes do not provide SF 1439. As discussed below, both SF 1435 and SF 1436 ask for an explanation if SF 1439 is not provided.

■ Section I—Status At Termination

Section I of SF 1435 provides for a computation of the contract price at the effective date of termination. Since the contract price is a ceiling on contractor recovery other than settlement expenses,³⁷ this computation is a critical element of your settlement proposal. The contract price at the time of termination is the price as originally awarded plus any equitable adjustments to which you are entitled. You need only prove incurrence to recover costs up to the original contract price. To recover additional amounts, you must prove entitlement to a commensurate equitable adjustment.³⁸

■ Section II—Proposed Settlement

Section II of SF 1435, Items 1 through 20, provides a format for summarizing and computing claimed costs. Schedules A through H on pages 2 to 4 of the form provide space for a more detailed explanation of claimed costs, credits, and payments received to date. In addition to Schedules A through H, it is useful to include a separate "Description of Cost Elements" setting forth the legal and factual bases for claimed costs.

Each Item (1–20) in Section II of SF 1435 is discussed in the paragraphs that follow.

■ Items 1 Through 7

(a) *Item 1, "Metals"*—Item 1 should set forth the amount claimed for metals *at cost*, including any freight charges, as listed in SF 1426, "Inventory Schedule A (Metals in Mill Product Form)." An explanation should be provided in the "Description of Cost Elements" of any difference between the amount claimed at Item 1 and that claimed in SF 1426. The amount on SF 1426 is often less due to losses during production.

(b) *Item 2, "Raw Materials (other than metals)"*—Item 2 sets forth the amount claimed for raw materials *at cost*, including freight, as listed in SF 1428, "Inventory Schedule B." Inventory Schedule B is for all raw materials other than the metals listed on SF 1426, "Inventory Schedule A." You should use a separate Inventory Schedule B for raw materials (Item 2), purchased parts (Item 3), and finished components (Item 4).³⁹ An explanation should be provided in the "Description of Cost Elements" for any difference between the amount claimed for raw

materials in Item 2 and the amount claimed in SF 1428, "Inventory Schedule B." The amount on SF 1428 is often less due to losses during production.

(c) *Item 3, "Purchased Parts"*—Item 3 sets forth the amount claimed for purchased parts *at cost*, including any freight charges, as listed in SF 1428, "Inventory Schedule B" (which should be a form separate from the schedule forms used for raw materials (Item 2) and finished components (Item 4)).⁴⁰ The "Description of Cost Elements" should explain any difference between the amount claimed for purchased parts at Item 3 and SF 1428, "Inventory Schedule B." As with raw materials, the amount on SF 1428 is often less due to losses during production.

(d) *Item 4, "Finished Components"*—Item 4 sets forth the amount claimed for finished components listed on SF 1428, "Inventory Schedule B" (on a form separate from those used for raw materials (Item 2) and purchased parts (Item 3)).⁴¹ Finished components should not be confused with "acceptable finished product," which is listed at Item 15. Finished components are parts of contract line items; acceptable finished products are the contract line items.

The amount claimed for finished components is composed of direct labor costs, direct material costs, and indirect factory expenses. An analysis of the amount of direct labor costs, direct material costs, and indirect factory expenses included in the amount claimed should be provided in Schedule A of SF 1435, "Analysis of Inventory Cost (Items 4 and 6)." The "Description of Cost Elements" should explain any difference between the amount claimed for finished components at Item 4 and the amount claimed in SF 1428, "Inventory Schedule B."

(e) *Item 5, "Miscellaneous Inventory"*—Item 5 sets forth the amount claimed for miscellaneous inventory. This item will be blank if the inventory all falls into other categories.

(f) *Item 6, "Work-in-Progress"*—Item 6 sets forth the amount claimed for work-in-process as listed on SF 1430, "Inventory Schedule C (Work-in-Process)." For some inexplicable reason, Item 6 is for listing "Work-in-Progress," while the "Inventory Schedule C" is for reporting "Work-in-Process." These items are the same.

The amount claimed is composed of direct material costs, direct labor costs, and indirect factory expenses. An analysis of the amount of these costs included in the amount claimed for work-in-progress should be set forth in Schedule A of SF 1435, "Analysis of Inventory Cost (Items 4 and 6)." An explanation should also be provided in the "Description of Cost Elements" for any difference between the amount claimed for work-in-progress at Item 6 and the amount claimed in SF 1430, "Inventory Schedule C." The amount on SF 1430 is often less due to losses during production.

(f) *Item 7, "Special Tooling and Special Test Equipment"*—Item 7 is for the "loss of useful value" of special tooling and special test equipment used to manufacture contract end items. Inventory of this type is listed on SF 1432, "Inventory Schedule D (Special Tooling and Special Test Equipment)."

"Loss of useful value" is the unutilized value of special tooling and special test equipment resulting from the termination. Under the FAR "Termination costs" cost principle, which governs the allowability of certain costs peculiar to contract terminations and is used in conjunction with the other cost principles,⁴² "loss of useful value" is "that portion of the acquisition cost which bears the same ratio to the total acquisition cost as the terminated portion of the contract bears to the entire terminated contract and other Government contracts for which the special tooling, or special machinery and equipment was acquired."⁴³ Only "special" tooling, machinery, or equipment qualifies for recovery as "loss of useful value" assets. In this context, the FAR defines "special" as meaning of such a specialized nature that the item's use is limited to "the development or production of particular supplies or parts" or to "the performance of particular services."⁴⁴

■ Item 8—Other Costs

Item 8 is for indicating the total of "Other Costs" detailed on Schedule B of SF 1435. As previously discussed, a contractor's recovery is limited to the contract price at the time of termination.⁴⁵ This price is composed of the price of the contract as awarded plus any equitable adjustments to which the contractor is entitled.

"Other Costs" are of three varieties: (1) *pure termination* "other costs" that do not add to the

contract price and are recoverable only up to the contract ceiling, including precontract costs, initial costs, and various costs continuing after termination (such as continuing facility costs), (2) *equitable adjustment* "other costs" that are not only recoverable but also add to the contract price against which a contractor may recover, including additional contract administration costs (in-house and outside professional fees) and research and development costs due to Government-directed changes, and (3) termination or equitable adjustment "other costs" that fall into *either category* (1) or (2), including facilities capital cost of money and delay costs.

These three categories are used in the following discussion of some of the "other costs" commonly incurred under terminated contracts. You should keep in mind that this list of "other costs" that you should consider claiming under a terminated contract is illustrative rather than exhaustive. Contractor personnel familiar with the terminated contract should attempt to identify additional "other costs" to be claimed. As noted earlier, the FAR entitles a terminated contractor to recover even normally unallowable costs if necessary for "fair compensation."⁴⁶

(1) *Pure Termination "Other Costs"*—

(a) Precontract Costs. One type of "pure termination" other costs to consider claiming is precontract costs. The allowability of precontract costs, in the absence of a termination for convenience, is governed by the FAR "Precontract costs" cost principle.⁴⁷ "Precontract costs" are defined as costs "incurred before the effective date of the contract directly pursuant to the negotiation and in anticipation of the contract award when such incurrence is necessary to comply with the proposed contract delivery schedule." These costs are allowable "to the extent that they would have been allowable if incurred after the date of the contract."⁴⁸ Interpreting the cost principle, the U.S. Claims Court developed a three-part test under which precontract costs are allowable if the costs (1) are incurred to meet the contract delivery schedule, (2) are incurred directly pursuant to the negotiation and in anticipation of the award, and (3) would have been allowable if incurred during contract performance.⁴⁹

This limitation on allowability may not apply after a contract is terminated for convenience, however. Because the normal FAR cost principles are "subject to" the general policy that the termination

settlement should compensate the contractor fairly,⁵⁰ precontract costs that would be unallowable if the contract had not been terminated may be recoverable.⁵¹ The ASBCA has stated that the earlier in performance a termination occurs the more likely it is that precontract costs will be allowed.⁵²

(b) Initial Costs. The FAR "Termination costs" cost principle allows a terminated contractor to recover its "initial costs," including "starting load costs" and "preparatory costs."⁵³ "*Starting load costs*" that are "not fully absorbed because of termination are non-recurring labor, material, and related overhead costs incurred in the early part of production." These costs result from factors such as excessive spoilage due to inexperienced labor, idle time and subnormal production due to testing and changing production methods, training, and lack of familiarity or experience with the product, materials, or manufacturing processes.⁵⁴ "*Preparatory costs*" incurred "in preparing to perform the terminated contract" include costs incurred for "initial plant rearrangement and alterations, management and personnel organization, and production planning."⁵⁵

(c) Continuing Facility Costs. "Costs continuing after termination," including continuing facility costs, are allowable under the FAR "Termination costs" cost principle if the costs cannot be discontinued despite all reasonable efforts.⁵⁶ There are two types of continuing facility costs—"idle capacity" and "idle facilities." These subcategories of continuing facility costs are defined by the FAR "Idle facilities and idle capacity costs" cost principle, a non-termination cost principle.⁵⁷ "Idle facilities" are "completely unused facilities that are excess to the contractor's current needs."⁵⁸ "Idle capacity" means "the unused capacity of partially used facilities." More specifically, it is "the difference between that which a facility could achieve under 100 percent operating time on a one-shift basis, less operating interruptions resulting from time lost for repairs, setups, unsatisfactory materials, and other normal delays, and the extent to which the facility was actually used to meet demands during the accounting period."⁵⁹

The amount claimed for continuing facility costs in the settlement proposal should include all allowable fixed costs from both the factory overhead and general and administrative expense overhead pools. The costs claimed should include depreciation,

maintenance, repair, housing, rent, insurance, property taxes, and other related costs.⁶⁰

The nontermination "Idle facilities and idle capacity costs" cost principle limits the recovery of idle facilities costs to "a reasonable period, ordinarily not to exceed 1 year."⁶¹ The ASBCA held in a nontermination case that the recovery period may exceed one year as long as the contractor makes a showing of diligent or reasonable efforts to limit the costs to the Government.⁶² The nontermination cost principle does not state for what period "idle capacity" may be recovered. The overriding "Termination costs" cost principle for costs continuing after termination does not contain the one-year limitation. It does state, however, that "any costs continuing after...termination due to the negligent or willful failure of the contractor to discontinue the costs shall be unallowable."⁶³ The bottom line is that the period of recovery would appear to be the same under both cost principles. For a discussion of how to avoid improper disallowances of idle capacity and idle facilities costs, see the 1995 BRIEFING PAPER.⁶⁴

(d) Severance Pay. Another type of the "costs continuing after termination" allowable under the FAR "Termination costs" cost principle is severance pay.⁶⁵ Under the "Compensation for personal services" cost principle, severance pay is allowable to the extent it is required either by (1) law, (2) a collective bargaining agreement, (3) established policy, or (4) circumstances of the particular employment.⁶⁶

(e) Standby Time. Also allowable as one of the "costs continuing after termination" is standby time. This is the time it takes to reassign employees working on the terminated contract to other work. The limitation on the amount recoverable is reasonableness. As noted previously, only costs continuing after termination that "despite all reasonable efforts by the contractor...cannot be discontinued immediately" are allowable under the FAR "Termination costs" cost principle.⁶⁷

(f) Rental Costs Under Unexpired Leases. Rental costs under unexpired leases are allowable under the "Termination costs" cost principle when the rental is shown to have been "reasonably necessary for the performance of the terminated contract."⁶⁸ After the termination, the contractor must make reasonable efforts to minimize the costs to the

Government.⁶⁹ Rental costs are allowable for the contract period and "*such further period as may be reasonable.*"⁷⁰ See the 1995 BRIEFING PAPER for a discussion of how to avoid improper disallowances of rental costs following a termination for convenience.⁷¹

(g) Unamortized Leasehold Improvements. The cost of unamortized alterations and reasonable restorations required by the lease are allowable under the FAR "Termination costs" cost principle when the alterations were necessary for performing the contract.⁷²

(2) *Equitable Adjustment "Other Costs"*—

(a) Additional Contract Administration—In-House Costs. As the result of stop work orders and various Government-directed changes, contractors often incur additional contract administration costs, such as costs incurred by contractor personnel for travel and related expenses. A contractor is entitled to an equitable adjustment for these costs.⁷³

(b) Additional Contract Administration—Outside Professional Fees. To respond to various Government-directed changes, contractors may be forced to retain outside counsel or other professionals. These costs should not be confused with legal and professional expenses incurred in conjunction with the termination for convenience settlement proposal. A contractor is entitled to an equitable adjustment in the contract price for professional fees and expenses incurred as a result of Government-directed changes.⁷⁴

The allowability of outside professional fees incurred during contract performance depends upon whether they were incurred for *contract administration* or to *prosecute a claim against the Government*. Outside professional fees incurred during performance for contract administration purposes are allowable.⁷⁵ Outside professional fees for prosecuting a claim against the Government are unallowable.⁷⁶

A factor in determining allowability is whether the request for equitable adjustment contains a CDA *claim certification* and *requests a final decision*. These are indicia of prosecuting a claim. There are conflicting considerations regarding seeking recovery of costs for outside professionals since, as is discussed later, a contractor is entitled to interest from the time of submission of a CDA claim.

Contractors sometimes claim outside professional fees incurred during performance as a termination settlement expense. This is a mistake since you may recover profit on performance costs but not on settlement expenses.⁷⁷

(c) *Research & Development Costs Resulting From Contract Changes.* As the result of various Government-directed changes, contractors may be forced to conduct R&D effort not otherwise required by the contract. A contractor is entitled to an equitable adjustment for such costs.⁷⁸

(3) *Either Category "Other Costs"—*

(a) *Facilities Capital Cost of Money.* A contractor may be entitled to recover facilities capital cost of money under the FAR "Cost of money" cost principle.⁷⁹ "Cost of money" is an imputed amount for the cost of capital for facilities devoted to contract performance. It is computed by multiplying the net book value of facilities committed to the contract by the interest rate set by the Secretary of the Treasury.⁸⁰ Cost of money may be either a pure termination "other cost" or an equitable adjustment "other cost." The proper characterization depends on that of the underlying costs on which cost of money is calculated.

You should claim cost of money in Item 8 if allowable to maximize your recovery following a convenience termination. Cost of money is allowable if either (1) the termination settlement proposal is the first cost proposal submitted under the contract, or (2) cost of money was requested on prior cost proposals.⁸¹

(b) *Delay Costs.* Another category of costs that may fall into either category of "other costs" is delay costs. Delay costs include unabsorbed overhead and the additional costs of performing in a later period, such as labor and material escalation costs. For the contractor to be entitled to an equitable adjustment for a delay period, the delay must be caused exclusively by the Government in its contractual capacity.⁸² As previously discussed, an equitable adjustment raises the contract price against which the contractor can recover its costs in the termination settlement. Costs for all other delay periods are pure termination "other costs" recoverable only up to the contract ceiling. These include delay periods for which the contractor is solely responsible; there is concurrent responsibility (contractor and Government in its contrac-

tual capacity); neither party is responsible, such as in the case of strikes, unusually severe weather, floods, fires, epidemics, and acts of God; or the Government is responsible in its sovereign capacity.⁸³ In applying these rules, it is necessary to distinguish between Government actions in its contractual capacity and Government actions in its sovereign capacity. Briefly stated, contractual acts are those directed specifically at the contractor, while sovereign acts are directed at the public generally.⁸⁴

If there is a sufficient contract price ceiling, a terminated contractor can recover for all days of delay irrespective of responsibility.⁸⁵ Under such circumstances, the number of days of delay is the difference between (1) the number of days in the original contract schedule to reach the stage of performance at the time of termination and (2) the number of days between the time of award and the termination for convenience. If there is not sufficient contract price for such a recovery, the contractor can still recover for delays for which it is entitled to an equitable adjustment (delays caused solely by the Government in its contractual capacity).

The next step is to calculate *unabsorbed overhead* for the days of delay. The U.S. Court of Appeals for the Federal Circuit has held that the *Eichleay* formula is the required method.⁸⁶ The following steps are used in the *Eichleay* formula to calculate the amount of recoverable overhead:

Step 1

$$\frac{\text{Contract billings}}{\text{Total billings for actual contract period}} \times \text{Total overhead for actual contract period} = \text{Overhead allocable to contract}$$

Step 2

$$\frac{\text{Overhead allocable to contract}}{\text{Actual days of contract performance}} = \text{Daily contract overhead}$$

Step 3

$$\text{Daily contract overhead} \times \text{Days of delay} = \text{Amount recoverable as unabsorbed overhead}$$

■ Items 9 Through 20

(a) *Item 9, "General and Administrative Expenses (from Schedule C)"*—The G&A expense rate should be applied to Items 1 to 8 and to Item 14, "Settlements With Subcontractors (from Schedule F)" on SF 1435. The G&A expense rate used for Government contracts must exclude unallowable costs.⁸⁷ The G&A expense rate used by a terminated contractor should be further reduced to reflect any costs normally charged as indirect costs that are charged as direct costs under the terminated contract.⁸⁸

A common mistake is not to apply the G&A expense rate to Item 14, "Settlements With Subcontractors," because it is below Item 9 for G&A expenses on SF 1435. However, the "Termination costs" cost principle provides that an "appropriate share of the contractor's indirect expense may be allocated to the amount of settlements with subcontractors."⁸⁹ G&A expenses on subcontractor settlements should therefore be included in Item 9 or Item 14 and explained as applicable at Schedule C or F of SF 1435. (For a discussion of the application of indirect costs to settlement expenses, see the explanation of Item 12, below.)

You should use final G&A expense rates if they are available. Where final rates are not available, you should use estimates. Identify the rates by fiscal year and indicate which are actual and which are estimates under Schedule C of SF 1435.

(b) *Item 10, "Total (Items 1 to 9 inclusive)"*—Item 10 is a computational block. List here the sum of the amounts claimed in Items 1 through 9.

(c) *Item 11, "Profit (explain in Schedule D)"*—A terminated contractor is entitled to a reasonable profit on its incurred costs other than settlement expenses.⁹⁰ The FAR directs the CO to consider the following factors in negotiating profit:⁹¹

- (1) Extent and difficulty of the work done by the contractor as compared with the total work required by the contract.
- (2) Engineering work, production scheduling, planning, technical study and supervision, and other necessary services.
- (3) Efficiency of the contractor.
- (4) Amount and source of capital and extent of risk assumed.

- (5) Inventive and developmental contributions and cooperation with the Government and other contractors in supplying technical assistance.
- (6) Character of the business, including the source and nature of materials and the complexity of manufacturing techniques.
- (7) Rate of profit that the contractor would have earned had the contract been completed.
- (8) Rate of profit both parties contemplated at the time the contract was negotiated.
- (9) Character and difficulty of subcontracting, including selection, placement, and management of subcontracts, and effort in negotiating settlements of terminated subcontracts.

The profit rate you propose should be based on these factors and explained in the "Description of Cost Elements."

Often the Government will contend that a contractor's profit is limited to the amount bid or negotiated for the contract when awarded. A termination for convenience sometimes results because what was intended as a production contract turns into an unanticipated research and development effort. Under such circumstances, the additional difficulty and risk would entitle the terminated contractor to a higher rate of profit than that bid or negotiated for the underlying contract.

A negative profit can be listed at Item 11 for any loss adjustment to which the Government is entitled. However, a contractor should not readily concede that the Government is entitled to a loss adjustment. As noted earlier in this PAPER, one of the techniques for avoiding a loss adjustment is to hold the Government to its burden of proof rather than admitting to a loss contract.⁹²

(d) *Item 12, "Settlement Expenses (from Schedule E)"*—A terminated contractor is entitled to recover as settlement expenses (1) accounting, legal, clerical, and similar costs reasonably necessary for preparation and negotiation of its termination settlement proposal and settlement of subcontractor termination settlement proposals and (2) reasonable costs

for storage, transportation, and disposition of termination inventory.⁹³

You should set up a separate account to accumulate settlement expenses for in-house personnel.⁹⁴ To avoid double counting, in-house personnel costs charged directly as settlement expenses should be removed from indirect cost pools.

The FAR provides that "indirect costs" for settlement expenses for in-house personnel "normally...shall be limited to payroll taxes, fringe benefits, occupancy costs, and immediate supervision costs."⁹⁵ Until recently, the DCAA's position was that this provision limited indirect charges for all personnel irrespective of whether the costs are normally charged directly or indirectly. By Memorandum dated November 22, 1996, the DCAA revised its *Contact Audit Manual* to conform with cases holding that the FAR limitation only applies to employee costs normally charged as indirect costs.⁹⁶ The DCAA no longer disputes that a contractor is entitled to follow its normal overhead practices for employee costs normally charged as direct costs.

(e) *Item 13, "Total (Items 10 to 13 inclusive)"*—Item 13 is a computational block. List here the sum of the amounts claimed in Items 10, 11, and 12.

(f) *Item 14, "Settlements With Subcontractors (from Schedule F)"*—Item 14 is for settlements with subcontractors. To protect the contractor, any settlements with subcontractors should, consistent with the FAR requirements, be made subject to CO approval.⁹⁷

As previously noted, a terminated contractor is entitled to recover G&A expenses on subcontractor settlements.⁹⁸ The G&A expenses claimed on subcontractor settlements should either be applied at Item 9 or included at Item 14 and explained as applicable at Schedule C or F.

(g) *Item 15, "Acceptable Finished Product"*—Acceptable finished product is listed at Item 15 at the contract price. As previously noted, "Acceptable Finished Product" means deliverables that are contract line items and not Item 4 "Finished Components," which are parts of contract line items.

(h) *Item 16, "Gross Proposed Settlement (Items 13 thru 15)"*—Item 16 is a computational block. List here the sum of the amounts claimed in Items 13 through 15.

(i) *Item 17, "Disposal and Other Credits (from Schedule G)"*—List here any disposal or other credits to which the Government is entitled. Provide details in Schedule G. Such credits should include, but are not limited to, amounts received by selling scrap and returning materials to vendors and materials used for or allocated to other contracts.⁹⁹

(j) *Item 18, "Net Proposed Settlement (Item 16 less 17)"*—Item 18 is a computational block. List here the amount remaining after the disposal and other credits set forth at Item 17 are subtracted from the gross proposed settlement at Item 16.

(k) *Item 19, "Advance, Progress & Partial Payments (from Schedule H)"*—List at Item 19 the sum of all advance, progress, and partial payments received under the contract. Advance, progress, and partial payments at Item 19 are all *unliquidated* payments made to the contractor before, during, and after performance.¹⁰⁰ This amount does *not* include payments for completed items invoiced at contract price. Provide details in Schedule H.

(l) *Item 20, "Net Payment Requested (Item 18 less 19)"*—Item 20 is a computational block. List here the amount remaining after the total for advance, progress, and partial payments at Item 19 is subtracted from the net proposed settlement at Item 18.

Total Cost Basis (SF 1436)

SF 1436, "Settlement Proposal (Total Cost Basis)," follows a similar format to SF 1435 and requests much of the same information. Both the background information on the contract and the computation of the contract price in Section I, "Status of Contract or Order at Effective Date of Termination," are the same as must be provided on SF 1435.

Section II of SF 1436, Items 1 through 19, likewise provides a format for summarizing and computing claimed costs. Schedules A to H on pages 2 to 4 of the form provide space for a more detailed explanation of claimed costs, credits, and payments received to date. As previously discussed, in addition to the explanation provided at Schedules A through H, your termination proposal should include a separate "Description of Cost Elements" setting forth the legal and factual bases for claimed costs.

Instructions for completing each Item (1 to 19) in Section II of SF 1436, with references where appropriate to the prior discussion in this PAPER of the corresponding line items in SF 1435, are provided in the paragraphs that follow.

(a) *Item 1, "Direct Material"*—Item 1 sets forth the amount claimed for direct material costs other than those included in Item 5, "Other Costs." "Direct material" is material that becomes part of the finished product or is otherwise consumed during production. Direct material costs include any transportation charges.

(b) *Item 2, "Direct Labor"*—Item 2 sets forth the amount claimed for direct labor costs other than those included in Item 5, "Other costs." Direct labor costs represent the wages and fringe benefits of personnel engaged in manufacturing.

(c) *Item 3, "Indirect Factory Expense (from Schedule A)"*—Item 3 sets forth the amount claimed for indirect factory expenses other than that included in Item 5, "Other Costs." Indirect factory expenses are all allocable manufacturing costs other than direct material and direct labor costs. The rates utilized should be adjusted to exclude any costs normally charged indirectly that are charged directly to the terminated contract.

(d) *Item 4, "Special Tooling and Special Test Equipment"*—Item 4 is for the *loss of useful value* of special tooling and special test equipment used to manufacture contract end items. See the prior discussion of SF 1435, Section II, Item 7.

(e) *Item 5, "Other Costs (from Schedule B)"*—The "other costs" that may be claimed in a total cost basis settlement proposal will be the same as under an inventory basis proposal. See the previous discussion of SF 1435, Section II, Item 8.

(f) *Item 6, "General and Administrative Expenses (from Schedule C)"*—The G&A expense rate is applied to Items 1 to 5 and Item 14, "Settlements With Subcontractors." See the earlier discussion of SF 1435, Section II, Item 9.

(g) *Item 7, "Total Costs (Items 1 thru 6)"*—Item 7 is a computational block. List here the sum of the amounts claimed in Items 1 through 6.

(h) *Item 8, "Profit (Explain in Schedule D)"*—As explained previously, a terminated contractor is

entitled to a reasonable profit on its incurred costs and post-termination costs other than settlement expenses.¹⁰¹ See the prior discussion of SF 1435, Section II, Item 11.

(i) *Item 9, "Total (Items 7 and 8)"*—Item 9 is a computational block. List here the sum of the amounts claimed in Items 7 and 8.

(j) *Item 10, "Deduct Finished Product Invoiced or To Be Invoiced"*—Item 10 is for finished product invoiced or "to be invoiced." Finished product is charged at the contract price.

(k) *Item 11, "Total (Item 9 less Item 10)"*—Item 11 is a computational block. List here the difference between the total for finished product at Item 10 and the subtotal at Item 9 (which is the total of Items 1 through 6 and 8).

(l) *Item 12, "Settlement Expenses (from Schedule E)"*—Item 12 is for the total of settlement expenses detailed on Schedule E of SF 1436. See the earlier discussion of SF 1435, Section II, Item 12.

(m) *Item 13, "Total (Items 11 and 12)"*—Item 11 is a computational block. List here the sum of the amounts claimed in Items 11 and 12.

(n) *Item 14, "Settlements With Subcontractors (from Schedule F)"*—Item 14 is for the total costs of settlements with subcontractors. List here the sum of the amounts detailed on SF 1436, Schedule F. See the prior discussion of SF 1435, Section II, Item 14.

(o) *Item 15, "Gross Proposed Settlement (Items 13 thru 14)"*—Item 15 is a computational block. List here the sum of the amounts claimed in Items 13 and 14.

(p) *Item 16, "Disposal and Other Credits (from Schedule G)"*—List here any disposal or other credits the Government is entitled to as detailed on SF 1436, Schedule G. See the previous discussion of SF 1435, Section II, Item 17.

(q) *Item 17, "Net Proposed Settlement (Item 15 less 16)"*—Item 17 is a computational block. List here the remainder after the total for disposal and other credits set forth at Item 16 is subtracted from the gross proposed settlement at Item 15.

(r) *Item 18, "Advance, Progress & Partial Payments (from Schedule H)"*—List at Item 18 the sum of all

unliquidated advance, progress, and partial payments received under the contract as detailed in SF 1436, Schedule H. See the earlier discussion of SF 1435, Section II, Item 19.

(s) *Item 19, "Net Payment Requested (Item 18 less 19)"*—Item 19 is a computational block. List here the remainder after the total for advance, progress, and partial payments at Item 18 is subtracted from the net proposed settlement at Item 17.

Inventory Schedules

To support a termination settlement proposal, contractors submit inventory schedules that provide information on various types of property acquired for the performance of the contract. Effective September 24, 1996, the FAR was amended to require contractors to submit inventory schedules *within 120 days* of the effective date of contract termination unless granted a time extension in writing by the CO.¹⁰² Previously, the FAR had imposed no deadline on the submission of inventory schedules following a termination for convenience. Inventory schedules should in any event be submitted as soon as possible to expedite plant clearance (the screening, redistribution, and disposal of contractor inventory from a contractor's plant or work site).¹⁰³ A CO will often not act on a request for partial payment until plant clearance is completed.

As noted earlier in this PAPER, the following inventory forms and their respective continuation sheets are required for *inventory* or *total cost* basis termination settlement proposals as applicable: SF 1426, "Inventory Schedule A (Metals in Mill Product Form)" (and SF 1427, "Continuation Sheet"); SF 1428, "Inventory Schedule B" (and SF 1429, "Continuation Sheet"); SF 1430, "Inventory Schedule C (Work-in-Process)" (and SF 1431, "Continuation Sheet"); and SF 1432, "Inventory Schedule D (Special Tooling and Special Test Equipment)" (and SF 1433, "Continuation Sheet").¹⁰⁴

These forms, which are largely self-explanatory, require a contractor to indicate the physical *condition* of each inventory item. For this purpose, the FAR provides the following condition codes:¹⁰⁵

Code 1, Unused-good. Unused property that is usable without repairs and identical or

interchangeable with new items from normal supply sources.

Code 2, Unused-fair. Unused property that is usable without repairs, but is deteriorated or damaged to the extent that utility is somewhat impaired.

Code 3, Unused-poor. Unused property that is usable without repairs, but is considerably deteriorated or damaged. Enough utility remains to classify the property better than salvage.

Code 4, Used-good. Used property that is usable without repairs and most of its useful life remains.

Code 5, Used-fair. Used property that is usable without repairs, but is somewhat worn or deteriorated and may soon require repairs.

Code 6, Used-poor. Used property that may be used without repairs, but is considerably worn or deteriorated to the degree that remaining utility is limited or major repairs will soon be required.

Code 7, Repairs required-good. Required repairs are minor and should not exceed 15 percent of original acquisition cost.

Code 8, Repairs required-fair. Required repairs are considerable and are estimated to range from 16 percent to 40 percent of original acquisition cost.

Code 9, Repairs required-poor. Required repairs are major because property is badly damaged, worn, or deteriorated, and are estimated to range from 41 percent to 65 percent of original acquisition cost.

Code X, Salvage. Property has some value in excess of its basic material content, but repair or rehabilitation to use for the originally intended purpose is clearly impractical. Repair for any use would exceed 65 percent of the original acquisition cost.

Code S, Scrap. Material that has no value except for its basic material content.

The forms also require the contractor to provide the price or costs of the inventory. Anytime the actual costs or invoiced price of an inventory item is not available, you should use an estimate and identify estimated costs with the symbol "(e)."¹⁰⁶ In theory, the use of estimates other than for bulk raw materials and metals and work-in-process will largely be limited to inventory schedules furnished for settlement proposals submitted on a total cost basis.

After inventory *category*, *subdivision*, *condition*, and *cost or price* determinations have been made, you should list the inventory on SF 1426, SF 1428, SF 1430, or SF 1432 as discussed below.¹⁰⁷

■ Schedule A (Metals In Mill Product Form) (SF 1426)

SF 1426, "Inventory Schedule A (Metals in Mill Product Form)," is used to list metals in raw or primary form as furnished by the mill. It is also used for nonmetallic materials such as plastics, rubber, and lumber in mill form.¹⁰⁸

For both inventory basis (SF 1435) and total cost basis (SF 1436) settlement proposals, inventory is listed on SF 1426 at cost, which includes any freight charges. Where the inventory basis (SF 1435) is used, the inventory listed on SF 1426 is included in Item 1, "Metals." As previously noted, the amounts on SF 1435 and SF 1426 often differ due to losses during production. If the total cost basis (SF 1436) is used, the inventory listed on SF 1426 is lumped with other types of material under Item 1, "Direct Material."

■ Schedule B (SF 1428)

SF 1428, "Inventory Schedule B," is a catchall schedule. It must be used for all inventory that does not belong on SF 1426, SF 1430, or SF 1432.¹⁰⁹ Inventory required to be listed on SF 1428 includes raw materials (other than metals), purchased parts, and finished components.

For both inventory basis (SF 1435) and total cost basis (SF 1436) settlement proposals, raw materials and purchased parts are listed at cost, which includes any freight charges. Under the inventory basis (SF 1435), the amount claimed for finished components is the sum of direct material costs, direct labor costs, and indirect factory expenses. The computation is made in Schedule A of SF 1435, "Analysis of Inventory Cost (Items 4 and 6)." On SF 1435, the amounts for raw materials are included under Item 2, "Raw Materials (other than metals)"; purchased parts under Item 3, "Purchased Parts"; and finished components under Item 4, "Finished Components." The amounts listed under Items 2, 3, and 4 on SF 1435 often differ from the amounts on the inventory schedule due to losses during production. If the total cost basis (SF 1436) is used, only direct material costs (including freight costs) are listed on SF 1428, "Inventory Schedule B." These costs are lumped with other material costs on SF 1436 under Item 1, "Direct Material."

■ Schedule C (Work-In-Process) (SF 1430)

"Work-in-process" is material "released to manufacturing, engineering, design or other services under the contract and includes undelivered manufactured parts, assemblies, and products, either complete or incomplete."¹¹⁰ Under the inventory basis (SF 1435), the amount on SF 1430, "Inventory Schedule C (Work-in-Process)," for work-in-process is composed of direct material costs, direct labor costs, and indirect factory expenses. You must provide a cost breakdown of these three factors in Schedule A, "Analysis of Inventory Cost (Items 4 and 6)." As previously discussed, "Work-in-Process" on Inventory Schedule C is the same as "Work-in-Progress" on SF 1435, Item 6. Under the total cost basis (SF 1436), the amount listed is limited to direct material costs, which include any freight charges.

■ Schedule D (Special Tooling & Special Test Equipment) (SF 1432)

SF 1432, "Inventory Schedule D (Special Tooling and Special Test Equipment)," is used for listing special tooling and special test equipment such as dies, jigs, and gauges.¹¹¹ If the inventory basis (SF 1435) is used for the settlement proposal, special tooling and special test equipment are priced at purchase price plus any direct material costs, direct labor costs, or indirect factory expenses. If the total cost basis (SF 1436) is used, pricing may be limited to acquisition or direct material costs. However, contractors using the total cost basis often elect to price special tooling and special test equipment in the same manner they would under the inventory basis.

If the inventory basis (SF 1435) is used, the amount claimed appears at Item 7, "Special Tooling and Special Test Equipment." If the total cost basis (SF 1436) is used, the amount claimed appears at Item 4, "Special Tooling and Special Test Equipment."

Schedule Of Accounting Information (SF 1439)

SF 1439, "Schedule of Accounting Information," provides the Government background information concerning the terminated contractor's account-

ing system and any deviations from the accounting system made in preparing the termination settlement proposal. To be fairly compensated and to maximize recovery, a contractor will often deviate from its regular accounting practices in submitting a termination settlement proposal. An example is charging costs normally charged as indirect costs directly to the terminated contract.¹¹²

The FAR requires all prime contractors to submit SF 1439, "Schedule of Accounting Information" in support of a termination settlement proposal,¹¹³ and both SF 1435 and SF 1436 ask for an explanation if SF 1439 is not provided. Prime contractors sometimes indicate they are not providing SF 1439 because they have a current CAS Disclosure Statement. Although such an explanation may be accepted, it is not a good idea to fail to provide SF 1439 if you are deviating from your normal accounting practices in your settlement proposal.

Subcontractors should consider submitting SF 1439 even though they are not required to do so. Furnishing SF 1439 will likely expedite the processing of partial payment applications.

Application For Partial Payment (SF 1440)

SF 1440, "Application for Partial Payment," is not a required form for submission of a fully compliant termination settlement proposal. However, to alleviate the cash-flow problems resulting from a termination, you may want to include an "Application for Partial Payment" with your settlement proposal.

Partial payments are available before settlement.¹¹⁴ Contractors may receive a partial payment that includes, in the aggregate, the following amounts:¹¹⁵

- (a) 100% of the contract price adjusted for items completed before the termination date or to be completed after the termination date with the CO's approval.
- (b) 100% of subcontractor settlements the contractor has paid that were approved by the CO.
- (c) 90% of the direct costs of termination inventory including raw materials, purchased parts, supplies, and direct labor.
- (d) 90% of other allowable costs not included above that are allocable to the terminated requirements including settlement expenses.
- (e) 100% of partial payments made to subcontractors.

The SF 1440, "Application for Partial Payment," asks for essentially the same information as provided on SF 1435, "Settlement Proposal (Inventory Basis)."

A partial payment request may be submitted with or after submission of the termination settlement proposal or interim settlement proposal.¹¹⁶ Where complex termination settlement proposals are involved, the Government often makes more than one partial payment before a final settlement is reached or the parties resort to litigation. To facilitate prompt processing, an interim settlement proposal and accompanying "Application for Partial Payment" should generally be limited to costs that the Government is unlikely to dispute.

You should consider requesting permission to submit an interim settlement proposal on a total cost basis. If the CO is amenable, this technique can be used to facilitate prompt submission and a partial payment. A CO may approve use of the total cost approach for an interim settlement proposal even where the final settlement proposal is to be submitted on an inventory basis.¹¹⁷ Before requesting permission to submit an interim settlement proposal on a total cost basis, you should discuss the matter with the CO. Otherwise, you may lose considerable time waiting for a reply.

The FAR requires that the Government "promptly" process the partial payment application.¹¹⁸ However, sometimes a CO will ignore this requirement or refuse to make a partial payment to force a complete settlement. You may be able to get a recalcitrant CO to make a prompt partial payment by pointing out that (1) payment is the Government's primary contractual obligation, and (2) failure to make payment may be a breach of contract entitling you to anticipatory profits and other special damages¹¹⁹ that are not available under the "Termination for Convenience of the Government" clause.¹²⁰

Requests For Equitable Adjustments

As previously discussed, contractor recovery following a termination for convenience is limited to the contract price.¹²¹ The contract price is the sum of the contract as awarded, plus any equitable adjustments to which the contractor is entitled. Thus, if a contractor claims amounts in excess of the original contract price, it must prove entitlement to a commensurate equitable adjustment to recover the excess. In other words, to recover amounts up to the original contract price, you need only show incurrence. To recover amounts in excess of the original contract price, you need to demonstrate a cause-and-effect relationship between some Government action or inaction and the additional costs.

You should therefore include a request for an equitable adjustment with your settlement proposal to claim amounts that exceed the original contract price. Such costs, except for G&A expenses and profit, should also be included in the termination settlement proposal under "Other Costs" (Item 8 on SF 1435 or Item 5 on SF 1436). It is not necessary to include G&A expenses and profit under the category "Other Costs" since they are added elsewhere on SF 1435 and SF 1436.

However, equitable adjustment claims are independent of termination settlement proposals.¹²² A terminated contractor may therefore first submit equitable adjustment claims for Government changes to start the accrual of CDA interest¹²³ and submit its termination settlement proposal later but within the one-year deadline. Since requests for equitable adjustments may be submitted separately, the failure to submit a termination settlement proposal in a timely manner does not necessarily foreclose the right to recovery for contract changes under requests for equitable adjustments.¹²⁴

Recovery Of CDA Interest

■ Requirements For A "Claim"

A contractor is entitled to interest from the date of submission of a CDA "claim."¹²⁵ For a submission by a contractor to the CO to qualify as a CDA "claim," it must (1) be in writing, (2) request payment of a sum certain, (3) be other than an invoice

or other routine request for payment,¹²⁶ (4) be certified if for over \$100,000,¹²⁷ and (5) request a final decision.¹²⁸

A termination settlement proposal prepared on an SF 1435 or 1436 readily meets requirements (1) through (3). A properly prepared SF 1435 or SF 1436 is in *writing* and requests payment of a *sum certain*. Furthermore, in a recent decision, the Federal Circuit held that a termination settlement proposal is *not* a routine request for payment.¹²⁹

To satisfy requirement (4), a CDA *certification* is required if you claim over \$100,000 in your settlement proposal.¹³⁰ It must state as follows:¹³¹

I certify that the claim is made in good faith; that the supporting data are accurate and complete to the best of my knowledge and belief; that the amount requested accurately reflects the contract adjustment for which the contractor believes the Government is liable; and that I am duly authorized to certify the claim on behalf of the contractor.

If the certification is defective and the CO so notifies the contractor within 60 days after claim submission, the CO need not issue a final decision.¹³² Otherwise the CO must, within 60 days of claim submission, issue a final decision or advise the contractor when a final decision will be issued.¹³³

The preprinted "Certificate" appearing before the signature block on both SF 1435 and SF 1436 does not meet CDA certification requirements. Therefore, a CO could refuse to issue a final decision within the 60-day window. If the CO ignores such a "defective certification" and issues a final decision, the defect is correctable anytime up to the entry of final judgment in the litigation of the claim.¹³⁴

Whether a termination settlement proposal that *requests a final decision* at the time the proposal is submitted meets the requirements for a CDA "claim" is unclear. In 1996, the Federal Circuit held that a termination settlement proposal that did not expressly request a final decision was not a CDA claim when submitted but ripened into a claim after negotiations between the parties reached an impasse. Although the court recognized that a request for a final decision need not be express, it reasoned that a termination settlement proposal is initially submitted for negotiation rather

than a final decision.¹³⁵ Since this Federal Circuit decision, there has been disagreement over whether a termination settlement proposal that expressly requests a final decision at the outset could qualify as a CDA claim when submitted. The ASBCA has held that, even absent an impasse in negotiations, a settlement proposal was transformed into a claim when a contractor requested a final decision.¹³⁶ However, the Department of Transportation Board has held that a settlement proposal is not a claim when submitted because it is contractually required to be submitted.¹³⁷ Commentators are also in disagreement.¹³⁸

■ Interest vs. Settlement Expenses

If a termination proposal is initially submitted as a CDA claim, the Government may attempt to disallow termination settlement expenses under the FAR "Costs related to legal and other proceedings" cost principle, which provides that the costs of pursuing a "claim" against the Government are unallowable.¹³⁹ This argument has been successful in nontermination cases.¹⁴⁰ However, where there is a termination for convenience, it would appear that such costs are still recoverable as settlement ex-

penses. Under the FAR "Termination costs" costs principle, a contractor may recover as settlement expenses professional fees and other costs for the "preparation and presentation...of settlement claims to the contracting officer."¹⁴¹ Professors Ralph Nash and John Cibinic concur based on a different rationale.¹⁴²

Assuming that our interpretation is proper and a termination settlement proposal can be initially submitted as a claim, the contractor should be entitled to receive both interest and the costs of preparing the settlement proposal. Just as the costs of preparing [a request for an equitable adjustment] for a directed change are properly costs of contract administration, the costs of preparing a termination settlement proposal are properly costs related to the termination. Both submissions are specifically required by the terms of the "Changes" and "Termination" clauses.

In sum, although there is some debate, it appears, at least to the authors, that (1) a contractor can initially submit a termination settlement proposal as a CDA claim and begin the accrual of interest, and (2) submitting a settlement proposal in this manner should not prejudice a contractor's right to recover settlement expenses.

GUIDELINES

These *Guidelines* are designed to assist you in preparing a termination settlement proposal after a contract has been terminated for the Government's convenience. They are not, however, a substitute for professional representation in any particular situation.

1. Submit a *timely* termination settlement proposal. Absent timely submission, the CO's or higher-tier contractor's payment determination is *not* subject to judicial review.

2. Follow basic *strategies for maximizing recovery*, including (a) claiming otherwise unallowable costs under the "fair compensation" principle, (b) not allowing the Government to improperly disallow costs by imposing its after-the-fact business judgment, (c) not accepting disallowances based on impractical proof requirements, (d) claiming all allowable costs, (e) charging normally indirect costs directly, (f) avoiding loss adjustments, (g) requesting a partial payment, and (h) obtaining professional help.

3. Become familiar with the *forms* for submitting a termination settlement proposal. These forms include (a) the termination settlement proposal, SF 1435 (Inventory Basis) or SF 1436 (Total Cost Basis), (b) the various inventory schedules and continuation sheets, SF 1426 to SF 1433, (c) SF 1439, "Schedule of Accounting Information," and (d) SF 1440, "Application for Partial Payment."

4. Supplement your termination settlement proposal forms with a "*Description of Cost Elements*." This is particularly important when you are using the FAR guarantee of "fair compensation" to claim an *otherwise unallowable cost*.

5. Be aware of the differences between the *preferred inventory basis* (SF 1435) and *total cost basis* (SF 1436) for preparing settlement proposals. Although both approaches theoretically lead to the same amount claimed, contractor recovery may be *less* under the *total cost method* where a *loss contract* is alleged.

6. Obtain *CO permission* if you plan to use the *total cost basis* (SF 1436) for your settlement proposal. Be sure to make a timely request, keeping in mind the deadline for submitting the termination settlement proposal.

7. Submit *requests for equitable adjustments* to which you are entitled. This will enable you to recover amounts *in excess of the original contract price* and avoid loss adjustments.

8. Adjust indirect cost rates to reflect costs normally charged indirectly that are *charged directly* to the terminated contract.

9. Completely fill out the applicable *inventory schedules*. Be sure to use the pertinent *condition codes*.

10. If you are using the *total cost basis* (SF 1436), do *not* allocate direct material costs, di-

rect labor costs, and indirect factory expenses to inventory.

11. When using the *inventory basis* (SF 1435), use the "Description of Cost Elements" to explain any *differences* between the amount claimed for inventory on SF 1435 and inventory listed on the various schedules.

12. To *expedite settlement*, always submit SF 1439, "Schedule of Accounting Information." To *facilitate cash flow*, submit an interim proposal and SF 1440, "Application for Partial Payment"

13. Consider submitting the settlement proposal as a *CDA claim* to recover *interest*. Be aware that the Government may argue that *settlement expenses* are an unallowable cost of prosecuting a claim against the Government.

★ REFERENCES ★

- | | |
|---|---|
| <p>1/ See generally Pushkar, Janik & Rhodes, "Dealing With the Effects of Downsizing," Briefing Papers No. 93-5 (Apr. 1993).</p> <p>2/ See, e.g., FAR 52.249-2 ("Termination for Convenience of the Government (Fixed-Price)" clause).</p> <p>3/ See FAR 52.249-2, paras. (f), (g), (i). See also FAR 49.113, 49.201, 49.202.</p> <p>4/ Seidman & Banfield, "Maximizing Termination for Convenience Settlements," Briefing Papers No. 95-5 (Apr. 1995).</p> <p>5/ FAR 49.206-1(a), 52.249-2, para. (e).</p> <p>6/ FAR 49.001.</p> <p>7/ FAR 52.249-2, para. (e).</p> <p>8/ FAR 52.249-2, paras. (e), (j); Do-Well Machine Shop, Inc. v. U.S., 870 F.2d 637 (Fed. Cir. 1989), 8 FPD ¶ 33, 31 GC ¶ 116.</p> <p>9/ See FAR 49.104(d), 49.208, 52.249-2, para. (l).</p> <p>10/ FAR 52.249-2, para. (l).</p> | <p>11/ This BRIEFING PAPER does not discuss the preparation of SF 1438, "Settlement Proposal (Short Form)," the use of which is limited to settlement proposals for fixed-price contracts less than \$10,000. See FAR 49.602-1(d).</p> <p>12/ FAR 49.602-1. See FAR 53.301-1435, -1436 (form illustrations).</p> <p>13/ FAR 49.602-2. See FAR 53.301-1426 to -1433 (form illustrations).</p> <p>14/ FAR 49.206-1(e), 49.602-3. See FAR 53.301-1439 (form illustration).</p> <p>15/ FAR 49.113, 49.201. See note 4, <i>supra</i>, at 3.</p> <p>16/ FAR 49.201(a).</p> <p>17/ 48 CFR § 9904.405. See generally Smith, Williams & Snyder, "Accounting for Unallowable Costs Under CAS 405," 97-6 Govt. Cont. Costs, Pricing & Acctg. Rep. 3 (June 1997); Boyd & Villet, "Cost Accounting Standards Fundamentals," Briefing Papers No. 96-12 (Nov. 1996).</p> <p>18/ 18 USC § 1001 (criminal False Claims Act); 31 USC §§ 3729-3733 (civil False Claims Act).</p> |
|---|---|

- 19/ FAR 49.602-4. See FAR 53.301-1440 (form illustration).
- 20/ See FAR 49.112-1, 52.249-2, para. (m).
- 21/ FAR 49.206-2.
- 22/ See FAR 31.205-42(c).
- 23/ FAR 49.206-2(b).
- 24/ FAR 49.206-2(a)(1).
- 25/ FAR 49.206-2(b)(4).
- 26/ FAR 49.206-2(b)(1).
- 27/ FAR 49.206-2(b)(1).
- 28/ See American Packers, Inc., ASBCA 14275, 71-1 BCA ¶ 8846; Douglas Corp., ASBCA 5550, 60-1 BCA ¶ 2531, 2 GC ¶ 217.
- 29/ FAR 49.203.
- 30/ Compare FAR 49.203(b) with (c).
- 31/ DCAA, DCAM ¶ 12-308 (July 1997).
- 32/ Maitland Bros., ASBCA 43088, 93-3 BCA ¶ 26007, affd. on reconsideration, 94-1 BCA ¶ 26285. See note 4, supra, at 5.
- 33/ See note 8, supra.
- 34/ Caskel Forge, Inc., ASBCA 7638, 1962 BCA ¶ 3318, 4 GC ¶ 258. See also Cubic Defense Sys., ASBCA 39859, 91-2 BCA ¶ 23748.
- 35/ See FAR 49.112-1, 52.249-2, para. (m).
- 36/ FAR 49.602-3. See FAR 49.602-1(d).
- 37/ FAR 49.207, 52.249-2, paras. (f), (g). See Seven Science Indus., ASBCA 23337, 80-2 BCA ¶ 14518.
- 38/ See, e.g., Durette, GmbH, ASBCA 34072, 91-2 BCA ¶ 23756.
- 39/ See FAR 45.606-5(e)(2)(i).
- 40/ See FAR 45.606-5(e)(2)(i).
- 41/ See FAR 45.606-5(e)(2)(i).
- 42/ FAR 31.205-42.
- 43/ FAR 31.205-42(d).
- 44/ FAR 45.101.
- 45/ FAR 49.207, 52.249-2, paras. (f), (g).
- 46/ FAR 49.201. See note 4, supra, at 3.
- 47/ FAR 31.205-32.
- 48/ FAR 31.205-32. See FAR 31.109.
- 49/ Penberthy Electromelt Intl. v. U.S., 11 Cl. Ct. 307 (1986), 5 FPD ¶ 120, 29 GC ¶ 40.
- 50/ FAR 49.113, 49.201. See Codex Corp. v. U.S., 226 Ct. Cl. 693 (1981), 23 GC ¶ 239.
- 51/ Codex Corp. v. U.S., note 50, supra; Kasler Elec. Co., DOTCAB 1425, 84-2 BCA ¶ 17374, 26 GC ¶ 326.
- 52/ Metered Laundry Servs., Inc., ASBCA 21573, 78-2 BCA ¶ 13451. See note 4, supra, at 6-7.
- 53/ FAR 31.205-42(c).
- 54/ FAR 31.205-42(c)(1).
- 55/ FAR 31.205-42(c)(2).
- 56/ FAR 31.205-42(b).
- 57/ FAR 31.205-17.
- 58/ FAR 31.205-17(a).
- 59/ FAR 31.205-17(a).
- 60/ FAR 31.205-17(a).
- 61/ FAR 31.205-17(b).
- 62/ General Dynamics Corp., ASBCA 19607, 78-1 BCA ¶ 13203.



63/ FAR 31.205-42(b).

64/ Note 4, *supra*, at 7-8.

65/ See FAR 31.205-42(b).

66/ FAR 31.205-6(g)(2)(i).

67/ FAR 31.205-42(b).

68/ FAR 31.205-42(e).

69/ FAR 31.205-42(e)(2).

70/ FAR 31.205-42(e)(1) (emphasis added).

71/ Note 4, *supra*, at 8.

72/ FAR 31.205-42(f).

73/ FAR 52.242-15 ("Stop-Work Order" clause), 52.243-1 ("Changes—Fixed-Price" clause).

74/ FAR 52.243-1.

75/ FAR 31.205-33.

76/ FAR 31.205-47(f)(1).

77/ FAR 49.202, 52.249-2, paras. (f), (g)(2)(iii).

78/ FAR 52.243-1. See *Bill Strong Enters., Inc. v. Shannon*, 49 F.3d 1541 (Fed. Cir. 1995), 14 FPD ¶ 18, 37 GC ¶ 141, overruled in part on other grounds by *Reflectone, Inc. v. Dalton*, 60 F.3d 1572 (Fed. Cir. 1995), 14 FPD ¶ 63, 37 GC ¶ 411.

79/ FAR 31.205-10.

80/ FAR 31.205-10(a)(1).

81/ See *Spectrum Leasing Corp. v. General Servs. Admin.*, GSBGA 12189, 95-1 BCA ¶ 27317; *AT&T v. General Servs. Admin.*, GSBGA 11730, 95-2 BCA ¶ 27869, 37 GC ¶ 531. See also FAR 31.205-10(a)(2); note 4, *supra*, at 8.

82/ See *Wilner Const. Co.*, ASBCA 26621, 84-2 BCA ¶ 17411, *affd.* on reconsideration, 84-3 BCA ¶ 17669.

83/ *Worsham Const. Co.*, ASBCA 25907, 85-2 BCA ¶ 18016, 28 GC ¶ 243 (Note).

84/ See *U.S. v. Winstar Corp.*, 116 S. Ct. 2432 (1996), 15 FPD ¶ 68, 38 GC ¶ 322. See generally Latham, "Government Interference and Sovereign Acts," *Briefing Papers* No. 76-3 (June 1976), 4 BPC 31.

85/ Note 83, *supra*.

86/ *Wickham Contracting Co. v. Fischer*, 12 F.3d 1574 (Fed. Cir. 1994), 13 FPD ¶ 1, 36 GC ¶ 201. See *Eichleay Corp.*, ASBCA 5183, 60-2 BCA ¶ 2688, 2 GC ¶ 485, *affd.* on reconsideration, 61-1 BCA ¶ 2894, 3 GC ¶ 138(a). See generally *Bastianelli & Lange*, "Recovering Delay Damages for Home Office Overhead," *Construction Briefings* No. 97-3 (Feb. 1997).

87/ FAR 31.201-6.

88/ See note 4, *supra*, at 4.

89/ FAR 31.205-42(h).

90/ FAR 49.202(a), 52.249-2, paras. (f), (g)(2)(iii).

91/ FAR 49.202(b).

92/ See note 4, *supra*, at 5.

93/ FAR 31.205-42(g)(1).

94/ See FAR 31.205-42(g)(2).

95/ FAR 31.205-42(g)(1)(iii) (emphasis added).

96/ DCAA, DCAM ¶ 12-309 (July 1997). See *Celesco Indus.*, ASBCA 22460, 84-2 BCA ¶ 17295, 26 GC ¶ 326; *Condec Corp.*, ASBCA 14234, 73-1 BCA ¶ 9808, 15 GC ¶ 295.

97/ FAR 49.108-3, 52.249-2, para. (b)(5).

98/ FAR 31.205-42(h).

99/ See FAR 31.205-42(a), 49.204, 49.206-2(a)(2), 49.207, 52.249-2, paras. (b)(9), (k)(3).

100/ FAR 49.206-2(a)(2), 52.249-2, para. (k)(1).



- 101/ FAR 49.202(a), 52.249-2, paras. (f), (g)(2)(iii).
- 102/ FAR 49.206-3, 52.249-2, para. (c) (added by 61 Fed. Reg. 39186 (July 26, 1996)).
- 103/ See FAR 45.601 (defining "plant clearance").
- 104/ FAR 49.602-2.
- 105/ FAR 45.606-5(d)(4).
- 106/ See FAR 45.606-5(d)(5).
- 107/ See also FAR 45.606-5(e).
- 108/ FAR 45.606-5(a)(1).
- 109/ FAR 45.606-5(a)(2).
- 110/ See FAR 45.501, 45.601.
- 111/ See FAR 45.101.
- 112/ See note 4, *supra*, at 4.
- 113/ FAR 49.206-1(e), 49.602-3.
- 114/ FAR 49.112-1(a), 52.249-2, para. (m)(1).
- 115/ FAR 49.112-1(b).
- 116/ FAR 49.112-1(a).
- 117/ See generally *Southeastern Servs., Inc.*, ASBCA 22816, 85-3 BCA ¶ 18183.
- 118/ FAR 49.112-1(a).
- 119/ See Nash, "Default for Failure To Proceed: The 'No Pay-No Way' Defense," 1 Nash & Cibinic Rep. ¶ 39 (May 1987).
- 120/ See FAR 52.249-2, paras. (f), (g).
- 121/ FAR 49.207, 52.249-2, paras. (f), (g).
- 122/ See *James M. Ellett Const. Co. v. U.S.*, 93 F.3d 1537 (Fed. Cir. 1996), 15 FPD ¶ 90, 38 GC ¶¶ 426, 477, 574.
- 123/ See 41 USC § 611.
- 124/ See *RBW & Assocs.*, AGBCA 96-205-R, 96-2 BCA ¶ 28616 (reversing its earlier decision on this issue based on note 122, *supra*), 38 GC ¶ 597.
- 125/ 41 USC § 611; FAR 33.208.
- 126/ See *Reflectone, Inc. v. Dalton*, note 78, *supra* (interpreting FAR 33.201 regarding requirements 1, 2, and 3).
- 127/ FAR 33.201. See 41 USC § 605(c)(1), FAR 33.207(a).
- 128/ See FAR 33.206; 41 USC § 605(a). See also note 122, *supra* (requiring at least an implicit request for final decision for a claim to exist).
- 129/ Note 122, *supra*.
- 130/ 41 USC § 605(c)(1); FAR 33.201, 33.207(a).
- 131/ FAR 33.207(c). See 41 USC § 605(c)(1).
- 132/ 41 USC § 605(c)(6); FAR 33.211(e).
- 133/ 41 USC § 605(c)(2); FAR 33.211(c).
- 134/ 41 USC § 605(c)(6); FAR 33.207(f).
- 135/ Note 122, *supra*.
- 136/ *Mid-America Engrg. & Mfg.*, ASBCA 48831, 96-2 BCA ¶ 28558, 38 GC ¶ 477. See West & Handwerker, "Feature Comment: The 'In Dispute' Requirement After *Ellett*: A Resuscitation of the *Dawco* Standards?," 38 GC ¶ 574.
- 137/ *RRP Const. Co.*, DOTBCA 2999 (Sept. 10, 1996), 38 GC ¶ 574.
- 138/ Compare, e.g., *Cibinic*, "The *Ellett* Case: What's All the Fuss About?," 11 Nash & Cibinic Rep. ¶ 8 (Feb. 1997) (termination settlement proposal can be a claim when submitted if it requests a final decision) with 38 GC ¶ 477 (parties must reach an "impasse" before termination settlement proposal can be a CDA "claim").
- 139/ FAR 31.205-47(f)(1).
- 140/ See note 78, *supra*.
- 141/ FAR 31.205-42(g)(1)(i)(A).
- 142/ *Cibinic*, note 138, *supra*, at 25.



SF 1435, SETTLEMENT PROPOSAL (INVENTORY BASIS)

SETTLEMENT PROPOSAL (INVENTORY BASIS)		FORM APPROVED OMB NO. 9000-0012
Public reporting burden for this collection of information is estimated to average 2.5 hours per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden, to the FAR Secretariat (VRS), Office of Federal Acquisition and Regulatory Policy, GSA, Washington, D.C. 20405; and to the Office of Management and Budget, Paperwork Reduction Project (9000-0012), Washington, D.C. 20503.		
FOR USE BY A FIXED-PRICE PRIME CONTRACTOR OR FIXED-PRICE SUBCONTRACTOR		
THIS PROPOSAL APPLIES TO (Check one) <input type="checkbox"/> A PRIME CONTRACT WITH THE GOVERNMENT <input type="checkbox"/> SUBCONTRACT OR PURCHASE ORDER		COMPANY
SUBCONTRACT OR PURCHASE ORDER NO.:		STREET ADDRESS
CONTRACTOR WHO SENT NOTICE OF TERMINATION		CITY AND STATE (include ZIP Code)
NAME		NAME OF GOVERNMENT AGENCY
ADDRESS (include ZIP Code)		GOVERNMENT PRIME CONTRACT NO. CONTRACTOR'S REFERENCE NO.
If moneys payable under the contract have been assigned, give the following:		EFFECTIVE DATE OF TERMINATION
NAME OF ASSIGNEE		
ADDRESS (include ZIP Code)		PROPOSAL NO. CHECK ONE <input type="checkbox"/> INTERM <input type="checkbox"/> FINAL
SF 1435, SCHEDULE OF ACCOUNTING INFORMATION <input type="checkbox"/> IS <input type="checkbox"/> IS NOT ATTACHED (If not, explain)		

SECTION I - STATUS OF CONTRACT OR ORDER AT EFFECTIVE DATE OF TERMINATION

PRODUCTS COVERED BY TERMINATED CONTRACT OR PURCHASE ORDER	(a)	PREVIOUSLY SHIPPED AND INVOICED	FINISHED		UNFINISHED OR NOT COMMENCED		TOTAL COVERED BY CONTRACT OR ORDER
			PAYMENT TO BE RECEIVED THROUGH INVOICING	INCLUDED IN THIS PROPOSAL	TO BE COMPLETED (Partial termination only)	NOT TO BE COMPLETED	
		(b)	(c)	(d)	(e)	(f)	(g)
QUANTITY							
\$							
QUANTITY							
\$							
QUANTITY							
\$							

SECTION II - PROPOSED SETTLEMENT

NO.	ITEM	(Use Columns (b) and (c) only where previous proposal has been filed)		TOTAL PROPOSED TO DATE	FOR USE OF CONTRACTING AGENCY ONLY
		TOTAL PREVIOUSLY PROPOSED	INCREASE OR DECREASE BY THIS PROPOSAL		
	(a)	(b)	(c)	(d)	(e)
1	METALS				
2	RAW MATERIALS (other than metals)				
3	PURCHASED PARTS				
4	FINISHED COMPONENTS				
5	MISCELLANEOUS INVENTORY				
6	WORK-IN-PROGRESS				
7	SPECIAL TOOLING AND SPECIAL TEST EQUIPMENT				
8	OTHER COSTS (from Schedule B)				
9	GENERAL AND ADMINISTRATIVE EXPENSES (from Schedule C)				
10	TOTAL (Items 1 to 9 inclusive)				
11	PROFIT (explain in Schedule D)				
12	SETTLEMENT EXPENSES (from Schedule E)				
13	TOTAL (Items 10 to 13 inclusive)				
14	SETTLEMENTS WITH SUBCONTRACTORS (from Schedule F)				
15	ACCEPTABLE FINISHED PRODUCT				
16	GROSS PROPOSED SETTLEMENT (Items 13 thru 15)				
17	DISPOSAL AND OTHER CREDITS (from Schedule G)				
18	NET PROPOSED SETTLEMENT (Item 16 less 17)				
19	ADVANCE, PROGRESS & PARTIAL PAYMENTS (from Schedule H)				
20	NET PAYMENT REQUESTED (Item 18 less 19)				

(When the space provided for any information is insufficient, continue on a separate sheet.)

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1435-102

STANDARD FORM 1435
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REV. 7-80

SF 1435/continued

SCHEDULE A - ANALYSIS OF INVENTORY COST (Items 4 and 6)

Furnish the following information (unless not reasonably available) for inventories of finished components and work-in-progress included in this proposal:

	TOTAL DIRECT LABOR	TOTAL DIRECT MATERIALS	TOTAL INDIRECT EXPENSES	TOTAL
FINISHED COMPONENTS				
WORK-IN-PROGRESS				

NOTE.-Individual items of small amounts may be grouped into a single entry in Schedules B, C, D, E, and G.

SCHEDULE B - OTHER COSTS (Item 8)

ITEM	EXPLANATION	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

SCHEDULE C - GENERAL AND ADMINISTRATIVE EXPENSES (Item 9)

DETAIL OF EXPENSES	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

SCHEDULE D - PROFIT (Item 11)

EXPLANATION	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

(Where the space provided for any information is insufficient, continue on a separate sheet.)

STANDARD FORM 1435 REV. 7-88 PAGE 2

SF 1435/continued

SCHEDULE E - SETTLEMENT EXPENSES (Item 12)

ITEM	EXPLANATION	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

SCHEDULE F - SETTLEMENTS WITH IMMEDIATE SUBCONTRACTORS AND SUPPLIERS (Item 14)

NAME AND ADDRESS OF SUBCONTRACTOR	BRIEF DESCRIPTION OF PRODUCT CANCELED	AMOUNT OF SETTLEMENT	FOR USE OF CONTRACTING AGENCY ONLY

SCHEDULE G - DISPOSAL AND OTHER CREDITS (Item 17)

DESCRIPTION	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

(If practicable, show separately amount of disposal credits applicable to acceptable finished product included in Item 15.)

(Where the space provided for any information is insufficient, continue on a separate sheet.)

STANDARD FORM 1435 (REV. 7-80) PAGE 3

SF 1435/continued

SCHEDULE H - ADVANCE, PROGRESS AND PARTIAL PAYMENTS (Item 19)			
DATE	TYPE OF PAYMENT	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY
(Where the space provided for any information is insufficient, continue on a separate sheet.)			

CERTIFICATE

This is to certify that the undersigned, individually, and as an authorized representative of the Contractor, has examined this termination settlement proposal and that, to the best knowledge and belief of the undersigned:

(a) AS TO THE CONTRACTOR'S OWN CHARGES. The proposed settlement (exclusive of charges set forth in Item 14) and supporting schedules and explanations have been prepared from the books of account and records of the Contractor in accordance with recognized commercial accounting practices; they include only those charges allocable to the terminated portion of this contract; they have been prepared with knowledge that they will, or may, be used directly or indirectly as the basis of settlement of a termination settlement proposal or claim against an agency of the United States; and the charges as stated are fair and reasonable.

(b) AS TO THE SUBCONTRACTORS' CHARGES. (1) The Contractor has examined, or caused to be examined, to an extent it considered adequate in the circumstances, the termination settlement proposals of its immediate subcontractors (exclusive of proposals filed against these immediate subcontractors by their subcontractors); (2) The settlements on account of immediate subcontractors' own charges are fair and reasonable, the charges are allocable to the terminated portion of this contract, and the settlements were negotiated in good faith and are not more favorable to its immediate subcontractors than those that the Contractor would make if reimbursement by the Government were not involved; (3) The Contractor has received from all its immediate subcontractors appropriate certificates with respect to their termination settlement proposals, which certificates are substantially in the form of this certificate; and (4) The Contractor has no information leading it to doubt (i) the reasonableness of the settlements with more remote subcontractors or (ii) that the charges for them are allocable to this contract. Upon receipt by the Contractor of amounts covering settlements with its immediate subcontractors, the Contractor will pay or credit them promptly with the amounts so received, to the extent that it has not previously done so. The term "subcontractors," as used above, includes suppliers.

NOTE: The Contractor shall, under conditions stated in FAR 15.804-2, be required to submit a Certificate of Current Cost or Pricing Data (see FAR 15.804-2(a) and 15.804-6).

NAME OF CONTRACTOR	BY (Signature of authorized official)	
	TITLE	DATE
NAME OF SUPERVISORY ACCOUNTING OFFICIAL	TITLE	

STANDARD FORM 1435 REV. 7-88 PAGE 4

SF 1436, SETTLEMENT PROPOSAL (TOTAL COST BASIS)

SETTLEMENT PROPOSAL (TOTAL COST BASIS)

FORM APPROVED OMB NO.
9000-0012

Public reporting burden for this collection of information is estimated to average 2.5 hours per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden, to the FAR Secretariat (VRS), Office of Federal Acquisition and Regulatory Policy, GSA, Washington, D.C. 20405; and to the Office of Management and Budget, Paperwork Reduction Project (9000-0012), Washington, D.C. 20503.

FOR USE BY A FIXED-PRICE PRIME CONTRACTOR OR FIXED-PRICE SUBCONTRACTOR

THIS PROPOSAL APPLIES TO (Check one)		COMPANY
<input type="checkbox"/> A PRIME CONTRACT WITH THE GOVERNMENT	<input type="checkbox"/> SUBCONTRACT OR PURCHASE ORDER	STREET ADDRESS
CONTRACTOR WHO SENT NOTICE OF TERMINATION		CITY AND STATE (include ZIP Code)
NAME		NAME OF GOVERNMENT AGENCY
ADDRESS (include ZIP Code)		GOVERNMENT PRIME CONTRACT NO. CONTRACTOR'S REFERENCE NO.
If moneys payable under the contract have been assigned, give the following:		EFFECTIVE DATE OF TERMINATION
NAME OF ASSIGNEE		
ADDRESS (include ZIP Code)		PROPOSAL NO. CHECK ONE <input type="checkbox"/> INTERIM <input type="checkbox"/> FINAL
SF 1436, SCHEDULE OF ACCOUNTING INFORMATION <input type="checkbox"/> IS <input type="checkbox"/> IS NOT ATTACHED (if not, explain)		

SECTION I - STATUS OF CONTRACT OR ORDER AT EFFECTIVE DATE OF TERMINATION

PRODUCTS COVERED BY TERMINATED CONTRACT OR PURCHASE ORDER (a)	QUANTITY	PREVIOUSLY SHIPPED AND INVOICED (b)	FINISHED ON HAND		UNFINISHED OR NOT COMMENCED		TOTAL COVERED BY CONTRACT OR ORDER (g)
			PAYMENT TO BE RECEIVED THROUGH INVOICING (c)	PAYMENT NOT TO BE RECEIVED THROUGH INVOICING (d)	SUBSEQUENTLY COMPLETED AND INVOICED * (e)	NOT TO BE COMPLETED (f)	
	\$						
	QUANTITY						
	\$						
	QUANTITY						
	\$						

SECTION II - PROPOSED SETTLEMENT

NO.	ITEM (a)	(Use Columns (b) and (c) only where previous proposal has been filed)		TOTAL PROPOSED TO DATE (d)	FOR USE OF CONTRACTING AGENCY ONLY (e)
		TOTAL PREVIOUSLY PROPOSED (b)	INCREASE OR DECREASE BY THIS PROPOSAL (c)		
1	DIRECT MATERIAL				
2	DIRECT LABOR				
3	INDIRECT FACTORY EXPENSE (from Schedule A)				
4	SPECIAL TOOLING AND SPECIAL TEST EQUIPMENT (SF 1432)				
5	OTHER COSTS (from Schedule B)				
6	GENERAL AND ADMINISTRATIVE EXPENSES (from Schedule C)				
7	TOTAL COSTS (Items 1 thru 6)				
8	PROFIT (Explain in Schedule D)				
9	TOTAL (Items 7 and 8)				
10	DEDUCT FINISHED PRODUCT INVOICED OR TO BE INVOICED *				
11	TOTAL (Item 9 less Item 10)				
12	SETTLEMENT EXPENSES (from Schedule E)				
13	TOTAL (Items 11 and 12)				
14	SETTLEMENTS WITH SUBCONTRACTORS (from Schedule F)				
15	GROSS PROPOSED SETTLEMENT (Items 13 thru 14)				
16	DISPOSAL AND OTHER CREDITS (from Schedule G)				
17	NET PROPOSED SETTLEMENT (Item 15 less 16)				
18	ADVANCE, PROGRESS & PARTIAL PAYMENTS (from Schedule H)				
19	NET PAYMENT REQUESTED (Item 18 less 19)				

* Column (e), Section I, should only be used in the event of a partial termination, in which the total cost reported in Section II should be accumulated to date of completion of the continued portion of the contract and the deduction for finished product (Item 10, Section II) should be the contract price of finished product in Column (b), (c) and (e), Section I.

NOTE. - File inventory schedules (SF 1426, 1428, 1430, and 1432) for allocable inventories on hand at date of termination (See 49.206).

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1436-103

STANDARD FORM 1436 (REV. 7-85)
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SF 1436/continued

SCHEDULE A - INDIRECT FACTORY EXPENSE (Item 3)			
DETAIL OF EXPENSES	METHOD OF ALLOCATION	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

NOTE.- Individual items of small amounts may be grouped into a single entry in Schedules B, C, D, E, and G.

SCHEDULE B - OTHER COSTS (Item 6)			
ITEM	EXPLANATION	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

SCHEDULE C - GENERAL AND ADMINISTRATIVE EXPENSES (Item 6)			
DETAIL OF EXPENSES	METHOD OF ALLOCATION	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

SCHEDULE D - PROFIT (Item 8)		
EXPLANATION	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

(Where the space provided for any information is insufficient, continue on a separate sheet.)

STANDARD FORM 1436 (REV. 7-80) PAGE 2

SF 1436/continued

SCHEDULE E - SETTLEMENT EXPENSES (Item 12)			
ITEM	EXPLANATION	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

SCHEDULE F - SETTLEMENTS WITH IMMEDIATE SUBCONTRACTORS AND SUPPLIERS (Item 14)			
NAME AND ADDRESS OF SUBCONTRACTOR	BRIEF DESCRIPTION OF PRODUCT CANCELED	AMOUNT OF SETTLEMENT	FOR USE OF CONTRACTING AGENCY ONLY

SCHEDULE G - DISPOSAL AND OTHER CREDITS (Item 16)		
DESCRIPTION	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

(If practicable, show separately amount of disposal credits applicable to acceptable finished product included on SF 1426.)

(Where the space provided for any information is insufficient, continue on a separate sheet.)

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SF 1436/continued

SCHEDULE H -- ADVANCE, PROGRESS AND PARTIAL PAYMENTS (Item 19)			
DATE	TYPE OF PAYMENT	AMOUNT	FOR USE OF CONTRACTING AGENCY ONLY

(Where the space provided for any information is insufficient, continue on a separate sheet.)

CERTIFICATE

This is to certify that the undersigned, individually, and as an authorized representative of the Contractor, has examined this termination settlement proposal and that, to the best knowledge and belief of the undersigned:

(a) AS TO THE CONTRACTOR'S OWN CHARGES. The proposed settlement (exclusive of charges set forth in Item 14) and supporting schedules and explanations have been prepared from the books of account and records of the Contractor in accordance with recognized commercial accounting practices; they include only those charges allocable to the terminated portion of this contract; they have been prepared with knowledge that they will, or may, be used directly or indirectly as the basis of settlement of a termination settlement proposal or claim against an agency of the United States; and the charges as stated are fair and reasonable.

(b) AS TO THE SUBCONTRACTORS' CHARGES. (1) The Contractor has examined, or caused to be examined, to an extent it considered adequate in the circumstances, the termination settlement proposals of its immediate subcontractors (exclusive of proposals filed against these immediate subcontractors by their subcontractors); (2) The settlements on account of immediate subcontractors' own charges are fair and reasonable, the charges are allocable to the terminated portion of this contract, and the settlements were negotiated in good faith and are not more favorable to its immediate subcontractors than those that the Contractor would make if reimbursement by the Government were not involved; (3) The Contractor has received from all its immediate subcontractors appropriate certificates with respect to their termination settlement proposals, which certificates are substantially in the form of this certificate; and (4) the Contractor has no information leading it to doubt (i) the reasonableness of the settlements with more remote subcontractors or (ii) that the charges for them are allocable to this contract. Upon receipt by the Contractor of amounts covering settlements with its immediate subcontractors, the Contractor will pay or credit them promptly with the amounts so received, to the extent that it has not previously done so. The term "subcontractors," as used above, includes suppliers.

NOTE: The Contractor shall, under conditions stated in FAR 15.804-2, be required to submit a Certificate of Current Cost or Pricing Data (see FAR 15.804-2(a) and 15.804-6).

NAME OF CONTRACTOR	BY (Signature of authorized official)	
	TITLE	DATE
NAME OF SUPERVISORY ACCOUNTING OFFICIAL	TITLE	

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STATEMENT OF OWNERSHIP, MANAGEMENT AND CIRCULATION

(Act of Aug. 12, 1970; Sec. 3685, Title 39, U.S. Code)

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C. Total paid circulation	801	787
D. Free distribution	27	24
E. Total distribution	828	811
F. Left-overs	727	914

I certify that the statements made by me above are correct and complete.

Filed—September 30, 1997

(signed) David B. Levendusky

