

**NCMA**  
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## CHANGES: OUT OF SCOPE, NOW WHAT?



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## AGENDA

8:00 - 8:30 – Registration, continental breakfast and networking

8:30 – NCMA Announcements and Speaker Introduction

8:30 – 9:30 Presentation

- Speaker's will take Q&A & Discussion during the Presentations

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**William M. Pannier**



**William M. Pannier** is a senior counsel in Holland & Knight's Los Angeles office. Mr. Pannier practices in the areas of federal, state and local government contracts, providing counsel and representation across a broad range of matters that include contract negotiations, disputes, protests and claims. He also has experience in compliance and enforcement defense matters – including internal investigations, voluntary and mandatory disclosures, and civil false claims – as well as small business issues, teaming, subcontracting, prime-sub disputes and construction.

Before joining Holland & Knight, Mr. Pannier served in the U.S. Air Force JAG Corps, where he concentrated in government contracts, advising on all aspects of the procurement process from acquisition strategy to source selection, award and contract administration. Among other assignments, he supported the Space and Missile Systems Center in Los Angeles.

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**Goals for this session: Know this**

- How to recognize in-scope and out-of-scope changes
  - How to tell the difference and ways to respond
- Understand the rights of contractors and other parties in the face of an out-of-scope change
- Key steps for a contractor to take when there has been an actual or constructive change
- What to watch for in order to appropriately account for and quantify change impacts
- Best practices for developing and submitting compelling REAs and claims

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## The Changes Clause: our framework

- Changes Clause (FAR 52.243 ff.): Govt has the right to make **unilateral changes within the general scope** of the contract; such changes must be of the types specified in the applicable Clause.
  - -1, Fixed Price
  - -2, Cost Reimbursement
  - -3, T&M, Labor Hour
  - -4, Construction
- Said another way, the C.O. may direct the contractor to perform work within the general scope of the contract pursuant to the Changes Clause.

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## The Changes Clause: our framework

- Typically, changes involve the scope of work (or, for FAR Part 12 commercial item contracts, the terms and conditions), e.g.:
  - Drawings and specs
  - Method or manner of performance (“means and methods”)
  - Sequence of work
  - Place of product delivery
  - Manner of product shipment or packaging
- Bottom line: Govt (C.O.) has broad authority to alter and direct the contract work

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## Framework for understanding the Changes Clause

- Focus: **The Mission**
  - Govt needs flexibility. Why?
    - Requirements evolve or become more defined
    - Needs change
    - Technology evolves, advances, etc.
    - Contracts are years long
    - The acquisition process alone can take years (“Speed of Business” vs. “Congressional speed”)
  - Bottom line: Flexible contracts best suit mission demands. Inflexible contracts aren’t useful and would be T4C’d.

## Framework for understanding the Changes Clause

- Purpose is to provide the gov't flexibility concerning contract performance and administration
- Gov't can order additional work within the general scope without a new procurement.
- Contractor is to be appropriately compensated for formal and/or informal changes
  - Constructive changes
- Note: Contractor is typically required to proceed with the work, **even if there is a dispute**
  - The contractor has the duty to perform

## Framework for understanding the Changes Clause

- Resolve issues of contract interpretation
- Allows for implementing contractor suggestions
  - Errors in contract drawings and specs
  - Improvements in processes, products, etc.
- Bottom line: establish by contract a cooperative environment designed to fulfill mission requirements

## Changes – may give rise to issues

- Changes may have disruptive impacts
  - Cost
  - Schedule
  - Personnel
- Difficult to:
  - Establish cause and effect relationships (causation)
  - Calculate quantum (cost impacts)
  - Obtain full compensation on an REA or claim
- This is especially true where there are multiple changes

## Changes – may give rise to REAs/claims

- Preparing an REA / Claim
  - Must establish causation
    - Because of X, contractor suffered impacts Y and Z
      - Direct impacts
      - Indirect impacts
    - This must be clearly explained by narrative description and supported by backup
  - Need adequate proof of claimed costs
    - Cost or pricing data
  - Not a way to “get well” on an unprofitable contract

## Fundamentally: What is a Change?

- Change = Sole Source Award
  - Procurement process is time consuming, costly
  - Not so with Changes
    - Definite requirement not required
      - Don't even need complete specs
    - No competition
    - No publicizing the requirement
    - No J&A

## Fundamentally: What is a Change?

- No price competition, but it's not like the govt lacks bargaining power
  - Unilateral change
    - Govt driven change
    - Direct contractor what to do
  - Bilateral change
    - Not necessarily govt driven
    - Parties mutually agree and execute a mod
      - » Govt agrees to every single thing about the change

## Fundamentally: What is a Change?

- How do we know if a new procurement must be undertaken?
  - First principles: Unlawful to circumvent competition requirements
    - Must allow potential offerors to compete for what should be a new procurement
  - Policed through the protest process
  - General Rule: issues of contract administration are not subject to protest by a competitor
  - Out of scope change = New procurement = Basis for protest by actual or prospective offeror

### ***“Within the general scope” - Case law says...***

“The applicable changes clause permits changes in the ‘drawings, designs or specifications’; however, the change must be ‘within the general scope of the contract.’ Whether a change is within the general scope of the contract is not always easy to determine.

We believe there are sufficient similarities between this situation and that considered by the Court of Claims in *KECO* to warrant following the logic of that case in the present situation. In *KECO* a change from electric refrigerators to gasoline-driven refrigerators was held to be a change within the general scope of the changes clause. The court there stated that consideration should be given [to] both the magnitude and quality of the change and whether the original purpose of the contract had been substantially changed.

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### ***“Within the general scope” - Case law says...***

In light of all the circumstances, we cannot conclude that the original purpose of the contract was so changed here as to require a conclusion that the change was beyond the scope of the contract.” *Loral Electronic Sys.*, B-170584, FEB 9, 1971

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## Scope of the Competition Test - Case law says...

“As a general rule, our Office will not consider protests against contract modifications, as they involve matters of contract administration that are the responsibility of the contracting agency. 4 C.F.R. Sec. 21.3(m)(1) (1989). **We will, however, consider a protest that a modification is beyond the scope of the original contract, and that the subject of the modification thus should be competitively procured absent a valid sole-source justification.**

## Scope of the Competition Test - Case law says...

In weighing the propriety of a modification, we look to whether there is a material difference between the modified contract and the prime contract that was originally competed. In determining the materiality of a modification, we consider factors such as **the extent of any changes in the type of work, performance period and costs between the contract as awarded and as modified.** We also consider **whether the solicitation for the original contract adequately advised offerors of the potential for the type of changes during the course of the contract that in fact occurred or whether the modification is of a nature which potential offerors would reasonably have anticipated under the changes clause.**” *Neil R. Gross & Co.*, B-237434, Feb 23, 1990 (citations omitted).

## Scope of the Competition Test

- Broad scope = latitude
- The broader the contract's scope, the broader the range of changes that are "in the general scope of the contract"
- Scope of the Competition Test: What work would offerors have perceived to be within the original competition?
  - Objective question viewed from the perspective of offerors from the original procurement
  - Fact-focused inquiry
    - Prices
    - Nature of proposals
    - Who were the actual offerors?

## More about Scope - Case law says...

"To determine what potential offerors would have reasonably expected, consideration should be given, in our view, to the procurement format used, the history of the present and related past procurements, and the nature of the supplies or services sought. A variety of factors may be pertinent, including: whether the requirement was appropriate initially for an advertised or negotiated procurement; whether a standard off-the-shelf or similar item is sought; or to whether, e.g., the contract is one for R&D, suggesting that broad changes might be expected because the gov't's requirements are at best only indefinite." *Am. Air Filter Co.*, B-188408, June 19, 1978

## Scope - Key questions for the inquiry

- Is the contract's original purpose substantially changed?
- Do the original contract and the contract as changed require essentially the same performance?
- Had the contract as changed been solicited in the first place, would the competition have been affected?
- Will a new procurement garner lower prices?
- Does a contract clause or provision permit the change?
- Note: "general scope" is broader than the express language of the contract (e.g., SOW, specs, drawings)

## "Within the general scope" - U.S. Supreme Court says...

- Work "within the general scope of the contract" is work that "should be regarded as fairly and reasonably within the contemplation of the parties when the contract was entered into." *Freund v. U.S.*, 260 U.S. 60 (1922).
- What do we know from the Changes Clause?
  - *The parties expect changes within the general scope.*

## “Material Difference” test - Case law says...

“In determining whether a modification triggers the competition requirements in CICA, our Office looks to whether there is a material difference between the modified contract and the contract that was originally awarded. In assessing whether a contract modification is outside the scope of the original agreement, we examine whether the original nature or purpose of the contract is so substantially changed by the modification that the original and modified contracts are essentially and materially different.

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## “Material Difference” test - Case law says...

In assessing whether the modified work is essentially the same as the effort for which the competition was held and for which the parties contracted, we consider factors such as the magnitude of the change in relation to the overall effort, including the extent of any changes in the type of work, performance period, and costs between the modification and the underlying contract. Where an agency has relaxed a contract's performance requirements, our Office also looks to whether the change in requirements was the type that reasonably would have been anticipated under the solicitation, and whether the modification materially changed the field of competition for the requirement.” *Poly Pacific Tech., Inc.*, B-296029, June 1, 2005

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## Time Extensions

- More time to complete performance (finite) vs. more time on contract (indefinite)
  - Finite = in scope
  - Indefinite = circumventing competition
    - Must meet sole source requirements

## Outside the General Scope

- “General scope of the contract” is broader than the supplies or services described in the contract and being acquired under it
- If a change is outside the general scope, it’s a cardinal change – a breach of contract – and the contractor is not obligated to perform the contract (not just the change)

## Cardinal Change - Case law says...

“The basic standard ... is whether the modified job ‘was essentially the same work as the parties bargained for when the contract was awarded. [The contractor] has no right to complain if the project it ultimately constructed was essentially the same as the one it contracted to construct.’ Conversely, there is a cardinal change if the ordered deviations ‘altered the nature of the thing to be constructed.’ ... Our opinions have cautioned that the problem ‘is a matter of degree varying from one contract to another’ and can be resolved only ‘by considering the totality of the change and this requires recourse to its magnitude as well as its quality.’ ... ‘There is no exact formula. ... Each case must be analyzed on its own facts and in light of its own circumstances, giving just consideration to the magnitude and quality of the changes ordered and their cumulative effect upon the project as a whole.’ ... In emphasizing that there is no mechanical or arithmetical answer, we have repeated that ‘[t]he number of changes is not, in and of itself, the test...” *Air-A-Plane Corp. v. U.S.*, 408 F.2d 1030 (Ct. Cl. 1969).

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## Cardinal Change is a question of fact

- **Because of a change:** Has there been a change in the function of what was contracted for?
  - Same function generally means the change was within the general scope of the contract
- Is the essential purpose of the contract still the same?
- Has there been a significant change in quantity? (e.g., # of buildings, materials)
- Has there been a dramatic cost increase (or decrease)?
- Has there been a large number of changes?
  - Is this really a whole new project?
  - Has there been a significant cumulative impact?
    - For REA or claim based on a cardinal change, it is difficult to track all costs and efficiencies lost, but do your best
- **Case outcomes are inconsistent and unpredictable**

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## Acceleration (change in overall time of performance)

- Best practice: negotiate a bilateral mod and ensure all acceleration-related costs are covered
  - Note: neither suspension of work nor delays are changes or constructive changes
- However, delay may result in changes to sequence or means and methods, which may be compensable under the Changes Clause

## Types of Formal Changes

- Drawings and Specifications
  - General Rule: Changes are OK
- Means and Methods
  - General Rule: Changes are OK
- Contract clauses, terms and conditions (e.g., warranty clause)
  - General Rule: Changes typically are ***not*** OK

## Responding to the Change

- Essentially 3 choices:
  1. Accept without reservation
  2. Perform the new work subject to a reservation of rights
    - Give notice of the change
    - Acknowledge it's within the Changes Clause
      - Not a cardinal change
      - Not outside the general scope
      - Not a breach of contract
  3. Refuse to perform

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## Informal Changes typically giving rise to REAs / Claims

- 5 key categories:
  1. Contract interpretation issues
  2. Defective specs
  3. Constructive acceleration
  4. Superior knowledge – misrepresenting or failing to disclose material facts (“vital info”) relating to the work or specs
  5. Govt. interfering, failing to cooperate, or hindering performance
    - Includes overzealous inspection, inconsistent inspecting, testing, imposing new tests, related communications and conduct

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## What about Deductions in Scope?

- De-scope or relax requirements: Deductive Change vs. Partial T4C
  - Key issue: Is there a major or minor impact on the work?
  - No clear test
- By accepting a change, contractor forfeits T4C rights
  - May or may not impact recovery (FAR cost principles apply to REAs, FAR calls for fairness and reasonable cost recovery for TSP)
  - At a minimum, govt is generally good about paying consultant costs for TSPs, not so much for REAs
  - Lost profit should be included, in any event
- Competition violation if T4C/Change would have significantly affected the original competition

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## Notice

- Always inform the C.O. of any actions, orders, or interpretations that will require extra work AND ask (in writing) that the C.O. direct that such extra work be performed pursuant to the Changes Clause.
  - The govt. is not supposed to get something for nothing
- FAR generally requires contractor to assert its right to an adjustment within 30 days of a change order.
  - However, this is not strictly enforced, esp. if govt. is not prejudiced by belated notice.
  - Conversely, if govt. is prejudiced by not being on notice, then that's a problem. Contractor has implied duty to notify govt. of performance cost impacts.

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## Negotiating with Uncle Sam

- High – Low – meet in the middle vs. FCA
  - Daewoo
- **Better to negotiate an overall compromise than go line item by line item.** See FAR 15.405

## 15.405 Price negotiation

(a) The purpose of performing cost or price analysis is to develop a negotiation position that permits the contracting officer and the offeror an opportunity to reach agreement on a fair and reasonable price. A fair and reasonable price does not require that agreement be reached on every element of cost, nor is it mandatory that the agreed price be within the contracting officer's initial negotiation position. Taking into consideration the advisory recommendations, reports of contributing specialists, and the current status of the contractor's purchasing system, the contracting officer is responsible for exercising the requisite judgment needed to reach a negotiated settlement with the offeror and is solely responsible for the final price agreement. However, when significant audit or other specialist recommendations are not adopted, the contracting officer should provide rationale that supports the negotiation result in the price negotiation documentation.

## 15.405 Price negotiation

(b) The contracting officer's primary concern is the overall price the Government will actually pay. The contracting officer's objective is to negotiate a contract of a type and with a price providing the contractor the greatest incentive for efficient and economical performance. The negotiation of a contract type and a price are related and should be considered together with the issues of risk and uncertainty to the contractor and the Government. Therefore, the contracting officer should not become preoccupied with any single element and should balance the contract type, cost, and profit or fee negotiated to achieve a total **result—a price that is fair and reasonable to both the Government and the contractor.**

## Truth in Negotiations Act (TINA)

- Cost or pricing data required for negotiated changes exceeding the stated threshold.
- Cost Accounting Standards threshold is \$750,000 (FAR 30.201-4; FAR 52.230-1–52.230-5)
  - Example: Change adds \$800k in new work but deducts \$600k of original work = \$200k net, TINA still applies
- Estimates are OK – e.g., the Navy doesn't want to delay resolution pending actuals
- TINA does not apply to damages.

## More on REAs and Claims

- “Analyzing and resolving claims can be the most time-consuming, costly, and difficult of all contract administration tasks.” Navy SUPSHIP Ops Manual, 18 Aug 2015
- Your job is to make this task easier.

## More on REAs and Claims

- When changes and other significant events occur, generate relevant data to support claims, focusing on entitlement and quantum
  - Keep detailed, organized records
    - Document who did what, when, why, how (at least MFR)
  - Separately track and code time
  - Maintain a file with all relevant docs
  - Hire a lawyer to engage experts (Attorney-client privilege and work product protections)
- Ascertain cost impacts (based on appropriate supporting backup)
  - Direct cost approach
  - Reasonable cost approach
  - Total cost approach

## More on REAs and Claims

- Include detailed factual narrative, including timelines
  - Relevant facts (who, what, when, where, why, how)
    - Contract docs (K and mods)
    - Sequence of events
    - Applicable data
    - Persons with knowledge
  - Impact analysis
    - Cause and effect (Entitlement)
    - Cost impact (Quantum)
    - Expert analysis (SMEs, Accountants, Schedulers, etc.)

## More on REAs and Claims

- Include exhibits
  - Provide relevant supporting backup, etc.
  - Highlight specific material you want the C.O. to see
- Govt. can't and won't pay what it is not shown to be responsible for.
- Bottom line: **Make your claim overwhelmingly persuasive the first time.**

## Claim resolution

- Negotiation and Settlement (difficult when parties are entrenched in opposing positions)
- Alternative Dispute Resolution (ADR) – mediation, etc. – is increasingly popular
- Litigation (time consuming, distracting, and expensive for everyone)
- Note: often filing an REA or certified claim increases visibility and brings outsiders to the matter.
- This can be a productive way for issues to be given the attention they deserve, by people with a more objective perspective.

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## Questions?

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