



Contractor Claims Avoidance

Attention to claims management and avoidance must begin well before the start of a project and continue until project completion. Review and analysis of plans, specifications, and contract language early in the project can eliminate ambiguities and identify potential claim areas. Implementation of controls and procedures during the project can minimize or even eliminate many issues which later may become the basis for a claim.

Contralytics can provide contract and specification review to identify potential areas of conflict before projects get started, consulting services for setting up procedures and controls that minimize claims, and continuing consulting services for review of and recommendations on specific contract problems that might arise during work performance.

The Nature of Contract Disputes

Contract disputes usually occur when contractors are seeking equitable adjustment for problems encountered in the performance of the contract for which they are not responsible. These contract impacting problems might be the responsibility of the buyer or a third party, or they might be the result of contractually external factors. The dispute is usually over the allocation of responsibility or some element of the scope of contract impact.

Most disputes result from changes to contract work which are usually identified too late to go through the normal contract change procedure process. These changes can be just as real and damaging to orderly project performance as formal changes and are recognized as such by the courts. However, disputes can also grow out of a breakdown in negotiations between the parties during the formal change process. No matter how the dispute arises, negotiation is always the preferred mode of settlement by all parties. If settlement is not possible, some contracts contain arbitration clauses which detail the procedures for settling contract disputes. When no arbitration clause is included in the contract, the parties might still agree to arbitration.

In government contracts, contract disputes which are not negotiable between the parties are taken before a Board of Contract Appeals, the United States Court of Federal Claims, or regular federal courts. The special Boards and Courts are generally comprised of judges with particular experience in the specifics of government contracting and in a particular branch of government. These agencies function as legal bodies and have built a large body of opinion relative to government contracts.

In commercial contracts, if a negotiated, mediated, or arbitrated settlement cannot be achieved, the contractor must pursue his case in the civil courts. No matter what mode of settlement is pursued, the contractor should present his case in the best possible manner if he is going to convince the negotiators, arbiters, or judges of the validity of any proposed contract adjustment.



The Dynamics of Contract Disputes

To understand how contract dispute situations can be avoided, a thorough understanding of their causes is essential. Disputes usually arise where contract requirements language is open to interpretation or where the facts concerning non-conformance to contract requirements are non-existent, incomplete, or are otherwise defective. Even where the contract and the facts are clear, disputes can arise about the exact nature and size of a contract impacting event. This is particularly true when the contractor has suffered disruption and loss of efficiency, since there is no totally objective method in existence for quantifying such impacts.

Whenever contract performance is degraded by an impacting event, contract management is faced with the formidable task of getting the buyer to agree to a change in the contract commensurate with the nature and size of that impacting event. Impacting events might be changes to the workscope or schedule issued by the buyer, or they might be the result of forces totally external to the contract. The most likely types of contract performance impacting events are:

- Workscope Changes (content or schedule)
- Late or Deficient Information, Material, or Equipment
- Stop Work Orders
- Force Majeure Events
- Other Contract Resource Demands
- Inadequate Contractor/Subcontractor Performance

When a contract performance impacting event occurs, the contract must be analyzed to determine if the impact has been anticipated and language has been included to deal with all its implications. If the particular impacting event was anticipated, the contractor must follow the contract specified procedures. If the particular impacting event was not anticipated, the contractor must proceed with the specified general procedure for changes to the contract (almost all major contracts, commercial and government, include change clauses which specify procedures to be followed in the preparation and presentation of change requests).

Government contracts frequently include a timing requirement which limits the time a contractor has to pursue a claim from the time the impact is identified or should have been identified. If a claim is to be avoided, this places an increased burden on the contractor for early identification of problems, in-place and efficient change procedures, and a real time collection of the data necessary for effective change presentation.

Government change clauses generally require the contractor to estimate the performance scope (direct impact) of the proposed change in terms of manhours, dollars, and time, whereas commercial change clauses are frequently limited to estimates in dollars only. In addition, it is sometimes necessary to estimate the indirect impact of delay, disruption, and inefficiency. This indirect impact must also be stated in manhours, dollars, and time for government contracts.



The basic methodology for determining the delay of impacting events has standardized around the use of Critical Path Method (CPM) network scheduling techniques. CPM, in many of its configurations, is widely accepted by government negotiators, industry arbitrators, civil courts, and government contract appeals boards and courts. The application of CPM in determining schedule impacts, however, varies widely from user to user, since the exact technique of application is dictated by the availability of data and different contractors collect different types and levels of data in support of their varied management information and accounting systems.

Determining disruption and loss of efficiency from contract impacting events requires the use of less exacting techniques than CPM. There are many methods in use for quantifying disruption and inefficiency, but all methods require reliance on subjective evaluations. Even sophisticated modeling techniques that use all objective data for their inputs rely on a subjective evaluation of element relationships at the basic algorithm level of the model.

A reliance on subjective evaluation is an open invitation for dispute between the contract parties. However, finding ways to eliminate or minimize such dispute is essential to the contractor, since the real cost of indirect impacts from contract impacting events can be as much or even more than those for the direct impact.

Complicating a potential agreement between the contract parties on the scope of a proposed change is the difficulty of understanding the complex relationships of all the impacted and impacting elements of contract performance and the dynamics of those relationships. With this complication of dynamic relationships, it is understandably difficult to show the kind of clear cause and effect relationship between a proposed change and its calculated scope of impact, which is the usual demand of the buyer before he will agree to a contract change. The contractor, therefore, has the burden of assuring that he has adequate data and an adequate presentation of that data, if he is going to successfully negotiate a contract change that captures the full impact he has suffered and avoid costly claims which are necessary for recovery when contract change negotiations fail.

The following discussion presents areas of operation and management that most frequently present problems in claims avoidance. There is an obvious difference in which of these problems might be critical to different types of businesses, different types of management structures, or too many other variables.

Probable Product Mix

Many U. S. industrial businesses are caught on the horns of a dilemma when it comes to optimizing operational procedures and production processes. Most industries have an available mix of commercial and government contracts on which they can bid. The contractual differences between commercial work and government work call for very different policies and procedures. If a business were projecting mostly commercial work with an occasional government but non-military job, it might be possible to design a set of procedures that were primarily



oriented to commercial contracts but with the flexibility to accommodate a non-complex government contract without excessive loss of efficiency. If the company were anticipating a 50-50 split between government and commercial work, it would probably be better to have two sets of at least some procedures. If the company were anticipating a significant portion of their business to be military work, a strong separation in all aspects of the required work should be considered between commercial and government work.

To further complicate the issue, many businesses have a significant variation in their products even within the general parameters of commercial or government work. These different products might dictate wholly different approaches to optimizing production output. These different production necessities usually mean different procedures to avoid potential claims situations or, more often, some sort of compromise in the procedures which seeks an optimum solution across the anticipated product spectrum.

The product mix basis for procedural changes could be from stated company policy, from the company's own analysis, or it could be generated by Contralytics or the company based on market analysis, company goals and objectives, and company capabilities. However the probable product mix is generated, it is an essential building block for procedural changes required for claims avoidance.

Estimating and Bid Procedures

Market dynamics can cause frequent shifts in estimating and bid policy within any company. It is essential for every company to remain competitive, and when the market shrinks and your competitors start bidding at greater risk or with purposefully lower margins, you must likewise trim your estimates. In this extremely competitive atmosphere, overruns will be common and attention will naturally become focused on assuring that any changes incurred in the contract be negotiated for the maximum justifiable amounts.

In exceptionally competitive bidding situations, it is more important than ever that management have as accurate an estimate as possible and as much backup data as possible when conducting bid reviews. If your company works like most, it is at bid review by top management that broad bidding strategies are considered to enhance the bottom line of the bid. When such changes are made, there must be procedures in place that will allow quick modification of the bid while still preserving a structure that is conducive to later change justification.

The structure and detail breakdown of the bid is very important to analyses that must be performed for change pricing. Proper estimate structure provides a rational basis for direct cost estimating of changes, and for estimating delay, disruption, and acceleration. In many government contracts this estimate is exposed during the bid process, and as a result, becomes even more important by having defacto approval by its government acceptance. However, it can also be helpful in good faith commercial negotiations.



Contracting Procedures and Controls

Businesses should have contracting procedures in place which generate, through the negotiating process, contracts with clearly defined baselines and steps to be taken in the event that contract changes are experienced. While most contracts have change clauses, many of those clauses are short on the specifics of what will be presented, what analysis techniques are acceptable, in what format the change will be presented, what alternatives are available to the parties when an impasse is reached in negotiations, etc. When these items are resolved during contract negotiation rather than after some major impact to the contract has occurred, it is frequently much easier to arrive at definitions and procedures which are more equitable for both parties.

It is usually a contracts department or other group, such as project management that has the responsibility to prepare and negotiate contract changes, but they rely extensively on other groups to identify potential changes, scope the requirements of the change, prepare the technical details of the change, and price the change. For these other groups to contribute effectively to the contract management effort, it is essential that they be thoroughly conversant with any unusual requirements of the specific contract. The contract management group must take the responsibility for the analysis of contract requirements and the dissemination of those requirements to all effected parties.

To facilitate this required communication and coordination, it is advantageous to have a reliable procedure in place rather than to rely on people activated systems, which can be unreliable, uneven from program to program, and frequently undocumented. Maintaining a complete and accurate record, though bothersome and costly, can prove invaluable in change negotiation and absolutely essential if arbitration or litigation is required.

Production Planning and Control

Production planning and production control are critical elements of all change negotiations. Production planning provides the basis against which all kinds of change impacts are measured, such as work item growth, resource usage growth, delay, disruption, and acceleration. Without a base plan, it is difficult to successfully negotiate the quantum value of contract changes which increase the contract value, particularly where impact growth is anticipated or has been experienced.

Most major contracts, whether commercial or government, now require a detailed plan and schedule for work performance, usually specifying a CPM-type computer program. Even when this is not required, it is usually to the contractors benefit to use one, not just for the increased efficiency of sound job planning but for its utility in avoiding claims by making change quantification more objective and less subjective and thereby enhancing the possibility of successful negotiation.

As crucial as the original plan is for claims avoidance, the ongoing performance of progress statusing, change integration, and resource reallocation is just as vital. In fact, there is really no substitute for being able to



accurately show the impact of a change at the time of its institution into the contract, and this depends on the exact status of production, materials, and resources at the time of the change. This is the true impact of the change and the proper basis for the quantification of the change. The more accurate and timely is this information, the greater the likelihood of an equitable change negotiation.

Material Planning and Logistics

One of the primary causes of delay, disruption, and acceleration is the late arrival of materials. Many times this delay and its adverse effects are the responsibility of the buyer. To assure that the buyer shoulders that responsibility, it is necessary for the contractor to have data adequate to clearly establish responsibility, allow objective quantification of the impact, and show a cause-and-effect relationship between the late material and its resultant impact.

Providing data sufficient for this task requires detailed material identification, approval, ordering, scheduling, storage, inspection, and delivery to the job site procedures, accompanied by comprehensive record keeping. Successfully negotiating a change for late material frequently depends on the documentation that shows when it was scheduled for some particular step in its logistic travels and when it actually arrived. These records must be part of a uniformly applied procedure rather than relying on personal recall of the facts for maximum effectiveness when presenting the change for negotiation.

The most effective material planning and control data is usually produced in an integrated system with production planning and control. When these two areas have been integrated in planning and scheduling, it is much easier to establish the validity of the material's proper schedule and to identify and display cause and effect relationships leading to impacts.

Quality Control/Assurance

Quality control and assurance is part of the last steps in the production process and, as such, is very important in the claims avoidance process. Many claims by the buyer against the contractor concern the failure of installed systems or components at product delivery or shortly thereafter. QA/QC procedures must include comprehensive test, inspection, and approval procedures where the customer is required to sign off on completed systems.

One of the problems frequently encountered in businesses is where the buyer's personnel remain in residence during repair, overhaul, or renovation work or where the buyer's personnel are phased into new construction before final product delivery. If systems are being used by the buyer's after they have been installed, repaired, or overhauled, they can be misused or broken. Any additional work required to restore the system to its original condition before final delivery should be to the account of the buyer not the contractor, but the buyer frequently tries to shift responsibility to the contractor. This would not be possible with a comprehensive QA/QC and system/area close-out procedure.



Management Information Systems

With the use of computer systems on the rise in even smaller businesses, many have established or are working towards establishing integrated management information systems (MIS). Such systems can be highly effective in the claims avoidance effort by identifying potential problems as early as possible to upper levels in the management structure to assure a quick response. Good management information systems take their building blocks from the various detail computer programs in use in the company like the planning and scheduling program, the accounting program, and the human resources program. These data are then integrated into a series of exception reports, trend analyses, and projections which present various levels of detail for the various levels of management.

For the purpose of claims avoidance, the company must review its MIS report formats to assure that potential contract changes are easy to identify and that enough information is provided to allow management to give positive direction to implement the change analysis and preparation process. As with most complex computer systems, making report format changes and producing mountains of paper on a regular basis is expensive, care should be taken to limit any changes and additional reporting requirements to only those absolutely needed.

Management Organization and Procedures

Communications across many departments within the company and within those departments is a vital link in claims avoidance. Frequently, minor changes in reporting and responsibility structures in a department can be very effective in problem identification and in shortening response time, but top level management procedures offer an even better possibility for improving claims avoidance.

The individual analyses discussed above should concentrate on the procedures within the respective departments or groups that utilize mechanisms by which identified potential changes are analyzed, scoped, priced, etc. within those affected departments. However, since the individual analyses must then be assembled into a comprehensive change package with all the elements needed for successful negotiation, all levels of procedures should be structured to smoothly integrate as company-wide procedures. This provides the proper level of department management attention needed for effective implementation and assures that the procedures are efficient from the total company viewpoint and not bound by department parochial preferences or deficiencies.

Contralytics Claims Avoidance Services

Contralytics personnel have a wide base of experience in the development of effective negotiating positions for contract adjustments and in the actual planning, operation, and management of construction and heavy industry. This combination of expertise makes it ideal for instituting effective claims avoidance measures since it has the perspective of real management experience in which



to formulate needed claims avoidance changes without causing unnecessary disruption to the normal conduct of business.