STATE OF MARYLAND
BOARD OF CONTRACT APPEALS
6 St. Paul Street
Suite 601
Baltimore, Maryland 21202-1608
Telephone: (410) 767-8228
Toll Free Telephone: 1-888-717-4710

SUMMARY ABSTRACT
DECISION OF THE MARYLAND STATE BOARD OF CONTRACT APPEALS

Docket No. 2130 & 2173	Date of Decision: 9/26/2001
Appeal Type: [ ] Bid Protest	[X] Contract Claim
Procurement Identification: Under DPSCS Contract No. 96034	
Appellant/Respondent: PHP Healthcare Corporation Department of Public Safety & Correctional Services	

Decision Summary:

Interest - The Board may not award interest pursuant to the provisions of Section 15-222 of the State Finance and Procurement Article to the Sta

BEFORE THE
MARYLAND STATE BOARD OF CONTRACT APPEALS

In The Appeals of PHP Healthcare Corporation	)
	)
	) **Docket Nos. MSBCA 2130 & 2173**
Under DPSCS Contract No. 96034	)
	)
	)

APPEARANCE FOR APPELLANT: **John G. Sakellaris, Esq.**
Bernstein & Sakellaris
Baltimore, MD

Philip M. Andrews, Esq.
Kramon & Graham, P.A.
Baltimore, MD

APPEARANCE FOR RESPONDENT: **Alan D. Eason**
Assistant Attorney General
Baltimore, MD

OPINION BY BOARD MEMBER HARRISON

In 1996 Appellant entered into a contract (Contract) with the Department of Public Safety and Correctional Services (Department) to provide healthcare services to inmates in the Department's facilities in the Baltimore Region. The Contract covered the period July 1, 1996 through June 30, 1997, and was extended pursuant to an option for an additional one year period ending June 30, 1998. Another option covered the year beginning July 1, 1998 and ending June 30, 1999. When Appellant declined to perform during this second option year unless the Department negotiated changes in the Contract to address various pending claims it had filed, the Department terminated the Contract for default, effective June 30, 1998. The instant appeals involving the issue of the propriety of the termination for default, were the subject of an interlocutory decision by the Board dated January 17, 2001 which is incorporated herein as if fully set forth (see Ex. A). In that

interlocutory decision the Board ruled in the Department's favor on entitlement and, with the agreement of the parties, deferred ruling on the Department's damages.[1]

Findings of Fact

1. At hearings on May 31, 2001 and September 10, 2001, the parties entered stipulations regarding various items bearing on the Department's damages.

2. As summarized below the parties have stipulated to certain elements of the Department's damages due to Appellant's breach when it failed to perform the second option year covering the period July 1, 1998 through June 30, 1999:

TABLE A	
Amount	Damages Element
$19,807,008.0l	Total cost of replacement performance for the option period.
$(16,358,700.00)	Total cost to the State if PHP had performed during the option period (subject to disputed adjustments in Table B).
$(200,000.00)	Additional cost to the State attributable to Claim 2 (except for population shortfall) if PHP had performed during the option period.

3. Under the parties' stipulations the State is due damages in the amount of the net of the figures set forth above in TABLE A which is $3,248,308.01[2], subject, however, to the Board's determination

[1] This interlocutory decision also addressed and resolved in the Department's favor MSBCA 2080 challenging the propriety of exercising the second year option and the termination for default.

[2] ($19,807,008.01 - $16,358,700.00 - $200,000.00 = $3,248,308.01)

as to Appellant's entitlement to two additional adjustments to these damages. As to these additional adjust-ments set forth below in Table B, the parties have stipulated as to quantum, but dispute entitlement:

TABLE B	
Amount	Damages Element
$(322,864.80)	Additional cost to the State attributable to the population shortfall claim if PHP had performed during the option period.[3]
$(77,396.00)	Additional cost to the State attributable to the CPI and COLA adjustment if PHP had performed during the option period.

Decision

For the reasons set out below, Appellant is not entitled to the adjustments to the Department's damages summarized in Table B above. Thus, the Department's damages from the breach are $3,248,308.01 as summarized in Table A above, and final disposition in that amount is rendered in favor of the State.

A. Population Shortfall

The Board, in its final decision of January 11, 2001, dealing with population shortfall, denied Appellant's appeal on the population shortfall issue.[4] In doing so, the Board held that the Department did not make a "positive and affirmative statement" as to the number of inmates to be housed in the Baltimore Region during the term of the

[3] With regard to the original Contract year and the first option period, the Board ruled in favor of the State on entitlement on this population shortfall issue by final decision dated January 11, 2001. That decision is currently pending judicial review in the Circuit Court of Baltimore City in case no. 24-C-01-000584.

[4] The Board's decision of January 11, 2001 is incorporated by reference as if fully set forth herein.

Contract (slip opinion at pp.18 & 19), and that assuming arguendo such a representation was made, Appellant did not reasonably rely on the statement (slip opinion at p. 19).

The analysis of the population shortfall issue with regard to the Department's default termination damages is identical to that for the period during which Appellant performed under the Contract. The Board has determined that Appellant is not entitled to additional compensation based on population shortfall for its past performance. The Board also determines that Appellant would not have been entitled to an adjustment to its projected compensation based on population shortfall had it, in fact, performed during the second option year. Accordingly, the Board denies the adjustment of $322,864.80 requested by Appellant related to population shortfall.

B. CPI and COLA

Appellant asserts that if the Board recognizes the appropriateness of a CPI and COLA adjustment for the second option year covering July 1, 1998 through June 30, 1999, Appellant is entitled to a different CPI and COLA adjustment than is used in the Department's proposed modification extending the Contract for the second option year. The Board disagrees. We noted the following in our interlocutory decision of January 17, 2001:

> *Did the elimination of the "Baltimore Region" CPI by the Department of Labor and the change by the State Legislature from a percentage to a dollar amount per employee COLA materially alter the calculation of the Contract price for the last option year such that it no longer could be calculated as "set forth in the bid/offer and Contract" as was required by the Court of Appeals and Board of Public Works Advisory. We think not and conclude that the consent of the Appellant was not required.*
>
> *In order to determine the price for the second option year, an adjustment was required pursuant to the terms of the Contract for the CIP and the COLA changes, as defined in the original Contract. As a result of post contract award*

action by the Federal Department of Labor the CPI numbers no longer existed as defined in the Contract. Similarly, the COLA adjustment was predicated on a percentage and the State had switched to a flat dollar amount increase. Thus, both definitions had to be revised in order to calculate a new Per Capita Price for the second option year. However, while the boundaries for determining the COLA and CPI number may have changed, the option year price was still being determined by resort to the concept of a CPI and COLA as set forth in the Contract. (Slip opinion at p. 11)

We therefore deny the requested adjustment of $77,396.00 based on CPI and COLA.

For the foregoing reasons, the Board determines that the Department has sustained damages in the amount of $3,248.308.01 as a result of Appellant's breach of the Contract. The Board may not award interest pursuant to the provisions of Section 15-222 of the State Finance and Procurement Article to the State[5]

Wherefore, it is Ordered this day of 2001, that the Appellant's challenge to the Department's termination of the Contract for default is denied and it is further Ordered that the State take appropriate action to recover the sum of $3,248,308.01 representing its damages resulting from Appellant's breach of Contract.

Dated:

Robert B. Harrison III
Board Member

I concur:

[5] Section 15-222(a) of the State Finance and Procurement Article only permits the Board to award interest on money that the Board determines to be due to the "Contractor."

Randolph B. Rosencrantz
Chairman

Certification

COMAR 21.10.01.02 **Judicial Review.**

A decision of the Appeals Board is subject to judicial review in accordance with the provisions of the Administrative Procedure Act governing cases.

Annotated Code of MD Rule 7-203 **Time for Filing Action.**

(a) Generally. - Except as otherwise provided in this Rule or by statute, a petition for judicial review shall be filed within 30 days after the latest of:

(1) the date of the order or action of which review is sought;
(2) the date the administrative agency sent notice of the order or action to the petitioner, if notice was required by law to be sent to the petitioner; or
(3) the date the petitioner received notice of the agency's order or action, if notice was required by law to be received by the petitioner.

(b) Petition by Other Party. - If one party files a timely petition, any other person may file a petition within 10 days after the date the agency mailed notice of the filing of the first petition, or within the period set forth in section (a), whichever is later.

* * *

I certify that the foregoing is a true copy of the Maryland State Board of Contract Appeals decision in MSBCA 2130 & 2173, appeals of PHP Healthcare Corporation under DPSCS Contract No. 96034

Dated: _____

Mary F. Priscilla
Recorder

EXHIBIT A

BEFORE THE
MARYLAND STATE BOARD OF CONTRACT APPEALS

In the Appeals of PHP Healthcare Corporation	**)**
	) Docket No. MSBCA 2080, 2130 & 2173
Under DPS&CS Contract No. 96034	**)**

APPEARANCE FOR APPELLANT: **John G. Sakellaris, Esq.**
Bernstein & Sakellaris
Baltimore, MD

APPEARANCE FOR RESPONDENT: **Alan D. Eason**
Assistant Attorney General
Baltimore, MD

OPINION BY BOARD MEMBER HARRISON

Appellant timely appeals the termination of the above captioned Contract for default and the denial of its claims and the assertion of damages by the State related to the default termination.

Findings of Fact

1. In June 1996, the State of Maryland, acting through the Department of Public Safety and Correctional Services (Department), entered into the above captioned Contract with Appellant to provide medical services to correctional system inmates in the Baltimore Region. The initial term of the Contract was for the 12-month period of July 1, 1996 through June 30, 1997. The State had the right to unilaterally extend the Contract for two one-year periods.

   The Contract contained the following provisions relevant to the renewal options granted the Department.

1.4. RENEWAL OPTIONS

The Agency solely and unilaterally may extend the term of the contract the number of consecutive periods of one year each as are stated in TITLE 1.5.2, RENEWAL OPTIONS.

*** *** ***

1.5.2. RENEWAL OPTIONS:

1.5.2.1. First Option Period - July 1, 1997 through June 30, 1998

1.5.2.2. Second Option Period - July 1, 1998 through June 30, 1999

6.8.1. RENEWAL NOTIFICATION

If the Agency does not wish to exercise a renewal option, it shall notify the contractor at least 90 days prior to the expiration of the current term of the contract.

6.8.2. RENEWAL COMPENSATION

6.8.2.1. GENERAL

6.8.2.1.1. The maximum compensation payable to the Contractor for the next renewal period for the various services, operating costs and equipment costs required under the contract shall be calculated as stated in this SUBARTICLE.

6.8.2.2. RENEWAL CALCULATION

6.8.2.2.1. The figures for a renewal term will be calculated as follows:

6.8.2.2.1.A. New Per Capita Price

(Per Capita Price x Primary Care Percentage x (1+COLA)) + (Per Capita Price x (1 minus the Primary Care Percentage) x (1+(0.75 x CPI)))

6.8.2.2.1.B. All Other Dollar Figures

6.8.2.2.1.B.(1) Any other dollar figures appearing in the contract that are not directly related to Primary Care will change by the same percentage as the accumulated CPI adjustments made to the Per Capita Price from the

beginning of the contract.

6.8.2.2.1.B.(2) Any dollar figures appearing in the contract that are directly related to Primary Care will change by the same percentage as the accumulated COLA adjustments made to the Per Capita Price from the beginning of the contract.

Additionally, the Contract defined CPI and COLA as follows:

Cost of Living Adjustment — *The annualized percentage adjustment in the salaries the Maryland State employees which has been authorized by the Maryland State Legislature to offset changes in the cost of living during a renewal term of this contract.*

Consumer Price Index — *The percentage change in the Medical Care index for Baltimore, MD for the period between January of the calendar year previous to the end of the current contract term and January of the calendar year in which the current contract term ends. This figure is stated in the Table entitled "Consumer Price Index for All Urban Consumers (CPI-U): Selected areas, by expenditure category and commodity and service group" which appears in the CPI Monthly Detail Report for January, which is published by the U.S. Department of Labor, Bureau of Statistics.*

2. The Contract provides for payment to Appellant to be as follows:

> *By the 15th business day of each month, the Contractor shall invoice the Agency for the amount listed in ATTACHMENT VI as PER CAPITA PRICE multiplied by the Billable Population Count.*

3. With the approval of the Board of Public Works, the Department issued unilateral Change Order No. 96034A, dated June 17, 1997, extending the Contract for the first additional one year period from July 1, 1997 to June 30, 1998.

4. Appellant performed during the first extension for ten months. However, by letter dated May 7, 1998 addressed to the Procurement Officer Appellant advised the Department that the "Department may

be required to cancel the renewal option of the Contract" and further advised that "unless the parties can agree on a price modification by May 13th, no unilateral change, Contract extensions, or other changes will be accepted by PHP, without PHP's written consent".

5. By letter dated May 13, 1998 from the Procurement Officer, Appellant was directed "to confirm in writing, to the Procurement Officer by 5:00 P.M. on Tuesday, May 19, 1998, that PHP will completely perform as directed above and will perform its obligations during the renewal option from July 1, 1998 through June 30, 1999." In this letter the Procurement Officer advised:

> *It is the intention of the Agency, at this time, to present this renewal to the Board of Public Works at its meeting of June 24, 1998. Subject to the Board's approval at that time, you are obligated and are directed to continue performing this Contract during the renewal period. Failure to confirm or an equivocal or conditional confirmation can be viewed as default and, taken together with Mr. Starr's letter to me dated May 7, 1998, can constitute your anticipatory repudiation of the Contract, warranting a termination for default pursuant to Subarticle 12.1 and any other legally available remedies.*

6. Appellant responded to the Procurement Officer's May 13, 1998 letter by letter dated May 19, 1998 requesting that the Contract not be renewed or extended nor terminated for de-fault.

7. By letter dated May 22, 1998 the Procurement Officer advised that he considered Appellant's May 19, 1998 letter as a notice of claim, asserted that Appellant was in default of the Contract and invited Appellant to show "just cause" in writing by May 27, 1998, why the Department should not terminate the Contract for default effective June 30, 1998, the date on which the Contract expired absent a second extension.

8. By letter dated May 27, 1998, Appellant disputed the Department's assertion that it had committed an anticipatory breach. In this letter Appellant stated:

> *In the event that the Board of Public Works approves a renewal of the contract including its reformation and provisions making PHP whole for past services and to the extent legally required, PHP intends to fulfill its obligations during the renewal period and will perform the contract during the renewal period.*

In the letter Appellant also advised the Department that it intended to bring the issues of Contract renewal before the Board of Public Works and sent a copy of the letter to the members of the Board of Public Works.

9. By letter to the Department dated the next day, May 28, 1998, Appellant advised:

> *As previously stated in numerous meetings and in correspondence to the Department, PHP has no intention to unilaterally rescind the contract; nor does PHP intend to unilaterally stop performing the contract. Indeed, in response to the meeting with the Department on May 12th, PHP gave assurances to the Department of the continued services that the Department requested following PHP's letter of May 6th and May 7th. In addition, PHP, pursuant to its obligations under the contract, will continue to provide services to the Department unless the Board of Public Works does not extend the renewal option for the fiscal year 1999.*

10. By letter dated May 29, 1998, the Department sent a modification to the Contract (Modification) and requested Appellant to sign and return the Modification as soon as possible. The Modification was never signed by either the Department or Appellant; but if given effect, the following modifications or changes to the Contract would have resulted:

(a) The Modification would have deleted paragraph

6.8.2.2.1A in Article 6 of the Contract, which provides as follows:

6.8.2.2.1.A. New Per Capita Price

(Per Capital Price x Primary Care Percentage x (1+COLA)) + (Per Capita Price x (1 minus the Primary Care Percentage) x (1+(0.75 x CPI))).

(b) In place of the above deleted paragraph the Modification would have substituted the following:

6.8.2.2.1A New Annual Per Capita Price.

6.8.2.2.1A.(1) For the period of 7/1/96 through 6/30/98: (Per Capita Price x Primary Care Percentage x (1 + COLA)) + (Per Capita Price x (1 minus the Primary Care Percentage) x (1+(075 x CPI))).

6.8.2.2.1A.(2) For the period of 7/1/99: (Annual Per Capita Price x Primary Care Percentage) + ((Average Annual COLA for the renewal term x Regional FTE For The Period) / Regional Divisor) + Annual Per Capita Price x (1 minus the Primary Care Percentage) x (1+(0.75 x CPI))).

(c) In addition to confirming the understanding of the parties that the Per Capita Price was an annual rather than a monthly price,[1] the Modification also would have changed the definitions of the Consumer Price Index (CPI) and Cost of Living Adjustment (COLA) to be used for calculating the price for the last renewal option. The CPI was changed to reflect the Baltimore, Maryland

[1] The Board has denied Appellant's appeal in MSBCA 2159 which sought payment of $341,893,540.82 based on an alleged mistake in its price offer not discovered until after award. However, the Board of Public Works had only approved a contract amount annually of $16,544,682.00. Appellant has appealed this decision issued on September 15, 2000 to the Circuit Court for Baltimore City, Case No. 24-C-00-004987.

CPI being changed by the Federal Government to a Baltimore/Washington regional CPI after the contract was entered into and a post contract award change by the State legislature from calculating COLA on a percentage basis to a flat dollar award per employee.

(d) In addition, the Modification would have added two new terms with definitions which were not previously in the Contract. It would have added the term "Regional FTE for Period" and defined it as 131. (a FTE means full time equivalent employee). Also, it would have added the term "Regional Divisor" and defined it as 7,266. Both items and definitions were used in the new formula to calculate the Per Capita Price for the new option year.

11. By letter dated June 2, 1998, Appellant continued to object to a default termination of its Contract.

12. During telephone conference calls on June 3 and 4, 1998, the Department instructed Appellant to sign and send back the Modification and confirmed that the Contract would be default terminated if Appellant did not sign the Modification. However, Appellant advised the Department that Appellant would not sign that Modification until after the Board of Public Works approved the renewal.

13. After the telephone conferences, by letter dated June 4, 1998 Appellant reasserted its position that no contract extension would be valid without the approval of the Board of Public Works and updated the quantification of previously filed claims. Also, by letter dated June 4, 1998, hand-delivered to the Secretary of the Board of Public Works, the Appellant protested any renewal or default termination of the Contract and requested to be heard on such issues.

14. By letter dated June 5, 1998 from the Procurement Officer, Appellant was default terminated effective 11:59 p.m. on June 30, 1998. The default termination was for the last renewal period.

The Board finds that the Procurement Officer had authority to issue the default termination on behalf of the Department.

15. As a result of the default termination, the Department withheld payment to Appellant in the total amount of $2,725,908.83 ($2,637,954.83 + $87,954.00).

16. Appellant filed a notice of claim concerning the propriety of the default termination and withholdings with the Procurement Officer by letter dated July 1, 1998. Thereafter, the claim was filed by letter dated July 30, 1998.

17. By letter dated April 19, 1999, the Department issued a final decision denying Appellant's claim for damages and upholding the default termination.

18. By letter dated March 10, 2000, the Department issued a final decision which affirmed withholding of the $2,725,908.83 and denied Appellant's claim for interest on the withheld amount. In this letter the State also affirmed its damages for the last option year in the amount of $3,448,308.01 based on payments made to a replacement contractor for the last option year.

19. The Board finds that Appellant has filed timely notices of claim and timely claims with the Procurement Officer and timely appeals to this Board with respect to the propriety of the default termination, the amounts being withheld, and the amounts being claimed as damages by the State as offsets.

Decision

We find that the termination for default herein was proper.

A. Consent Argument

As a result of the changes in the CPI and COLA and certain other changed matter, Appellant argues that its consent was required before any price for the new option year could be determined. For reasons more fully set forth below we conclude that Appellant could be required

to accept the last option year without the Department first obtaining its consent to the changes, because the boundaries for such changes and their implementation were set forth in the original Contract.

Focusing first on the changes in the CPI and COLA in the Modification Appellant argues that because of the changes in the CPI and COLA any attempt to exercise the last option year would have been in violation of the public bid requirements of the General Procurement Law (and COMAR).

In City of Baltimore v. Bio Gro Systems, 300 Md. 248(1984), the Court of Appeals considered a declaratory judgement action brought by the City to determine the validity of a renewed contract with a sludge disposal company. The issue in that case, as stated by the Court, was the propriety of an extension by mutual consent of a competitively bid contract beyond its original term. Id. at 300 Md. 249-250. The Court adhered to the general rule that a "true option" that simply extends an agreement on a unilateral and continuing basis, is permissible; however, terms involving future negotiations or alternating terms are improper because they circumvent the competitive bidding requirements. Id. at 300 Md. 249-250.

In the present matter, the Maryland Board of Public works had specifically spoken to the issue addressed in the Bio Gro Systems case; Board of Public Works Advisory No.: P-003-98, dated May 26, 1998. The Department was aware of the Board of Public Works Advisory since it was faxed to Appellant on June 3, 1998 by the Procurement Officer two days before the default termination. In its Advisory, the Board of Public Works stated that:

> *The only type of option that the State may exercise in lieu of a new procurement –– is one where "no negotiation [is] involved because the State alone holds the power to extend the contract" and the terms for the option period are set forth in the original bid (or proposal).*

Referring to Penpac, Inc. v. Morris County Municipal Utilities Authority, 690 A.2d 1094(N.J. Super. 1997) the Advisory further states, "the court [in Penpac] confirmed this principle even when the government and the contractor agreed to prices lower than those contained in the original contract."

In this Advisory, the Board of Public Works also set forth various guidelines, including as particularly applicable in this appeal:

> *I. A valid contract option is one where "the State alone holds the power" to exercise the option and the option price is fixed in, or is objectively ascertainable under the terms of the original contract. . . .*
>
> *II. D. Pricing:*
>
> *(1) Prices for both the initial term and the option periods (or option quantities) must be set forth in the original bid/offer; or*
>
> *(2) If option period prices are not fixed at the time of bid/offer, objective criteria for adjusting the initial prices when the State exercises the option (e.g., consumer price index, wholesale price index, appropriate published industry index) must be set forth in the bid/offer and contract.*
>
> *III. The exercise of a contract option must be approved and awarded before the initial term, or any previously-awarded option term, expires. A contract which has expired and is closed out may not be reinstated through modification, or the exercise of options.*

In the present appeals, once again, the rule of adherence to the original Contract terms in the exercise of an option applies to the question of whether the Contract herein could be properly extended. Extensions of contracts on alternating terms, specifically including

provisions governing pricing, are improper because they circumvent competition bidding requirements. A true option is unilateral, unconditional, and in exact accord with the original agreement. Appellant argues that the option exercise attempted here is precisely the type of option exercise that is against the public bid requirements of the State and would have been void if successfully exercised by the State. Appellant's argument continues that an anticipatory breach of what would have been a void contract would not support a default termination and thus the default termination must be set aside.

Did the elimination of the "Baltimore Region" CPI by the Department of Labor and the change by the State Legislature from a percentage to a dollar amount per employee COLA materially alter the calculation of the Contract price for the last option year such that it no longer could be calculated as "set forth in the bid/offer and Contract" as was required by the Court of Appeals and Board of Public Works Advisory. We think not and conclude that the consent of the Appellant was not required.

In order to determine the price for the second option year, an adjustment was required pursuant to the terms of the Contract for the CIP and the COLA changes, as defined in the original Contract. As a result of post contract award action by the Federal Department of Labor the CPI numbers no longer existed as defined in the Contract. Similarly, the COLA adjustment was predicated on a percentage and the State had switched to a flat dollar amount increase. Thus, both definitions had to be revised in order to calculate a new Per Capita Price for the second option year. However, while the boundaries for determining the COLA and CPI number may have changed, the option year price was still being determined by resort to the concept of a CPI and COLA as set forth in the Contract.

It is well settled law in Maryland that to be valid, the exercise of an option must be unequivocal and in accordance with the terms of

the option. Katz v. Pratt Street Reality Company, 257 Md. 103, 118(1970); Simpers v. Clark, 239 Md. 395, 401(1965); Foard v. Snider, 205 Md. 435, 446(1954).

The law in Federal procurement is in accord with the Maryland law on exercise of options. As provided in TECOM, Inc., IBCA No. 2970a-1, 95-2 BCA ¶27607, "[t]he courts generally tend 'to construe the attempt to accept the terms offered under the option strictly.' " TECOM at 137,593 (quoting Williston on Contracts, §61D (3d ed., 1957). The exercise of an option must consequently be "unconditional and in exact accord with terms of the option." Id. (quoting Corbin on Contracts, §264(1963)). "Nothing less will suffice unless the optionor waives one or more of the terms of the option." (quoting Id. Williston on Contracts, §61D). Indeed, not only are attempts to exercise options subject to strict scrutiny, the terms of the option are construed in favor of the party against whom the option would be exercised. Id.

In TECOM, the Board decided that the contractor could not be bound to an option by an unsigned modification. Id. at 137,594 (citing Mil-Spec. Contractors v. U.S., 835F.2d, 865,867-68 (1987)). A contract modification that requires endorsement by the contractor and the contracting officer is a "bilateral modification," and it is only binding upon execution by both parties. Id. (citing 48 CFR 43.103(a) (1986)).

In a similar matter, Varo, Inc., the Armed Services Board of Contract Appeals awarded summary disposition to the contractor because the government was adding clauses not originally in the contract in an effort to exercise a renewal option. ASBCA Nos. 47945, 47946, 96-1 BCA ¶28,161 at 140,563.

> An acceptance [of an option] must be unconditional and in exact accord with the terms offered. General Dynamics Corp., ASBCA No. 20882, 77-1 BCA ¶12,504. Any attempt by the Government to alter the conditions of the contractor's obligation as part of an attempted option exer-

> cise renders the attempt ineffective. Chemical Technology, Inc., ASBCA No. 21863, 80-2 BCA ¶14,728.

Varo, Inc. at 140,564 (quoting Grumman Technical Services, Inc., ASBCA No. 46040,95-2 BCA ¶27,918 (slip op., 5 September 1995)). "The inclusion in the exercise of an option of a provision(s) departing from the original contract provisions, makes such option exercise invalid." Id. (relying upon numerous authorities cited therein). See also Lear Siegler, Inc., ASBCA No. 30224, 86-3 BCA ¶19,155.

Adherence to the original terms of a contract in the exercise of an option is particularly important in matters of price, cost, and compensation. "The Government is simply not free to change the price which it will pay under the contract's option provision. Nothing could be more basic to the exercise of an option." A-1 Garbage Disposal & Trash Service, ASBCA No. 30623, BCA 89-1 ¶21, 323 at 107,528. This is true notwithstanding whether the government or the contractor benefits or loses from even a dramatic increase or decrease in costs. See United Service Corporation, ASBCA Nos. 25786, 25981, BCA 82-2 ¶15,985 at 79,268-72.

It is not clear to us, herein, however, that before the option year price could be calculated Appellant, herein, had to agree to a new method of calculating the CPI and the COLA adjustments. The changes in the CPI and COLA do not negate the fact that the price in the FY 1999 option year is still calculated based on the CPI and COLA. While these terms in the Contract are defined in terms of the methodology for calculating in effect at the time the Contract was entered into, July 1, 1996, nothing in the Contract language suggests that a change in the methodology to calculate CPI and COLA is prohibited. The CPI is still the CPI and the COLA is still the COLA.

Appellant next argues that the requirement in the Modification to use 7,266 as a "Regional Divisor" and 131 as the number for Regional

FTE's constituted impermissible changes. Concerning this 7,266 Regional Divisor issue we note that we have denied Appellant's appeal in MSBCA 2076 which is incorporated herein by reference and made a part hereof. The 7,266 divisor was the number offerors' were required to use in calculating their final price offers and included in the Contract documents in Addendum No. 5. Concerning the Regional FTE (full time equivalent employee) issue, we note that 131 was the number of FTE's that Appellant had proposed in its final proposal to the State and that was incorporated into the Contract. The State does not need Appellant to agree to what it previously has agreed to. Accordingly, we find that the changes pertaining to the Regional Divisor and FTE herein are not such as to prevent the State from exercising its option without Appellant's consent or to require any pre-option negotiation.

B. Board of Public Works Approval

Appellant argues that the exercise of the option herein was deficient because it lacked the approval of the Board of Public Works. Although the Department otherwise advised Appellant that the option was being exercised under the option provisions of the Contract, the Department exercised its option to extend the Contract by not giving the Appellant notice of its intention not to renew as provided under ¶6.8.1.

6.8.1. entitled RENEWAL NOTIFICATION provides:

> *If the Agency does not wish to exercise a renewal option, it shall notify the contractor at least 90 days prior to the expiration of the current term of the contract. (emphasis supplied).*

It is not the case, as Appellant has argued, that the exercise of the option lacked the approval of the Board of Public Works. The above renewal language, exercising the option upon the failure to give notice, had been approved by the BPW as part of the original Contract.

Compare Contel Page Service, Inc., ASBCA No. 32100, 87-1 BCA ¶19540. That language existed, unchanged, on March 31, 1998, the date notice that the option would not be exercised was due. Accordingly, the Department already had the approval of the Board of Public Works to exercise the option by not giving Appellant notice to the contrary.

C. Anticipatory Repudiation Argument

Appellant next argues that it did not commit an anticipatory repudiation respecting the extension of the Contract for FY'l999.

Maryland courts have held that in order to constitute anticipatory repudiation, there must be a definite, specific, positive, and unconditional repudiation of the contract. Rosenbloom v. Feiler, 290 Md. 598, 613(1981); C.W. Bomquist & Co., Inc. v. Capital Area Realty Inventors Corp., 270 Md. 486, 494(1973). Maryland courts have found anticipatory breach only where a party's refusal to perform was positive and unconditional, that is, when in anticipation of the time of performance one definitely and specifically refuses to do something which he is obligated to do.

See Weiss v. Sheet Metal Fabricators, 206 Md. 195(1955) and cases and authorities cited at p. 204. A clear statement of the standard for what action constitutes an anticipatory breach is set forth by the Court of Special Appeals in Harrell v. Sea Colony, Inc., 35 Md. App. 300, 306(1977) when it approvingly quotes Corbin as follows:

> *In 6 Corbin, Contracts, §973, the standard for determining an anticipatory breach of contract is set forth:*
> *"In order to constitute an anticipatory breach of contract, there must be a definite and unequivocal manifestation of intention on the part of the repudiator that he will not render the promised performance when the time fixed for it in the contract arrives. Doubtful and indefinite standards that the performance may or may not take place and statements that, under certain circumstances that in fact do not yet exist, the performance will not take place, will not be held to*

> *create an immediate right of action. A mere request for a change in the terms or a request for cancellation of the contract is not in itself enough to constitute a repudiation."* (emphasis in original)

See also Fairfield Scientific Corp., ASBCA 21151, 78-1 BCA ¶13,082 recon. denied, 78-2 BCA ¶13,429(1978), affd, 228 Ct.Cl. 264 (1981); Howell Tool and Fabricating, Inc., 96-1 BCA 28,225, ASBCA No. 47939(1996) (anticipatory repudiation exists where one party to the contract manifests a positive, definite, unconditional, and unequivocal intention not to render the required performance).

Thus, a mere request for a change in terms or a request for cancellation of the Contract is not in itself enough to constitute a repudiation. Similarly, while a contractor must continue to work pending resolution of a dispute, a notice of claim, a claim or an appeal under the disputes clause is not an act of repudiation under the dispute resolution provisions of the General Procurement Law and COMAR. See also Norfolk Air Conditioning Service and Equipment Corporation, ASBCA Nos. 14080, 14244, 71-1 BCA ¶8617; Dale Construction Co. v. United States, 168 Ct.Cl.692, 721(1964); Howell Tool and Fabricating, Inc., supra.

We also note that the government has the burden of proof with respect to a default termination. Driggs Corp. v. Md. Aviation Adm., 348 Md. 389(1998); Lisbon Contractors, Inc. v. U.S., 828 F2d 759, 764 (Fed. Cir. 1987).

A Procurement Officer's subjective reasoning from a contractor's words or actions of an intention not to render the promised performance is not legally sufficient. Fairfield Scientific Corp., supra. (Board must be satisfied objectively that the actions were manifested in a manner susceptible of only one reasonable interpretation that the contractor unequivocally intended not to perform). Further, there is no anticipatory breach where the professed inability to perform can be

overcome and the contractor expresses a willingness to continue performance. Manhattan Lighting-Equipment Co., ASBCA No. 5113, 60-1 BCA ¶2646. This Board, similarly, has recognized that the standard for review of a default termination is "an objective one". The Driggs Corp., MSBCA 1775, 5 MSBCA ¶397(1996) at page 27.

Based on application of the above legal principles to the record in these appeals we find that the default termination was appropriate. Our review of the specifics supporting the default termination follows.

The default termination is supported by matter in Appellant's letters dated: May 7, 1998; May 19, 1998; May 27, 1998; May 28, 1998; June 2, 1998; and June 4, 1998. The statements supporting default termination in each of these letters are discussed below.

1. May 7, 1998 Letter

With respect to the May 7, 1998 letter, Appellant states:

> *. . . the Department has failed to negotiate an equitable change in compensation to offset the substantially increased costs associated with the Department's unilateral modifications. . . . Unless significant funds are paid to PHP under this Contract immediately, the Department may be required to cancel the renewal option of the Contract as of the beginning of the new fiscal year.*

In the above quoted portion of the May 7, 1998 letter, Appellant states that the Department may be required to "cancel" the renewal option because of Department actions. Nothing contained in this letter can be interpreted as a clear and unequivocal refusal to perform. However, a threat is definitely implied. If the Department does not pay Appellant significant funds (as an "equitable change in compensation" to offset increased costs) the Appellant may not perform.

May 19, 1998 Letter

A paragraph in the May 19, 1998 letter from Appellant provides as

follows:

> *As stated by officials of PHP to representatives of the Department during the meeting on Tuesday, May 12, the Department should not recommend renewal or extension of the contract unless the Department reaches a complete agreement or settlement with PHP that resolves all outstanding disputes and claims, and pays PHP increased compensation that is due and payable to PHP because of unilateral changes that were ordered by the Department and unilateral mistakes that have been made by the Department which have resulted in a substantial amount of uncompensated health care services that have been provided to inmates by PHP.*

As with the May 7, 1998 letter, Appellant reasserts its position that the State has taken actions which may relieve Appellant from its obligations. While the threat of non-performance is clearly made Appellant stops short of actually stating that it will stop performing before its legal position has been upheld through the disputes process.

May 27, 1998 Letter

In the May 27, 1998 letter Appellant states:

> *In the event that the Board of Public Works approves a renewal of the contract including its reformation and provisions making PHP whole for past services and to the extent legally required, PHP intends to fulfill its obligations during the renewal period and will perform the contract during the renewal period. Before the Department submits a recommendation or request seeking Board approval of the renewal, however, representatives of PHP want to have a face-to-face meeting with officials of the Department to discuss and negotiate changes and modifications that should be made in the contract and resolution of past claims. PHP will contact Secretary Stuart Simms to schedule that meeting.*

This letter clearly escalates the threat of anticipatory repudiation contained in the previous correspondence and is contained

in a response to the Procurement Officer's invitation of May 22, 1998 to show cause why Appellant's Contract should not be terminated for default.

May 28, 1998 Letter

In the May 28, 1998 letter Appellant states:

> *As previously stated in numerous meetings and in correspondence to the Department, PHP has no intention to unilaterally rescind the contract; nor does PHP intend to unilaterally stop performing the contract. Indeed, in response to the meeting with the Department on May 12th, PHP gave assurances to the Department of the continued services that the Department requested following PHP's letter of May 6 th and May 7 th. In addition, PHP, pursuant to its obligations under the contract, will continue to provide services to the Department unless the Board of Public Works does not extend the renewal option for the fiscal year 1999.*

This letter indicates that it is part of Appellant's response to the Procurement Officer's letter of May 22, 1998 inviting Appellant to show cause why its Contract should not be terminated for default. However, the letter conditionsperformance on Board of Public Works approval of the option.

In its June 2, 1998 letter Appellant stated that "PHP Healthcare remains committed to completing our contract obligations." However, that letter also indicates that Appellant does not believe that the Department has been acting in good faith to resolve the disputes between the parties.

June 4, 1998 Letter

The June 4, 1998 letter is over sixteen pages in length. It is addressed to the Department's Secretary. The first paragraph thereof provides as follows:

> *This letter responds to your request that PHP execute an unmodified renewal of the Contract by today. As we indicated to you during the phone*

conference, neither the state nor PHP is well served by this ultimatum. Renewal of the Contract requires a meeting of the minds of the parties. Because the Department has refused to negotiate in good faith modifications to the Contract, this has not occurred. PHP has no way of knowing: (i) whether the Department intends to repudiate its responsibilities for the renewal by its ongoing conduct and (ii) what if any other changes or modifications the Department intends for the Contract renewal period that it has offered to competing offerors but not to PHP.

We find that a fair reading of the June 4, 1998 letter to the Department constitutes grounds to terminate for anticipatory repudiation; i.e. it fairly states that Appellant will not perform in the FY'1999 option year unless the Department agrees to settle its claims on Appellant's terms. On pages 10 and 11 of the letter the following is stated:

*PHP suggests that there are two approaches to reach a settlement of the renewal and out-standi*ng claims.

First, the parties could agree to renew the Contract taking into account current pricing changes which reflect the changes adopted by the Department and offered as modifications to the Contract subject to approval by the Board of Public Works. For PHP to be willing to proceed with this option, a realistic financial settlement of the outstanding claims is needed which reflects a substantial discount from the amounts set forth in this letter.

Second, the parties could agree to mutually non-renew the contract on the grounds that the renewal option is void, provided that i), PHP gives temporary assistance to transition to a new contractor, ii) the Department addresses PHP claims as set forth in this letter within 45 days, iii) the Department agrees not to take adverse actions against PHP during the transition, and iv) the Department agrees to substanti-

ate administrative efforts set forth in this letter.

These threats that the claims (exceeding 9 million dollars) must be settled to Appellant's satisfaction in order for Appellant to have any obligations to perform during FY'1999 clearly rise to the level of an anticipatory breach. The letter also sets forth throughout several pages many administrative and management conditions Appellant would insist upon being implemented or adopted by the Department as a condition for Appellant's continued performance and additional renewal costs as related to its claims that exceed 4.7 million dollars. This letter alone, and certainly combined with statements set forth in previous letters as set forth above, provide objective grounds upon which a default termination could be based.

Based on the above we find that the Procurement Officer and Agency Head properly and reasonably determined that Appellant was in default for an anticipatory breach of the Contract, because Appellant would not have performed without the Department agreeing to various conditions and paying various claims that Appellant had no legal right to insist upon as a condition for performance in the FY'1999 option year. The Board also finds that Appellant never cured such breach. The Board further finds that the State is not required to send an option for renewal to the Board of Public Works for approval with matter contained therein that a contractor has no intention of performing in order to preserve the right of the State to terminate the contractor for default.

D. Price Change and Counter-Offer Argument

In our final decision in MSBCA 2159 we have rejected Appellant's argument that the change contained in the Modification to reflect the agreement of the parties that Appellant was only entitled to some fifteen million annually as approved by the Board of Public Works rather than twelve times that amount precluded exercise of the renewal

option. We reaffirm our decision in MSBCA 2159 herein.

We also find that the Department's insistence that Appellant sign the Modification to confirm that it would perform the Contract during the option year did not amount to a counter-offer. The facts in this case can be distinguished from those in Lear Sigler, Inc., supra. In Lear Sigler, the contracting officer issued a modification purporting to exercise an extension of the contract term which contained a funding contingency not in the original contract. The Armed Services Board of Contract Appeals held that the modification was not in accordance with the exercise of the option contained in the original contract. However, the Modification in the instant appeal does not impermissibly contain terms that differ from those in the Contract, and thus did not amount to a counter-offer that relieved Appellant from performing during the renewal period.

Accordingly, the appeals are denied. This decision, however consistent with Driggs Corp. v. MD Aviation Adm., 348 Md. 389(1998), is an interlocutory decision pending resolution of any issues of damages resulting from the Board's determination herein that the Department has met its burden of proof to demonstrate that the termination for default of Appellant's Contract was reasonable and in accordance with legal requirements. Upon receipt of this decision counsel are to contact the Board to schedule a conference to discuss any issue of damages.

So Ordered, this day of 2001.

Dated:

Robert B. Harrison III
Board Member

I concur:

Randolph B. Rosencrantz
Chairman

I certify that the foregoing is a true copy of the Maryland State Board of Contract Appeals interlocutory decision in MSBCA 2080, 2130 & 2173, appeals of PHP Healthcare Corporation under DPS&CS Contract No. 96034.

Dated:

Mary F. Priscilla
Recorder