

Recovery of Damages: Types of Damage and Methods of Proof

Prepared and Presented by:

Steve Williams
Commercial Litigation Group
YoungWilliams P.A.

steve.williams@youngwilliams.com

www.youngwilliams.com

Direct: 601.360.9007

Fax: 601.355.6136

Mobile: 601.594.9007

Street:
210 East Capitol Street
Suite 2000
Jackson, Mississippi 39201

Mail:
P. O. Box 23059
Jackson, Mississippi 39225-3059

RECOVERY OF DAMAGES: **TYPES OF DAMAGE AND METHODS OF PROOF**

Calculating damages for a change order or a construction claim is ultimately predicated on the basic theory of liability. Generally, two types of damages are recoverable in construction cases: those based on breach of contract and those based on tort liability.

1. Contract. Breach of contract arises when one party to a contract fails to do what the contract requires the party to do. Restatement, (Second) of Contracts § 235. A contract breach may occur whether the obligations of the contract are express or implied.

Under the AIA changes clause, changes ordered by the Owner require that the contract sum and the contract time be “adjusted accordingly.”

AIA document A 201 (1987 ed.), section 7.3.1 provides in part:

A Construction Change Directive is a written order prepared by the Architect and signed by the Owner and Architect, directing a change in the Work and stating a proposed basis for adjustment, if any, in the Contract Sum or Contract Time, or both. The Owner may by Construction Change Directive, without invalidating the Contract, order changes in the Work within the general scope of the Contract consisting of additions, deletions or other revisions, **the Contract Sum and contract Time being adjusted accordingly.** (emphasis added.)

The Federal Government changes clause requires the contracting officer to “make an equitable adjustment and modify the contract in writing.” Federal Acquisition Regulation 52.243-4 (d) (Aug 1987) provides in part as follows:

If any change under this clause causes an increase or decrease in the Contractor's cost of, or the time required for, the performance of any part of the work under this contract, whether or not changed by any such order, **the Contracting Officer shall make an equitable adjustment and modify the contract in writing.** However, except for an adjustment based on defective specifications, no adjustment of any change under paragraph (b) of this clause shall be made for any costs incurred more than 20 days before the Contractor gives written notice as required. In the case of defective

specifications for which the government is responsible, the equitable adjustment shall include any increased cost reasonably incurred by the Contractor in attempting to comply with the defective specifications. (emphasis added.)

Adjustments made under the changes clauses should reimburse the contractor for all costs caused by the change and should extend the contract time to account for delays to the project resulting from the change. The contractor is also entitled to receive reasonable allowances for overhead and profit on changes that increase the cost of the contractor's work. United States v Callahan Walker Constr. Co., 317 US 56 (1942); Nebraska Public Power District v Austin Power, Inc., 773 F.2d 960, 970-72 (8th Cir. 1985).

The contract adjustment should focus on the contractor's cost of performing the added work. Usually, the changes provision of the contract provides for pricing of the change order work. For example, AIA Document A201, General Conditions of the Contract for Construction (1987 ed.), sets out several methods for determining the price of changes or extra work in subparagraph 7.3.3. These are:

- (1) Mutual acceptance of a lump sum properly itemized and supported by sufficient substantiating data to permit evaluation;
- (2) Unit prices stated in the contract or subsequently agreed upon;
- (3) Cost plus a fee, either fixed or percentage; or
- (4) The method provided in 7.3.6.

Under Section 7.3.6, if none of the other methods is agreed upon, the architect determines the amount of time and money to be allowed for the change. In addition to allowing the contractor a reasonable amount for overhead and profit, the clause defines costs to include:

- (1) Cost of labor;
- (2) Cost of materials, supplies and equipment;
- (3) Rental cost of machinery and equipment, excluding hand tools;
- (4) Bond premiums and insurance, permit fees and taxes related to the work; and
- (5) Additional costs of supervision and field office personnel directly attributable to the change.

If the contractor disputes the architect's determination, he can resort to the disputes resolution provisions of the contract or file suit.

Generally, the goal of compensation for breach of contract is to place the parties in the position they would have been in had the contract been performed. Miller v. Robertson, 266 U.S. 243 (1924). Two major forms of damages result from breach of contract. Direct damages are those which flow from the direct, natural, and immediate impact of the breach. Special or consequential damages are those which do not flow directly from the breach itself but result as a consequence of the breach.

The latter damages must be within the contemplation of the parties or foreseeable in order to be recovered. Often, these types of damages are referred to as "impact" costs. Performance of the actual change might be relatively insignificant, but the change could still be more costly if it delays the work, disrupts the contractor's operations, or alters the contractor's planned method of performance.

Such delay and disruption costs are generally recoverable under changes clauses. See, e.g., Merrit-Chapman & Scott Corp. vs. United States, 429 F.2d 431 (Ct. Cl. 1970). Thus, contractors should carefully evaluate how changes affect the cost, manner, and time of

performance to ensure that all such factors are included in the change order request or claim.

Some of the typical cost impacts flowing from breach of the contract include the following:

1. Labor

Additional Man-hours
Overtime
Inefficiency/Loss of Productivity
Increased Wage Rates

2. Equipment

Prolonged or Inefficient Use
Added Equipment
Resort to More Expensive Equipment
Idle Equipment

3. Material

Additional Material
More Expensive Material
Material Cost Increases

4. Job Site Overhead

Added Supervision
Extended Supervision
Greater or Prolonged Commitment of Job Site Resources (office trailer, utilities, etc.)

5. Home Office Overhead

Additional Home Office Expense
Extended Home Office Overhead

In the case of Aetna Casualty and Surety Company v. Doleac Electric Co., Inc., 471 So. 2d 325, the Mississippi Supreme Court addressed some of the above damage elements as follows:

The general rule with respect to damages resulting from breach of contract is that where complete performance is prevented by either party, the other who is willing to

perform is entitled to damages sufficient to make him whole. *Beech v. Johnson*, 102 Miss. 419, 59 So. 800 (1912). The plaintiff in such a case is entitled to recover any damages directly attributable to the defendant's breach. *Luria Brothers & Co. v. United States*, 369 F.2d 701 (Ct.Cl.1966); *J.D. Hedin Construction Co. v. United States*, 347 F.2d 235, (Ct.Cl.1965).

An element of damage claimed in the case sub judice is loss of productivity of its labor. "That loss of productivity of labor resulting from improper delays caused by defendant is an item of damages for which plaintiff is entitled to recover admits of no doubt, *Abbett Electric Corp. v. United States*, 162 F.Supp. 772, 142 Ct.Cl. 609 (1958); nor does the impossibility of proving the amount with exactitude bar recovery for the item ... (citations omitted). It is a rare case where loss of productivity can be proven by books and records; almost always it has to be proven by the opinions of expert witnesses. However, the mere expression of an estimate as to the amount of productivity loss by an expert witness with nothing to support it will not establish the fundamental fact of resultant injury nor provide a sufficient basis for making a reasonably correct approximation of damages. See *Wunderlich Contracting Co. v. United States*, 351 F.2d 956, 968, 173 Ct.Cl. 180, 199 (1965)." *Luria Brothers, supra*, at 712-713. *Id.* at 330.

Another type of damages which receives much press attention is punitive damages. Exemplary or punitive damages are in addition to actual or compensatory damages. They are imposed for the punishment for the wrongdoing of the defendant and as an example so that others may be deterred from the commission of similar offenses which in theory protects the public. *Yazoo v. Mississippi Valley R. R. Co. v. May*, 104 Miss. 422, 61 So. 449 (1913); *Yazoo & Mississippi Valley R. R. Co. v. Hardie*, 100 Miss. 132, 55 So. 42 (1911).

Punitive damages are not recoverable for simple breach of contract. See *Hans Const. Co., Inc. v. Drummond*, 653 So.2d 253 (Miss. 1995). But, punitive damages may be recovered where the breaching party has acted maliciously, outrageously, or fraudulently so as to create an independent tort.

2. Tort. Tort liability is different from contract liability. Torts are vaguely defined as "a civil wrong other than breach of contract, for which the Court will provide a remedy in the form of an action for damages." Prosser, *The Law of Torts*, § 1 (5th ed. 1984).

In addition to the theory of simple negligence, modern litigation has included an expanding array of torts such as breach of implied warranties of good faith and fair dealing, negligent misrepresentation, wrongful interference with contract relations, conversion, and many others. Under tort theories of liability, the injured party can recover all damages “proximately caused” by the tort. The goal is to restore the injured party to the position it would have been in had the wrong not been committed.

3. Compensability. Whether sounding in contract or in tort, the contractor’s performance may be delayed by acts of the owner or other causes beyond the contractor’s control. Delay damages or impact costs are in addition to the direct damages discussed above. Generally, there are four types of delays on a construction project:

1. excusable delays or
2. non-excusable delays; and
3. compensable delays or
4. non-compensable delays.

Excusable delays are those that occur through no fault of the contractor. Under the Federal Acquisition Regulations, an excusable delay must be unforeseeable, beyond the control of the contractor and without the contractor’s fault or negligence. Federal Acquisition Regulation 52.249-10 (b) provides:

(b) The Contractor’s right to proceed shall not be terminated nor the Contractor charged with damages under this clause, if-

(1) The delay in completing the work arises from unforeseeable causes beyond the control and without the fault or negligence of the Contractor.

Examples of such causes include-

- (i) Acts of God or of the public enemy,
- (ii) Acts of the Government in either its sovereign or contractual capacity,

- (iii) Acts of another Contractor in the performance of a contract with the Government,
- (iv) Fires,
- (v) Floods,
- (vi) Epidemics,
- (vii) Quarantine restrictions,
- (viii) Strikes,
- (ix) Freight embargoes,
- (x) Unusually severe weather, or
- (xi) Delays of subcontractors or suppliers at any tier arising from unforeseeable causes beyond the control and without the fault or negligence of both the Contractor and the subcontractors or suppliers; **and**

(2) The Contractor, within 10 days from the beginning of any delay (unless extended by the Contracting Officer), notifies the Contracting Officer in writing of the causes of delay. The Contracting Officer shall ascertain the facts and the extent of delay. If, in the judgment of the Contracting Officer, the findings of fact warrant such action, the time for completing the work shall be extended. The findings of the Contracting Officer shall be final and conclusive on the parties, but subject to appeal under the Disputes clause. (emphasis added).

The clause gives several examples of the types of delays which qualify as excusable.

In addition to the unforeseeability and lack of fault requirements, the contractor in the federal setting is also required to notify the Contracting Officer in writing of the delay within 10 days of the event causing the delay. Again, this writing and timing requirement underscores the importance of understanding and following the terms of the contract.

Non-excusable delays are those which are caused by the contractor or its subcontractors, suppliers, or employees.

Compensable delays are those caused by the owner or persons under the owners control. The contractor receives compensation (equitable adjustment) and additional performance time for compensable delays.

Unusually severe weather can be an excusable delay under appropriate circumstances. If proved, the contractor is entitled to a time extension. But, since the

weather is not the fault of the owner, the contractor does not receive additional compensation because of the delay.

Under the Federal Acquisition Regulations, for example, the contractor must give the Government written notice whenever its work is delayed, hindered, or made more difficult by Government action. The contractor must give the contracting officer notice within 10 days from the beginning of any delay stating the cause of the delay. As soon as possible after the notice, the contractor should calculate the additional compensation claimed and supply the information with supporting documentation to the contracting officer.

All of a contractor's damages must be adequately proved. The contractor must establish the amount of its damages with reasonable certainty and must also show that the damages were caused by the party from whom the relief is sought. These standards of causation and reasonable certainty were explained by the Court in Wunderlich Contracting Co. v United States, 351 F So. 956 (Ct. Cl. 1965) as follows:

A claimant need not prove his damages with absolute certainty or mathematical exactitude. It is sufficient if he furnishes the Court with a reasonable basis for computation, even though the result is only approximate. Yet this leniency as to the actual mechanics of computation does not relieve the contractor of his essential burden of establishing the fundamental facts of liability, causation, and resultant injury.

Exact computation of damages is virtually impossible due to the complex inter-relationship of the various factors attributable to delay and imperfection in contractor's accounting system. However, contractors should present the best accounting records and job site documents to prove the actual cost of any claim. Contractors can significantly

improve their chances of recovering damages by keeping detailed and accurate records of their operations and of specific impacts of delay or disruption to their schedules.

Several categories of records which are helpful in proving delay damages include the following:

1. diaries
2. daily job reports
3. time records
4. accounting records
5. production records
6. photographs
7. charts
8. schedules

One tool used by contractors in determining impact is the Critical Path Method (“CPM”) Schedule. This tool allows the contractor to identify all activities required to perform the work. The inter-relationship between those activities are identified and plotted on charts. The time required for each activity is estimated, and this analysis allows the contractor to identify the chain of activities which take the most time to complete and which is referred to as “the Critical Path.”

A delay in any of the activities along the Critical Path will probably cause a delay to the entire project. Therefore, CPM Schedules can be helpful to a contractor in proving entitlement to additional time. However, since the CPM Schedule only shows worked as planned, it cannot be used as a substitute for records of the actual work performed.

Updated CPM Schedules and other types of project schedules can assist the contractor in proving his damages if they are updated on a regular basis. Furthermore, an as built CPM Schedule is a good tool to pinpoint and measure the impact of delays as compared to the original, planned CPM Schedule.

The Courts have also allowed contractors to recover overhead costs incurred during periods of owner-caused delays. Mississippi follows this rule. In Aetna Casualty and Surety Company v. Doleac Electric, Inc., 471 So.2d 325, the Mississippi Supreme Court held:

Aetna acknowledges the general rule that home office overhead is a well-recognized item of damage for delay and an injured party is entitled to recover it. *Guy James Construction Co. v. Trinity Industries Co.*, 644 F.2d 525 (5th Cir.1981); *J.D. Hedin Construction Co. v. United States*, 347 F.2d 235 (Ct.Cl.1965); *General Insurance Co. of America v. Hercules Construction Co.*, 385 F.2d 13 (8th Cir.1967). In the case sub judice Mr. Doleac testified that the overhead expense was calculated by taking the percentage of the overhead attributable to the project (5.9 percent) and applying it to the total overhead expense during the over-run period.

Recovery for office overhead is allowed where the cost of overhead attributable to the particular job is applied prorata to the additional time required to complete the job as a result of the breach. *See General Insurance Co. of America v. Hercules Construction Co.*, supra at 22; *Luria Brothers*, supra at 710-711; *J.D. Hedin Construction Company*, supra, at 259. *Id.* at 330.

Home office overhead and its recovery as a part of compensable delays are difficult subjects. The formula most often used for allocating extended home office overhead to the delay on a particular project is called the “Eichleay formula.” It became popular and was developed from a Board of Contract Appeals case, Eichleay Corp., 60-2 BCA ¶ 2688 (1960). Its use was affirmed in Capital Electric Co. v. United States, 729 F.2d 743 (Fed. Cir. 1984).

The basic formula is stated as follows:

EICHLEAY FORMULA

Step 1

Billings for This Contract	=	Percentage for Allocation of Home Office Overhead to This Contract
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Total Billings for All Contracts During Period of This Contract		

Step 2

Allocation Percentage (from Step 1)	X	Total Home Office Overhead for Period of This Contract	=	Home Office Overhead (in Dollars) Allocable to This Contract
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Step 3

Allocated Overhead Amount (from Step 2)	=	Daily Home Office Overhead Rate for for This Contract (in Dollars Per Day)
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Actual Days of Performance of This Contract		

Step 4

Daily Rate (from Step 3)	X	Number of Days Delay to This Contract	=	Claim for Unabsorbed Home Office Overhead (in Total Dollars)
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The discussion of damages in this chapter is by no means exhaustive. It will give the reader a basic understanding of the issues relating to recovery of construction damages and the types of damages available. As the old saying goes, “time is money.” And the saying is particularly true to those in the construction business. However, proof of damages is always the most difficult part of the claims process.

Contractors can significantly facilitate their recovery of damages by keeping detailed and accurate records of their construction operations and of the specific impact of delay and disruption to their schedules. Without such documentation, it may be difficult to prove the amount of damages suffered. Failure to maintain such records may significantly reduce or even defeat a contractor’s legitimate recovery of cost.

Contractors can also facilitate the recovery of their damages by the wise use of legal counsel and construction consultants in the preparation and presentation of their claims.