Quantification and Substantiation of Contractual Claims

(A short series of articles addressing some difficult and challenging areas.)

By Mark Entwistle FDBF

1. Head/Home Office Claims

The role of a Dispute Board – sole or multi-member, dispute avoider or dispute resolver - is challenging and is subject to varying attitudes and approaches, not only of parties to construction/engineering contracts, but also of DB members themselves. The legal and technical background and experience of the parties and DB members, and their understanding of the Contract and the obligations and rights of the parties, can vary considerably, creating a potent mix of ingredients from which a wholly baked and desirable product is expected to emerge.

Regardless of the factual matrix of any dispute, the reality is that the focus, and therefore the result, most often relates to money being in issue between the parties. Often, elements of a dispute can be complex and/or the sums involved very significant. In such circumstances, even 84 days is not a long time for a DB to do justice to the parties’ respective cases.

Readers will know well enough what the usual causes of dispute are and it is not proposed to address those well-known factors. Rather, the challenging issues presented by several particular aspects of quantum claims are to be considered. For this purpose, the series of papers will use as a model Contract the FIDIC Red Book (although all other FIDIC Contracts can be taken as following the same model so far as financial recovery for claims is concerned).

It is almost inevitable (save in relation to Employer’s claims for delay damages or arising from quality issues) that the party claiming money will be the Contractor. The heads of claim advanced by claiming Contractors are well-known, though not necessarily well understood around the world. This series of papers attempts to address some of the challenging issues that arise in relation to certain aspects of quantum claims; to suggest how a claiming party needs to approach its claims; how a responding party might reasonably demand to be persuaded; and how a DB should approach its determination of sums that may be found due for payment to the Contractor. The series will focus upon four key areas: additional head/home office overhead recovery, claims arising from disruption or unproductive working, additional site set-up/preliminaries charges and interest/financing charge recovery. This first paper addresses the first of those complex areas.

It should not be necessary to recite in detail the provisions of the FIDIC Red Book as regards a claiming Contractor’s financial entitlements when it comes to claims. Clause 20.1 sets out the procedure to be followed where a Contractor “considers himself to be entitled….. to any additional payment, under any Clause of these Conditions or otherwise in connection with the Contract…..”. In other words, it is recognised that a claiming Contractor has the right to frame its claims either under any clause of the Contract that confers entitlement in principle, and/or by reliance upon rights conferred by the applicable law. Under English law, that would permit a damages claim to be pursued where the Employer was asserted to have breached the contract.

Examples of Contract provisions that expressly permit financial recovery include: clause 4.7 (Setting Out) and clause 4.12 (Unforeseeable Physical Conditions) – both of which expressly
refer to additional Costs. Otherwise, it is to be observed, that the Contract is not a model of clarity as to the circumstances in which a Contractor might be entitled to advance financial claims based upon express entitlements under the Contract terms.

“Cost” is defined (clause 1.1.4.3) as meaning “all expenditure……incurred….on or off the Site, including overhead and similar charges…”

It can be seen that the essence of a Contractor’s entitlement to recovery of additional monies through the application of the express terms of the Contract, is framed as relating to additional costs incurred by circumstances where the Contract conditions state that recovery, in principle, can be made. That contractual route to recovery thus precludes claims for losses sustained (since such matters cannot be classified as “costs”).

Though it might be observed that all claims are different on their facts, the principles that apply can be thought of as universal and, thus, the approach to either advancing claims or considering them for payment may be regarded as standard practice. That does not render the issue of financial claims any less challenging, and the elements causing greatest discord and challenge never seem to vary. The first principal area of difficulty is addressed below.

Additional head/home office overhead recovery

This head of claim is most often (in fact, almost exclusively) applied in relation to delayed completion, though that need not necessarily be so. Additional overhead costs could legitimately be claimed even though completion occurred on time, or even early. The logic underpinning the usual claim advanced is that the claimant (Contractor) has been retained on the project (for reasons that entitle it to claim) for a protracted period. That additional period is often related to an extension of time claimed or granted, though that is not a necessary pre-cursor to such a claim. It is perfectly arguable that a Contractor might have completed early but for the event(s) relied upon.

Almost inevitably, this head of claim will be advanced by use of a formula calculation, though other means of quantification are possible, such as where a claimant can demonstrate, with supporting evidence, that certain specific additional head office costs were incurred as a direct consequence of the event(s) relied upon. The demands of brevity, however, mean that a focus will be played here on the use of formulae.

There are a number of formula calculations that, over the years, have become attractive to claimants or have been recognised, and even supported, in decided legal cases. Despite that, paying parties remain (perhaps understandably) nervous about accepting the quantified results of formulae used. Understandably, because it is not at all unusual for the outcome of the application of such a formula to derive a frighteningly large sum claimed, and it is not uncommon for the head/home office overheads claim to be the largest head of claim advanced.

Two significant points need to be borne in mind. Firstly, it is not sufficient for the claiming party to merely make the formula calculation without regard to the particular circumstances relied upon as underpinning the claim, or to the broader picture as far as the project is concerned. Secondly, the fact that a formula calculation can be argued either as a means of quantifying additional cost or sustained loss, means that great care needs to be taken to establish that entitlement to recovery is demonstrated in principle (having regard to the applicable Contract terms), and that quantification is substantiated and realistic.

It is not intended, here, to consider in detail the various formulae that are in (relatively) common usage, save to record that the Hudson Formula (generally now discredited) applies the
monthly/daily overheads written into the successful bid, the Emden Formula (generally preferred) is founded upon the claiming party’s published accounts, as is the Eichleay Formula (commonly used in the USA and Canada).

The significance of the use of a formula, at all, lies in the fact that the basis of the claiming party’s claim is that, generally as a result of the delayed completion of a project, either head/home office costs have been incurred in greater sums than would have been the case with timely completion (the “additional costs” argument), or that the prolonged retention of resources on site (workforce or management) has denied their use on future projects where they would have, once more, contributed to deriving income that would have funded the organisation’s head/home office costs (the “losses” argument).

It can easily be recognised that the approach taken by a claimant (arguing losses or additional costs) is likely to be dictated by exactly what the Contract allows to be recovered. There is nothing at all, in principle, wrong with that, though it might seem odd that a particular claimed sum could be potentially argued to constitute a cost or a loss, depending upon what was the claimant’s particular preference.

In either event, what the claimant needs to demonstrate (and the other party (and the DB) needs to be satisfied about) is that the cause of delay relied upon brought about the effect claimed, and that can only be properly established, it is suggested, by a forensic examination of the claimant’s company accounts (where additional costs are contended for), or by considering the plausibility of the argument that retention of resources on the project meant that opportunities for further and future contracts were lost (where loss of opportunity is the basis of claim).

Either way, it must be regarded as wholly insufficient for a claimant to merely apply a formula and think that the job is done. The application of a more critical approach to considering formula calculations has been reflected in many court judgments throughout the world.

So far as recovery under FIDIC Contracts is concerned, where additional costs form the basis of recovery, the claimant must, it is suggested, be in a position to bring forward in supporting evidence a forensic analysis of its accounts to demonstrate (to the applicable standard of proof) that:

1) additional head office costs were incurred during the period concerned,
2) the extent to which the claimant’s general panoply of overhead requirements were of a type that were applicable to its contracting operations,
3) such additional costs were directly attributable to the events that the claimant relies upon,
4) such costs were either expressly recoverable under the terms of the Contract (or not excluded thereby) or under the applicable law,
5) such costs had not been recovered by the application of other provisions of the Contract.

Where a loss-based approach is contended for, the claimant must be in a position to adduce evidence to the effect that:

1) the resources retained on the project were of a type that the claiming Contractor would have applied an overheads uplift to when pricing bids for future projects,
2) market conditions, at the time such resources might have become available, were such as to render it more likely than not that the Contractor could have acquired additional project work to deploy those resources upon, such as to once again enable them to contribute to overhead funding.
3) such costs had not been recovered by the application of other provisions of the Contract7.

In conclusion, it can be seen that claiming or allowing recovery of head/home office contribution is not a simple matter, even where the (seemingly straightforward) application of a formula might be permissible. The parties themselves and the DB (or other tribunal) should approach the matter with great care so as to avoid either allowing a claiming Contractor an unmerited windfall or denying a proper and valid financial entitlement to recovery.


2 The applicable period might be that when the delay actually occurred during the progress of the works, or the period of the extension itself at the end of the project.

3 In other words, overhead costs related to aspects of the business not connected to the contracting arm should be excluded.

4 For example, in the valuation of variations or by re-measurement of works.

5 For example, the retention of sub-contract resources might reasonably be expected to be omitted from the calculation where the sub-contracting market were such as to render available sub-contractors for future project work.

6 For this purpose, it is suggested, it is not necessary for a claimant to be required to supply evidence of declining project bidding opportunities.

7 Even though the basis of claim pursued is loss of opportunity, any contributions made by resources retained longer on site, by way of the undertaking of varied or additional re-measured works, would have reduced the loss sustained.

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