Proving a Total Cost or Modified Total Cost Method Claim

by Thomas S. Cosma and Mitchell W. Taraschi

Mentioning the concept of a 'total cost claim' to most experienced construction law practitioners will likely be greeted with a smirk and a derisive "good luck" comment. Few legal propositions can match the bar raised for proving such claims, expressed in the following judicial sentiments: This method "has never been favored by the court and has been tolerated only when no other mode was available and when the reliability of the supporting evidence was fully substantiated;"[1] trial courts "must use the total cost method with caution and as a last resort;"[2] and "the preferred way for a contractor to prove increased costs is to submit actual cost data because such data 'provides the court, or contracting officer, with documented underlying expenses, ensuring that the final amount of the equitable adjustment will be just that—equitable—and not a windfall for either the government or the contractor.'"[3]

So the logical question presented to any contractor contemplating a total cost method (TCM) or modified total cost method claim faced with overcoming such hurdles is, "why bother?" For two reasons, one practical and the other technical (in the legal sense).

On construction projects of substantial size and complexity, it is often difficult to tie specific breaches, or a single particular error or omission, to a discrete damage item—in the linear sense. While that difficulty has diminished with increasingly sophisticated construction cost accounting systems, not all contractors possess the financial and staff resources needed to effectively utilize such job cost accounting systems, and others are simply unwilling to devote the considerable time and expense involved in segregating their damage claims.

The other reason is found in the elements of a TCM claim itself. The ABA Model Jury Instructions on Construction Cases contains the following formulation of the TCM theory for recovery of damages:

> To recover any sums under the total-cost theory of damages, the contractor must prove by a preponderance of the evidence each of the following: (1) that the nature of the particular losses it suffered makes it impossible to attach a dollar figure to determine them with a reasonable degree of certainty; (2) that the contractor's bid for the contract was both a realistic and accurate bid when made; (3) that the contractor's actual costs spent on the project were reasonable under the circumstances; and (4) that the contractor was not responsible for its additional costs to complete the job because of its own delays and mismanagement. If the contractor fails to prove any one of these elements by a preponderance of the evidence, then you may not award the contractor damages. If the contractor has proved these elements, then you may award damages calculated by the difference between the contractor's actual costs on the project, plus a reasonable amount for overhead and profit, less what it has been paid so far on the contract.[4]

So the total cost method is based on a formula that *assumes* the contractor is owed the difference between the actual cost of the contract and the contractor's bid.[5] Even if the contractor could satisfy the first three prongs of the TCM test, what is the likelihood that a trier of fact would find in a large, complex construction project that took several years to complete, with scores of subcontractors and multi-prime contractors all working simultaneously, that the contractor-claimant was completely without sin? It is no wonder, then, that the New Jersey Department of Transportation's Standard Specifications for Road and Bridge Construction precludes claims based upon the TCM or modified TCM theory of recovery.[6]

Analyzing those decisions that have allowed such claims yields three observations: In each case there was clear, virtually undeniable proof of the defendant's underlying liability for breach of contract or a design error; where one or more of the elements required to uphold a TCM claim wasn't satisfied, the court slid into modified TCM mode rather than resort to an outright dismissal of the entire case;[7] and where the contractor presented a mixture of some claims that may be linked to discrete damages and others that may not, those courts allowed the jury to sort them out by charging *both* the TCM or modified TCM theory and the normal segregated damages' jury charge.[8] Nevertheless, each court was compelled to examine the elements of a TCM claim.

Courts that take a *strictissimi juris* approach to the TCM method hold that if a plaintiff cannot prove all four elements of the TCM, or if the defendant can disprove one of them, the court must deny recovery under the method. More liberal courts allow the use of a modified TCM to prevent the defendant from obtaining a windfall stemming from the plaintiff's inability to satisfy all of the elements of the TCM. Principally, the modified TCM allows a court to adjust the contractor's damage claim by reflecting, for example, the value of a contractor's errors in its bid preparation, damages traceable to the fault of the contractor or one of its subcontractors, or job costs found to be exorbitant.[9]

The Nature of the Particular Losses Makes Determining the Amount Impossible or Highly Improbable

The contractor must demonstrate that proving actual losses is either impossible or highly impracticable, and adequately separate any additional costs for which it is responsible.

When weighing the impracticability prong, where a plaintiff fails to maintain its records, courts are disinclined to allow a plaintiff to rely on the TCM "based on a bed of its own making."[10] Where the failure to maintain essential cost records is the reason why proof of actual damages becomes impossible or highly impracticable, the claimant is unlikely to meet with a receptive ear from the court.[11]

Probably the best example of a factual scenario where this test was satisfied is found in *J.D. Hedin Constr. Co. v. United States*.[12] A TCM claim was allowed for one issue: The additional cost of supplying and installing concrete piles where the specifications clearly stated cast-in-place piles, each within a thin steel case, was specified. But the actual conditions revealed much worse soil conditions, leading to an idle period while there was a redesign, and then a fix involving heavy steel pipe piles in place of the concrete piles. The contractor resorted to a TCM claim due to the difficulty in determining the incremental costs of re-excavating some footings, additional backfill, more form work and grading, with attendant labor and water pumping operations.

The court observed:

> The exact amount of additional work which plaintiff had to perform as a result of the foundation problem is difficult, if not impossible, to determine because of the nature of the corrective work which was being performed. The adverse weather conditions during the extended period in which the excavations remained open caused a myriad of problems. Additional trenching, form construction, and pumping of surface water became necessary. Re-excavation by hand was sometimes required. The extreme muddy conditions caused difficulties and slowed down performance. There is no precise formula by which these additional costs can be computed and segregated from those costs which plaintiff would have incurred if there had been no government-caused difficulties.[13]

Of course the *caveat* here is that *J.D. Hedin* is over 50 years old, so its continued vitality in the face of the interven-

ing advances in job cost accounting systems may be open to question. As one of the leading commentators has argued, "more sophisticated job cost accounting and scheduling systems" have made it "easier for the contractor to segregate damages," and more difficult for them to establish that it is "impossible or at least highly impracticable to determine losses on a segregated basis due to the nature of the circumstances."[14]

The Reasonableness of the Original Bid

The second element requires the claimant prove that its original bid was reasonable. This requirement prevents a claimant from "get[ting] the benefit of its own failure to anticipate that level of difficulty that a reasonable contractor should have expected."[15]

Is it sufficient to show that the prices submitted for all of the bids were in close proximity to one another? Conversely, if the claimant's bid was extremely low in comparison to the remaining bids, is its bid unreasonable on its face, or did all the other bidders get it wrong?

Bidding construction projects is an art. Most contractors jealously guard their bid estimate worksheets, strategies and methodologies from public (and hence their competition's) view. It would be dangerous to assume that this test can be satisfied by a mere comparison of tightly priced bids. The factors courts consider in determining if this element has been met are: testimony from the engineer who prepared the bid, including the engineer's experience and qualifications in preparing similar bids; the proximity of the bid prices to one another; the contractor's level of experience in obtaining and successfully completing similar projects; and clear and convincing proof (such as executed change orders) that additional work was required above and beyond the original specifications.

The Total Costs Incurred Must be Reasonable under the Circumstances

The third element requires the claimant show that its actual costs were reasonable and accurately recorded.[16] If, for example, the additional costs were simply overruns of anticipated costs that it would have otherwise had to absorb within its contract price, they are not recoverable. So while in one sense proofs covering the total costs incurred might be the least difficult part of the TCM test to satisfy, in another sense it may be the easiest to disprove. The claimant must demonstrate, with specificity, that the costs were reasonable in light of the required changes.

What happens when a claimant has refused to provide the back-up information evidencing the claimed costs? How can their reasonableness, in light of the required changes, be challenged? At that point the court must decide if it is willing to allow the claimant to back out those costs, as well as costs determined to be unreasonable, from the remainder of the claim, and allow it to proceed as a modified TCM case.

Such were the circumstances in *State Highway Comm'n v. Brasel & Sims Constr. Co.*[17] A one-year project became a two-year project as a result of the state highway department's failure to provide an adequate source of water and properly depict the soil quality of a gravel pit. The court stated that these two conditions "resulted in delays throughout the entire construction period, the cost of which would have been difficult, if not impossible, to calculate by any other method" than the TCM.[18] Consequently, it allowed the contractor to use an unsegregated damages' approach over a subgroup of work items:

> Brasel & Sims [the claimant] isolated the areas of the construction project affected by the breach and applied the total-cost method to calculate increased costs *with respect to each area*.[19] (Emphasis added)

Lack of Contractor Responsibility for the Claimed Additional Costs

Finally, a claimant is required to show that it was not the party responsible for the additional costs. As noted at the outset of this article, in order to fit within the four corners of the TCM test, a contractor may not recover where it is found responsible *for even a portion of the claimed damages*.[20] This follows from the general rule that "[w]here both parties contribute to the delay neither can recover damage[s], unless there is in the proof a clear apportionment of the delay and expense attributable to each party."[21]

The disqualifying responsibility is not limited to substantive issues (such as commission of a contributing cause), but includes the contractor's duty to maintain adequate records. In *Cavalier Clothes Inc. v. United States*, the court determined that the plaintiff's failure to retain records led to its inability to distinguish between delays attributable to its own actions and those allegedly attributable to the defendant and, thus, the plaintiff could not demonstrate its additional costs were due solely to the defendant's actions.[22] In other words, the claimant must demonstrate "a clear apportionment of the delay and expenses attributable" to the defendant as opposed to the other alleged causes of damages.[23] The failure to quantify damages (in a modified TCM approach) caused by a contractor's own conduct (*e.g.,* shutting down work due to a fatality on site) is fatal where the contractor concedes its responsibility for various added costs as a result of such conduct.[24]

But where a contractor puts forth its total costs by category, and they are attacked by the defendant in like fashion, a modified TCM approach has been upheld. In *Thalle Constr. Co. v. Whiting-Turner Contr. Co.*,[25] for instance, the district court examined the categories of damages asserted by the subcontractor against the prime contractor, deducted

those costs the subcontractor either conceded were its responsibility or found by the court to be chargeable to the subcontractor's errors, further deducted from the subcontractor disallowed or excessive items such as lost labor cost due to inclement weather, overstated idle equipment charges and paving materials' costs, and losses attributable to labor unrest and union difficulties, before arriving at a reduced total cost claim that was, in reality, a modified TCM damage award.

In sum, news of the TCM's and modified TCM's demise as viable methods for proving unsegregated damages in all construction cases is still premature. Resort to these methods will in all likelihood continue to wane, given the continued judicial scrutiny and their spotty success. Most importantly, however, advancements in construction cost accounting methods have already undercut one of the main tenets of the TCM theory of damages, further narrowing the basis for claiming impracticability. ⚖

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ENDNOTES

1. *Meva Corp. v. United States*, 206 Ct. Cl. 203, 511 F.2d 548 (1975).
2. *Servidone Constr. Corp. v. United States*, 931 F.2d 860, 861 (Fed. Cir. 1991).
3. *North Star Alaska Housing Corp. v. United States*, 20 76 Fed. Cl. 158, 213 (Fed. Cl. 2007) (*citing Propellex Corp. v. Brownlee*, 342 F.3d 1335, 1338-39 (Fed. Cir. 2003) (*quoting Dawco Constr. Inc. v. United States*, 930 F.2d 872, 882 (Fed. Cir. 1991), *overruled on other grounds by Reflectone v. Dalton*, 60 F.3d 1572 (Fed. Cir. 1995)).
4. ABA Model Jury Instructions: Construction Litigation, Second Edition, Sec. 18.01 (2015).
5. *Raytheon Co. v. White*, 305 F.3d 1354, 1365 (Fed. Cir.), *reh'g denied,* 2002 U.S. App. LEXIS 27409 (2002); *see also Sunshine Constr. & Engineering, Inc. v. United States*, 64 Fed. Cl. 346, 371 (2005).
6. Section 104.03.06 ("Unacceptable Cost Calculation Methods") of the 2007 NJDOT Standard Specifications for Road & Bridge Construction, provides in pertinent part:

   The Contractor has the burden of substantially proving entitlement to and quantifying its costs. The Department will not make payment for costs calculated using the following methods:

   1. Total Cost Method. Method based on calculating costs as the difference between the Contractor's bid for the Work from the Contractor's calculation of costs for the Work.
   2. Modified Total Cost Method. Method based on calculating damages as the difference between the Contractor's bid for a portion of the Work and the Contractor's calculation of cost for that portion of the Work.

   In comparison, Section 107.02 of the NJDOT Standard Specifications requires for all contractor claims, including delay claims, "the exact amount sought and a breakdown of that amount into the following categories:

   a. Direct Labor
   b. Direct Materials
   c. Job Overhead
   d. Overhead (General and Administrative)
   e. Subcontractor's Work
   f. Other categories as specified by the Contractor."
7. *But see, Lighting & Power Servs. V. Roberts*, 354 F. 3d 817 (8th Cir. 2004).
8. *See, for example, Transpower Constructors, Div. of Harrison Int'l Corp. v. Grand River Dam Authority*, 905 F.2d 1413, 1417, n.1 (10th Cir. 1990), where the jury was instructed: "[A] party need not prove the amount of his damages with mathematical exactness. It is sufficient if the party furnishes data from which the amount of damages can be established with reasonable certainty. You are instructed that a party has proven the amount of his damages with reasonable certainty if he has presented evidence which shows the amount of damages as a matter of just and reasonable inference."
9. *Bagwell Coatings, Inc. v. Middle South Energy, Inc.*, 797 F.2d 1298 (5th Cir. 1986); *Glasgow, Inc. v. Department of Transp.*, 529 A.2d 596 (Pa. Commw. 1982).
10. *Cavalier*, 51 Fed. Cl., at 419.
11. *See, AMEC Civ., LLC v. DMJM Harris, Inc.*, 2009 U.S. Dist. LEXIS 55410 (D.N.J. June 30, 2009).
12. 171 Ct. Cl. 70, 347 F.2d 235 (1965).
13. 171 Ct. Cl. 86-87, 347 F.2d at 248.
14. 6 Bruner & O'Connor on Construction Law § 19:93 (2002).
15. *Servidone Constr. Corp. v. United States*, 19 Cl. Ct. 346, 385-386 (1990), *aff'd*, 931 F.2d 860 (Fed. Cir. 1991).
16. *Servidone*, 931 F.2d at 861-62; *Cavalier*, 51 Fed. Cl., at 423.
17. 688 P.2d 871 (WY. Sup. Ct. 1984).
18. 688 P.2d, at 878.
19. *Id*.
20. *Net Constr., Inc. v. C&C Rehab & Constr., Inc.*, 256 F. Supp.2d 350 (E.D. Pa. 2003)(subcontractor alleged that the general contractor's mismanagement caused a lack of productivity, but admitted that the work had also been delayed by soil conditions, adverse weather, and its own work, but was unable to allocate a portion of its total extra costs to these factors).
21. *William F. Klingensmith v. United States*, 731 F.2d 805, 809 (Fed. Cir. 1984) (internal quotations and citations omitted). *Cavalier*, 51 Fed. Cl. at 424.
22. 51 Fed. Cl., at 424.
23. *Weeks Dredging & Contracting, Inc. v. United States*, 13 Cl. Ct. 193, 241 (1987) (*quoting Klingensmith*, 731 F.2d at 809).
24. AMEC Civ., LLC, 2009 U.S. Dist. LEXIS 55410 at 38-39.
25. 945 F. Supp. 652 (S.D.N.Y. 1996).