Settlement Procedures: Highway Contractors' Claims

DOWELL H. ANDERS, Chief Counsel, Office of the Chief Counsel, Federal Highway Administration

•IF you think I have a different perspective today on the settlement of highway contractors' claims than I did when I was Chief Attorney for the Arkansas State Highway Department, you are right. In the old days the engineers of the highway department would indulge me by discussing with me a few of the more difficult claims which they were trying to settle with the "hard-nosed" Bureau of Public Roads division engineer for Arkansas. Now that I am on the other side of the fence I am beginning to understand why the Bureau of Public Roads took its so-called "arbitrary" attitude on settlement of Federal-aid highway claims; and I hope at the end of my talk that you too will understand better some of our mutual problems.

The role of the Federal Highway Administration should be one, not of direct participation in state decisions affecting Federal-aid reimbursement, but rather one of review and either approval or disapproval of a state decision. However, I would like to stress throughout my discussion that the key to a successful Federal-state relationship is understanding and cooperation. The states and the Administration, as partners, must make every effort to understand the policies and laws under which the other must operate. Understanding is not concomitant with unreserved agreement that these are the best policies and laws. However, there must be compliance with the Federal law and the policies and requirements of the Administration if there is to be Federal participation in Federal-aid projects; and the Administration will certainly attempt to make its decisions compatible with the policies and laws of the state highway departments.

Since the Administration has a review authority with respect to state highway contractors' claims, I feel that my time would be spent most constructively by discussing what I feel is the state's responsibility in the resolution of construction claims. There is one clear premise from which we must proceed. We must recognize that an adjudication of claims by administrative findings by a state official (including a contracting officer), by a state contract appeals board, or by a state court may be conclusive under state law as to a dispute between the contractor and the state, with whom the contractor has privity, but it is not conclusive between the state and the Federal Highway Administration insofar as Federal-aid reimbursement is concerned. One further and basic reservation I would have to the Administration standing in the shoes of a state with regard to such adjudications, and one with which you certainly would not disagree, is that the Administration should not be liable for a claim which is attributable entirely to negligence or other culpable action on the part of the state personnel in administration of the contract.

The administration has authorized its division engineers and certain subordinate officials in the field to approve contracts for construction let by the states, to approve amendments thereto, and to concur in any change orders or other claim settlements by the states which involve additional performance and monetary obligations. In many cases, such an official, at his own discretion or pursuant to written instructions and policy and procedural memorandums, seeks the advice of the Regional Federal Highway Administrator and his staff; and the latter official may, in turn, request advice of the headquarters staff in Washington. These officials have a staff responsibility which must be maintained if the Administration is to perform its job properly.

Paper presented at the Sixth Annual Workshop on Highway Law, University of Wisconsin, July 24-27, 1967.

The "legal" problems which arise in a state highway department under road construction contracts seldom involve only legal questions; they invariably also involve factual data and engineering decisions. This is why we, in the General Counsel's office, receive the mixed questions of law and engineering through the same channels of division engineer, Regional Federal Highway Administrator and Office of Engineering and Operations in Washington. Then the respective offices may apply their engineering judgment and evaluation to the problems.

Now, as to how to settle claims, let me recommend our procedures with respect to direct Federal contracts. The greater number of claims arise under Federal construction projects as a result of changes made in the course of the work which entitle the contractor to an equitable dollar adjustment and/or an extension of time. Our large dollar claims arise under the changed conditions clause of the Government contract terms. Since our Government contract clauses permit equitable adjustment, we encourage our engineers on the project to try to reach a settlement with the contractor, incorporate it in a change order and obtain the contractor's agreement thereto.

Our experience has been that both the contractor and the Government are never in a better position to make a decision on a claim or to further explore the facts necessary for settlement than they are at the time the situation occurs which is the basis of the claim. However, human nature being what it is, when it comes to the matter of settling the dollar value of the change or the appropriate extension of time, we succumb too often to the temptation to let the contracting officer and the lawyers argue it out with the contractor after the job is completed.

We also have the more serious problem of oral directions by the engineer to change the work, which are not converted to written orders. These are recognized by the Federal appeal boards and courts as constructive changes for which the contractor is entitled to relief.

Sometimes a project engineer cannot obtain a settlement agreement from the contractor on a written change order. Or a contractor's claim may be in the nature of a changed condition which requires extensive development of geological information and the application of case law. In these instances, we ask our project engineers to refer the matter immediately through the division engineer to the Regional Federal Highway Administrator for engineering evaluation and then to my office for legal review. This insures that, while the work is still in progress and the facts are fresh in the minds of all parties, we can give the project engineer further advice and propose settlement terms. As a practical matter, we can also insure that the project engineer documents the claim adequately and obtains any data which are essential to settlement on the claim at a later date.

When the Federal project engineer and the contractor are in the middle of a construction project, during a limited construction season, there is a natural reluctance to do more than is really necessary with respect to claims which the contractor is not willing to resolve on the spot. We realize that cooperation and good relationships between the project engineer and the contractor and his work force must be maintained if the job is to be completed on time. However, the contractor must take the time to give notice of potential claims; the project engineer, as well as the contractor, must document those claims which cannot be settled by agreement or change order; and they must do it thoroughly enough so that there is no misconception as to the basis of claim at a later date.

I emphasize the need for solid documentation of unsettled claims. I find, in Federal claims work, that the primary reason for the inability to settle claims is the inability to reconstruct from the records kept, by both the project engineer and the contractor, the factual situation out of which the claim arose. This is why we must resort to extensive examination and cross-examination in appeals board proceedings. The mass of Federal case law that has grown up around construction contract claims is more than adequate to settle the claims. But the documentation must be equally adequate so that the parties can agree upon the basic facts of the claim. The same can undoubtedly be said of state claims.

If I had to develop an axiom at this point, it would be "A claim that is supported by clear and adequate documentation proceeds from strength." The measure of a state's

success on a particular claim for Federal reimbursement is necessarily the extent to which such claim is supported by adequate documentation. I would suggest that particular attention be given to the following categories of documentation of a construction claim:

1. The facts giving rise to a claim are most important. It has often been said that it is facts, to which legal principles can be applied which win law suits. We have received from some states claims for reimbursement, with a statement such as the following: "Since you are paying 95 percent of the bill and we are paying 5 percent, we would like your advice on whether we should pay this claim. The following facts appear to us to favor the position of the contractor." This naturally leaves us in some doubt as to what facts or law might favor the state in this claim. This is one reason why we like the claims reviewed by our division and regional engineering staff.

For every inadequately documented claim, we are fortunate in receiving many more which are accompanied by well-organized factual information, substantiated by correspondence, excerpts from diaries, photographs, pictorial diagrams, exhibits, and, finally, convincing argument and engineering evaluation encompassing the entire claim.

2. The legal basis for paying the claim. The engineer may make a very valid factual and engineering presentation for the settlement of a claim but if the proposed settlement is contrary to the law of the state in which the contract is made, the claim must fail. Therefore, you, as legal counsel, should be in on the ground floor in the development of the claim. We, in the Administration's Office of General Counsel, defer to your judgment, as State counsel, to know best what is the prevailing law of the state on a particular legal matter. Although we defer to your judgment, this does not mean that we succumb to it. We research the law you cite very carefully.

One of our most experienced private claims attorneys in Washington has this motto over his desk: "When all else fails, read the contract." What he is saying is that there are more solutions to be found in the contract provisions than the parties ever dreamed were there. And yet, it is surprising how many claims we receive from state highway departments which contain no reference whatever to specifications or to the contract provisions of the particular contract.

About a year ago we received a claim from a state highway department for work that had been performed on a project after completion of the work called for by the contract. The work had apparently been performed without the benefit of a change order or supplemental agreement by the parties and the only legal basis presented to us by the state for payment of the claim was a short excerpt from chapter 1 of Williston on Contracts to the effect that until a contract is fully performed it is executory and may be amended by the parties. State counsel was certainly safe in selecting chapter 1 of Williston because Mr. Williston does not begin hedging his legal principles until the later chapters. But we are still at a loss to understand what significance this legal principle has with respect to the claim presented—since the contract had not been amended. Lack of in-depth legal review is one of our many problems in the presentation by states of their claims, and we are understandably on the defensive. If you think this does not apply to you, I suggest you review carefully some of the claims which have been turned down by the Bureau of Public Roads in the past and then decide whether you could have presented a better legal position on behalf of your client—the state highway department.

3. Present an auditable claim. The great majority of claims are dollar claims and should, therefore, contain appropriate cost breakdowns from which state auditors, and in turn the Administration auditors, can audit the claim. Another problem is the basis on which claims are settled—total cost, costs related to contract unit prices, or opinions of experts ("jury verdict" basis). Therefore, the state highway department would be well advised to consult with Federal Highway Administration accountants to determine which cost principles would be most acceptable to them and to document the claim accordingly.

4. Argue from strength rather than weakness. Give us all the facts, all the law and all the figures necessary to support your claim but then argue from strength rather than weakness. I assure you we would like to be convinced that you are right. If you

want to be fully convincing you must substantiate everything you assert to the fullest extent possible, referencing specifications, contract provisions and the law of the State. Do not make statements which you cannot support. In short, if it is evident from your presentation that you are convinced of the validity of your claim, you will undoubtedly convince us also.

This is, in essence, all we ask of the states as a basis for determining their right to Federal reimbursement on most construction claims which they settle with contractors. I feel it would be unfair to the Federal Highway Administration for me to recommend any less than this. At the National Highway Claims Conference of the American Road Builders' Association in March 1967, I was pleased to hear John E. Harwood, Deputy Commissioner and Chief Engineer of the Virginia Department of Highways, take this same position with regard to the Federal-state relationship on claims; namely, that the state must assume the responsibility that it has under the contract with the contractor, and only the contractor, and render prompt decisions on and approvals of claims without regard to the possible position of the Bureau of Public Roads.

With respect to who is best qualified to document, present arguments and settle claims, we have found in the Federal program that this person is the engineer who is the contracting officer on Federal construction projects. We have no legal objection to a state administrative contract appeals board standing in the shoes of such a qualified state engineer or reviewing a decision made by him. The Federal Highway Administration would have an interest, of course, in the technical ability of members of such a board to understand and determine the engineering problems involved in the dispute. Again, we would expect the issues to be settled on the basis of the applicable contract provisions and specifications, state law, and such adequate documenation and cost analysis as would permit a detailed audit by our officials for purposes of Federal reimbursement. Similarly, an award made on the basis of a decision by a state court would have to be supported, in the record made before the court, by the applicable contract provisions and specifications, as well as by state law, since the reimbursement authority of the Federal Highway Administration is expressly limited under 23 USC 121 to those "costs of construction incurred by [the State] on a project... in accordance with the plans and specifications...."

In the past, the Bureau of Public Roads has been asked to participate in a state contractor's claim which was approved by the state legislature. The Comptroller General of the United States (9 Comp. Gen. 175, Oct. 30, 1929) has held that there is neither a legal nor an equitable obligation on the part of the United States to pay to a state a sum of money for its Federal-aid construction merely because the state legislature passed a bill in favor of the contractor and the supreme court of the state later upheld such action as an obligation on the state highway department to submit a claim to the United States.

While on the subject of claims, we should not overlook the preventive responsibility we, as lawyers, have to our respective organizations to assist them in avoiding claims. When a claim arises and we are asked to interpret a contract provision, how many times have we found that there is such ambiguity in the provision that the claim can only be resolved by court action? We can serve our clients best if we promptly revise, for future use, such an ambiguous provision and any related provisions in order to "write out" future claims of a similar nature.

In other instances, the claim may have arisen because of misinterpretation by the project engineer or because of his failure to properly administer the work under the contract. We are using the "newsletter" approach to bring to the attention of our field engineers on Federal projects not only these types of recurring claims but also our recommendations as to how they might have been avoided by proper project administration.

We have heard complaints from some state highway department attorneys that the Federal Highway Administration division engineers in their states were denying claims which they felt both had merit and would have received favorable consideration from officials at the regional or Washington headquarters level. My only answer to this is to keep "pushing the button" until you receive consideration of the claim at the level

desired. You must use your own discretion in what decisions to appeal. Your working relationships with our division engineers would not be greatly enhanced were you to appeal every one of his adverse decisions regardless of the merits of the decision.

In conclusion, let me emphasize that a good claim will always be a good claim, to whomever it is presented. Although the Federal Highway Administration has a veto or second-guessing authority over the states in the area of Federal reimbursement, this authority will be exercised in a reasonable way. Most of our problems can be resolved by more effective communication. A complete and thorough resolution of the state claim, well documented, founded in state law and applicable Federal law and regulations, has assurance of acceptance by the Administration.