

15-1 BCA P 35820 (Civilian B.C.A.), CBCA 3450, 2014 WL 7001508

CBCA

Civilian Board of Contract Appeals

KIEWIT-TURNER, A JOINT VENTURE, APPELLANT

v.

DEPARTMENT OF VETERANS AFFAIRS, RESPONDENT

Granted December 9, 2014

William E. Dorris, Chad V. Theriot, Reginald A. Williamson, and Damian M. Brychcy of Kilpatrick Townsend & Stockton LLP, Atlanta, GA; and Michael A. Branca of Peckar & Abramson, P.C., Washington, DC, counsel for Appellant. Charlma Quarles, Stacey North-Willis, Khaliah Wrenn, Benjamin Diliberto, and Eyvonne Mallett, Office of General Counsel, Department of Veterans Affairs, Washington, DC, counsel for Respondent.

Before Board Judges **DANIELS** (Chairman), **POLLACK**, and **STEEL** (presiding).
DANIELS, Board Judge.

In an earlier decision in this case, we held that the appellant, Kiewit-Turner, A Joint Venture (KT), may seek declaratory relief regarding the following three questions: (1) Did the contract modification known as SA-007 obligate the respondent, the Department of Veterans Affairs (VA), to provide a design that could be built for \$582,840,000? (2) Did the VA materially breach the contract by failing to provide a design that could be built for that amount of money? (3) If such a breach occurred, is KT entitled to stop work? *Kiewit-Turner, A Joint Venture v. Department of Veterans Affairs*, CBCA 3450, 14-1 BCA 35,705.

After hearing testimony for eight days, reviewing a voluminous documentary record, and considering lengthy briefs and reply briefs submitted by the parties, we now answer each of these questions in the affirmative.

On August 31, 2010, the VA awarded to KT a contract for the performance of preconstruction services on a medical center campus in Aurora, Colorado. The contract included an option for the performance of construction services as well. The contract was described as an “integrated design and construct,” or IDc, type contract - something similar to the “construction management at risk” or “construction management as constructor” types of contract used in the private sector.

Under an IDc contract, the construction contractor is brought into a project early, to analyze the design and give advice on the basis of which the owner can either direct its design team - with which it contracts separately - to make design changes, or alternatively, procure additional funds. James Lynn of Jacobs Engineering Group, Inc. (Jacobs), the VA's construction manager for this project, explained that “[t]he only way any kind of early contractor involvement type of approach works is if there's true collaboration and a level of trust built between the parties, the owner, architect and contractor.” The VA had never used this type of contract before. The agency's own project management plan recognized as a high risk that “IDc represents new contracting approach for VA; does not fit existing procedures which is complicated by VA culture that does not encourage or is [not] comfortable with new approaches.”

Indeed, the VA did not use the IDc mechanism properly right from the start. At the time KT was brought into the project, the design team - a joint venture team (JVT) consisting of Skidmore Owings & Merrill, S.A. Miro, Cator Ruma, and H+L Architects - had already been under contract since January 2006, and after a hiatus of nearly two years, had been at work since November 2007.¹ By August 2010, the design was already at the Design Development (DD) -1 stage (50% complete)² and funding decisions had been made. This limited the agency's flexibility to make modifications based on KT's pre-construction services advice. A September 2011 review by the Army Corps of Engineers, which was commissioned by the VA, confirmed that the IDc contract was not properly used: “[T]he IDc contract type may have not been appropriate for the Medical Center

Replacement in Denver.... [P]roceed[ing] with design development to major design milestones (DD1) prior to procurement of the IDc contractor ... did not permit the IDc contractor to integrate with the designer to achieve the benefits related to this contract type.... The current methodology appears to be counterintuitive to the Government's ability to achieve best value.”³

A key early VA funding decision was establishing a construction cost target, known as the estimated construction cost at award, or ECCA, at \$582,840,000. This ECCA was prescribed, on the same day as the KT contract was awarded, through a modification to the JVT's contract.

Notwithstanding the strictures imposed by the VA, KT devoted considerable manpower to pre-construction activities and submitted numerous reports to the agency. KT informed the VA at many stages that the design lacked coordination and completeness, that the design was over budget and included elements that were above the standard for a healthcare facility, and that value engineering (VE) was not being incorporated into the design.

The VA did not criticize KT's pre-construction work. To the contrary, both the VA's project executive for this project until June 2013 and agency counsel acknowledged at our hearing that the contractor fulfilled all of its pre-construction contractual requirements. The pre-construction services are not at issue in this case.

As early as October 2010, an independent advisor was cautioning the VA's project executive that the costs of the project, per the then-current design, were increasing. In November, the project executive's supervisor told him that “[the] DD1 packet is unsatisfactory and the JVT is not listening to the directions they are given from the user [side] or from the CFM [VA Office of Construction and Facilities Management] side.” In January 2011, KT estimated that the design would cost \$589 million to construct; the JVT essentially agreed, putting the figure at \$587 million. In April 2011, KT estimated that the design, which was then at the DD-2 stage (65% complete), would cost \$659 million to construct. This figure was \$76 million more than the ECCA. (KT later revised this estimate to \$664 million.) Although estimates of construction costs made by KT and the JVT were supposed to be reconciled at each stage of design, this KT estimate was not reconciled with the JVT's estimate.

Nevertheless, the VA asked KT to prepare a proposal for the optional work under its contract - constructing the medical facilities. In July 2011, the parties agreed that KT would submit a firm target price (FTP) proposal in the amount of \$603 million. On August 25, 2011, KT submitted such a proposal. The price was \$599.6 million for construction itself and \$3.4 million for all pre-construction activities, with a ceiling price of \$609 million. The FTP was based on a detailed analysis of DD-2 enhanced drawings. The proposal included many pages of general, technical, and pricing clarifications, which noted assumptions on which the proposal was based. We credit the testimony of KT's former managing partner that including these sorts of assumptions and qualifications in a proposal is typical in the commercial world for an IDc-type contract where the design is incomplete. The proposal assumed that the VA would ensure that the design include \$23 million of value engineering (VE) items and that KT would negotiate price reductions of nearly \$31 million from its subcontractors. KT's detailed FTP proposal became known as “The Book.”

By the time that KT submitted its proposal, the VA also had in hand an independent estimate prepared by Jacobs which showed that the cost of construction would be \$677,697,408.

Over the next two months, KT and the VA negotiated regarding KT's proposal, with KT frequently modifying pages of The Book to show agreed-upon changes. On October 4, KT submitted a revised Book. Negotiations continued, and by the end of October, only one item, an economic price adjustment clause proposed by KT, remained in dispute.

Mike Rossi of VCI, a company which had been engaged by the VA to advise it on early contractor involvement contracts, recommended to the VA that it not conclude a FTP until drawings were complete, since proposals at an earlier stage of design development would necessarily involve contingencies. The VA did not follow his suggestion, however. It scheduled a meeting for November 9, 2011, in an attempt to finalize a FTP. Participants included high-level representatives from KT and the VA, as

well as Mr. Lynn of Jacobs. Chris Kyrgos, the VA contracting officer's supervisor, traveled from Washington, D.C., to Denver for the meeting.

Mr. Kyrgos demanded that KT remove the clarifications, qualifications, and assumptions from The Book and present a proposal based on the most recent set of drawings.

KT responded that the clarifications, qualifications, and assumptions were necessary and reasonable given the state of the drawings on which the proposal was based. KT maintained, and the contracting officer agreed, that it would need several weeks to price the new drawings. KT's managing partner explained further that in light of the contractor's estimate that the current design would cost more than \$664 million to construct, KT could not possibly build the project for only \$603 million. KT and VA participants both testified that Mr. Kyrgos refused to consider negotiations based on The Book. The negotiations appeared to be at an impasse.

At this point, Mr. Lynn stepped forward to act as a mediator. He proposed that if the VA would agree to present a set of drawings that could be constructed for the ECCA, KT would agree to perform the construction work for the price it had offered. He then drafted a handwritten statement entitled ““Agreements - Path Forward.”” The three key paragraphs of this statement read:

1. All parties agree that they must get price to \$604 mil. They will each expend resources to keep that goal.
2. VA shall cause JVT to produce a design that meets their ECCA with use of alternates and other methods as a safety net.
3. Agreed: ... FTP set to \$604m[illion]/clg.[ceiling]@610.

The difference between the ECCA of \$582,840,000 and the FTP of \$604 million was that the latter included pre-construction and off-site infrastructure work, as well as other items, but the former did not.

The contracting officer and others signed the statement on behalf of the VA; the managing partner and another individual signed it on behalf of KT. Both parties understood that by making this agreement, the VA recognized that it would have to ensure that through the use of VE and other means, the JVT would produce a design which could be constructed for less than the current estimated cost of the project. KT's managing partner testified that “[t]he big caveat there is they have to produce a design that meets the ECCA because the current design didn't come anywhere close to that.” Mr. Lynn testified that including paragraph 2, regarding the ECCA, broke the impasse. The agreement did not reference any particular set of drawings; it contemplated that a future design would meet the ECCA.

Within two days after this Path Forward agreement was signed, KT sent to the contracting officer a new FTP proposal for construction work which was a mere page-and- a-half long. This proposal reiterated the contents of the agreement and did not reference any particular set of drawings or any part of The Book. A week later, KT's managing partner and the VA contracting officer agreed to modification SA-007 to the contract, exercising the agency's option to have KT perform construction work and establishing a FTP of \$604,087,179. Modification SA-007 included these paragraphs:

10. Both parties agree that they must achieve a goal to get the project price at or below \$604,087,179.00. Both parties agree to expend the necessary resources to keep the project goal.
11. The VA shall ensure the A/E (Joint Venture Team) will produce a design that meets their Estimated Construction Cost at Award (ECCA) with use of alternate and other methods as a safety net.

Like the handwritten agreement, but unlike documentation used in prior negotiations, SA-007 does not mention any particular set of drawings. Demonstrating that both parties understood this, in March 2012, KT's deputy managing partner and the VA contracting officer gave to personnel from both parties a presentation entitled “SA-007 and Managing to the \$604M.” The presentation asked, “Does SA-007 clearly define the scope of work?” and provided the answer, “No. Defines the box.” The VA adhered to this understating well into 2013. In January of that year, the facilitator of the “blue ocean” meeting (see below) wrote in her summary, “It was noted by the VA that the \$604 MM Firm Target Price agreement between the VA and KT was not based on any set of design documents.” In April, at a meeting with the JVT, Mr. Kyrgos stated that “only what is stated in the SA[-007] document itself has relevance [to the VA-KT contract]. Any previous document used in negotiations has no relevance or weight in this contract.”

On November 18, 2011 - the same day on which modification SA-007 was signed - the VA issued to KT a notice to proceed with the construction work. At that time, KT expected, based on communications from the VA, to receive 100% complete construction documents by the end of January 2012. In late 2011, however, the VA let lapse its architect/engineer peer review contract, and without a peer review, the agency would not release the 100% design package. The package was then projected to be delivered by April 2012. On April 5, 2012, KT told the VA that the “lack of this information is currently creating numerous negative impacts in material procurement/fabrications, obtaining approvals of submittals, coordination of trades, putting work in place in the field, as well as obstructing our ability to maintain the schedule as currently planned.”The next day, KT sent another letter, documenting the delay and its impact for each design package. KT followed this with yet another missive on May 8 on the same subject. While awaiting the 100% documents, KT proposed that it solicit subcontractor bids based on 95% drawings, but the VA rejected this request.

The 100% documents were finally delivered to KT on August 31, 2012. These documents turned out to be far from finished, however. An architect working for Jacobs estimated that the drawings were only 80% complete. The JVT later had to supplement them with an unusually large number of joint supplemental instructions (JSIs), some of which - including redesign of two parking garages and the energy center - were significant. The incomplete design, and changes to it, also prompted KT to issue an unusually large number of requests for information (RFIs), seeking clarification as to design elements. Responses to RFIs were often late and/or incomplete. The JSIs and RFIs further delayed procurement of subcontractor work. The VA had known about the incompleteness of the purported 100% design in June 2012, when the JVT had told the agency that more than 1400 design changes requested by the medical center would not be included in the August drawings.

KT planned to subcontract about 85% of the work on this project. All subcontracts valued at \$300,000 or more were required by the contract to be secured through a competitive process in which at least three bids were made. The subcontracting process required consent to each subcontract from the VA's contracting officer.

By the fall of 2012, according to witnesses from KT, the VA medical center, and a VA resident engineer on the project, prospective subcontractors were reluctant to submit bids for project work because subcontractors were not being timely paid for work they had performed. Sureties were also refusing to participate in the project due to the lack of timely payment to subcontractors. The VA's incomplete design, failure to process change orders from the spring of 2011 to the spring of 2012, failure to process JSIs in a timely fashion, and failure to make timely payment to KT were the cause of this predicament. Those firms that did bid on subcontracts increased their prices to account for the risk of not being paid timely, or even not being paid at all. A VA resident engineer wrote in December 2012, “The bad name of this project is on the street. No one wants to bid on this project.”At the same time, more buildings were being built in the Denver area, further depleting the number of firms interested in bidding on this project and increasing the amounts of the bids that were submitted.

A September 2011 project management plan prepared by the VA and Jacobs noted “project is over budget” as a risk. The plan stated, “Problem with scope and design management has caused budget overruns.”It said that this risk had a high probability and that “extensive VE” was required to reduce it. Compounding the problem, the plan said, was that the JVT did not recognize the problem's existence.

When the plan was updated in July 2012, the same problem was identified. Mr. Lynn explained that a principal contributor was the JVT's reluctance to participate in the VE process. By March 2013, in another iteration of the report, the VA expressed concern that the project might be \$200-300 million over budget.

Meanwhile, according to detailed estimates, the project's cost was increasing. A report of a weekly meeting in January 2012 showed that the project was considered at that time to be \$56.7 million over budget. In March 2012, KT cautioned the VA that the cost was trending above \$700 million. In April, Jacobs pegged that cost, based on the 95% drawings extant at the time, at \$712 million. KT thought the cost, based on those drawings, was \$717 million. The JVT, on the other hand, gave an estimate of \$607 million. Mr. Lynn told the VA project executive that “massive VE” would be required to bring the price down to that level,

and that “because JVT does not believe there is actually a budget issue, they are not fully cooperating with the VE process.” KT’s deputy managing partner explained to the VA project manager, in August, that the JVT’s cost estimates were unrealistically low because they were not based on market research or actual bids, and incorporated improper quantity estimates.

As subcontractor pricing became available, KT informed the VA that costs were increasing further. By December 2012, KT estimated the cost at nearly \$769 million, even if VE changes of \$50 million were incorporated into the design. A VA resident engineer told associates he believed the final cost would exceed \$800 million. In January 2013, Jacobs estimated, based on purported 100% drawings, that the cost would be \$784,963,063. (The VA did not inform KT of this estimate until much later.) In March, KT submitted to the VA a firm fixed price proposal, based primarily on competitive subcontractor bids, in the amount of \$897,584,831 (with clarifications and qualifications). The VA rejected this proposal, with the contracting officer stating that the agency “will continue to hold Kiewit-Turner responsible to the firm target price and ceiling price established in SA-007.” (The parties never agreed on a firm fixed price, as opposed to a firm target price, for KT’s work.) In June, KT told the VA that the cost could be as high as \$1.085 billion.

Like Jacobs, the JVT provided to the VA a cost estimate based on purported 100% drawings. This estimate was prepared by a subcontractor to the JVT, Rider Levett Bucknall (RLB), using parameters issued by the VA and under direction from the JVT. RLB’s lead estimator testified that he has no idea whether the criteria his firm used in making the estimate accurately reflected project conditions; creation of the estimate was merely an academic exercise. He stated that his firm was expressly told not to consider the impact of payment issues on subcontractor pricing. RLB estimated, given the constraints under which it was operating, that the project would cost \$645 million. In February 2014, it lowered the amount, after a review by the JVT, to \$630 million. The VA adopted this figure as the “independent government estimate.” Even at the amount of \$630 million, JVT members complained that the estimate was \$48 million over the ECCA and would cause the JVT to have to redesign the project to lower its cost.

At times, the VA did make efforts to cause the JVT to modify the design to meet the ECCA of \$582,840,000. In September 2011, the agency’s project executive and contracting officer issued a critical performance evaluation of the designer. They complained that the JVT had chosen form over function, placed an over-emphasis on aesthetics, had produced an unnecessarily complex design, did not believe that a budget problem existed, and was often uncooperative with the agency. In December 2011, the contracting officer denied the JVT’s request for release of retainage, “[d]ue to the ECCA above the contract stated limit and the complete design has not been accepted.” In March 2012, the contracting officer reminded the JVT that under its contract, when bids exceeded the estimated price, the JVT had to “perform such redesign and other services as are necessary to permit contract award within the funding limitation.” In May 2012, he wrote, “The Government will work with JVT to incorporate VE items that will bring the cost of the project back to the ECCA.” In January 2013, after receiving the Jacobs estimate based on purported 100% drawings, he told the JVT, “The current design ... exceeds the estimated cost of construction at award (ECCA) of \$582,840,000.00 by an estimated \$199,160,000.00 [T]he Government ... directs [the

JVT] to perform redesign and other services to provide a design within the funding limitations.” The contracting officer’s supervisor, Mr. Kyrgos, acknowledged to others in the VA, “[The JVT] appears to have misled the VA [i]n delivering a project way above the ‘design to cost.’”

At many other times, however, the VA acted in a contradictory fashion. In March 2013, after telling the JVT to redesign the project to the ECCA, the agency directed KT to proceed with construction based on the drawings current at that time. KT complained in response, “KT cannot construct a project within the bounds of the FTP if the design exceeds the ECCA by approximately \$199 million.... [B]y directing KT to construct the current 100% design that the VA recognizes is in need of a substantial redesign, the VA is quickly creating a massive funding issue on this project.” In a separate letter of the same date, KT asserted, “[T]he VA cannot direct KT to work beyond the current funding limitations. This means that the VA cannot direct KT to complete the project as reflected in the current 100% design unless and until additional funding is allotted and the FTP and ceiling prices are increased.” The contracting officer was unmoved; he responded, “[T]he Government is holding Kiewit-Turner responsible to the firm target price and ceiling price established in SA-007.”

According to all the estimates which were made, the cost of the project was at all times higher than both \$582,840,000 - the amount to which the VA in SA-007 committed to be the cost of construction - and \$604,087,179 - the amount to which both parties agreed in that contract modification would be the total project price for KT's services. The VA, Jacobs, and KT did expend significant amounts of resources, as required by SA-007, to try to reduce costs. After signing the modification, KT, realizing that the cost already exceeded these figures, brought on as many as thirty personnel specifically to work on VE efforts. The contractor enlisted some of its subcontractors to generate VE ideas as well. KT proposed many multi-million-dollar VE changes to modify the design so as to bring it within budget. Most of them were rejected by the VA. Often, however, even if a VE proposal was approved at all levels of the VA, the JVT refused to incorporate it into the design, and notwithstanding prodding by Jacobs, the VA did not press the JVT to take appropriate action.

In January 2013, immediately after receiving the Jacobs cost estimate of \$784,963,063, the VA brought together KT and the JVT to discuss how the project might be redesigned to be within budget. A VA executive explained that "the VA's intent [was] to focus on the JVT's obligation to deliver a design at or below the ECCA." The three-day meeting which ensued - called the "blue ocean" meeting - was devoted to brainstorming to develop cost-cutting ideas. More than seventy ideas, valued at over \$400 million, were advanced. The Jacobs subcontractor employee who facilitated the meeting considered that \$157 million of the suggestions could be classified as "easy/like acceptance" or "local approval only required." Personnel at the medical center reviewed the ideas and determined that over \$140 million were "acceptable" and an additional over \$100 million were "undesirable but will live with."

Mr. Lynn testified that despite his efforts to secure agency determinations on the blue ocean proposals, the VA would not make decisions on them. The agency tells us in its brief that it ultimately accepted only about \$10 million of the blue ocean ideas. Others were said to have been rejected on the grounds that they required waivers from federal mandates; violated VA energy, physical security or redundant system requirements; or proposed reductions of scope that would negatively impact patient care.

In April, VA headquarters executives became concerned about the agency's position on this project. One of them wrote to another, "We sent a letter to the [JVT] that the design was over the ECCA by \$199 million? Can we get a copy of that letter so we can see the context before we all go to the roof and jump[?]" Also in April, Mr. Kyrgos asked the JVT to "prepare an estimate based on 100% CDs [construction documents].... VA stated that this will become the IGE [[independent government estimate].... VA directed that the JVT estimate should not be influenced by actual amounts."

In May 2013, the contracting officer - without informing KT - directed the JVT "not to incorporate any of the changes included in the attached list into the Construction Documents." A month later, he wrote to the JVT, "Please do not proceed with any costcutting items from the January 2013 meeting." Also in June, the VA's director of cost estimating determined that the Jacobs estimate of nearly \$785 million should be rejected because Jacobs' failure to use actual known costs was a "fatal flaw" that undermined the reliability of the estimate. (The reason that Jacobs had not used actual known costs, however, was that the contracting officer had specifically directed the firm not to use them. The contracting officer did not disclose this fact to the cost estimating director.) And the contracting officer told KT that it must use pricing from The Book, the contents of which had been made irrelevant when SA-007 was agreed to, as the basis from which pricing change orders would be considered.

On April 30, 2013, KT requested a final decision from the contracting officer as to whether the VA had breached its obligation under the contract to provide a design that could be built for the ECCA of \$582,840,000 and whether KT consequently had the right to suspend work. The contracting officer issued a decision denying that the VA had breached the contract and directing KT to proceed with construction of the project. The agency has no plans to redesign the project. According to VA witnesses, the agency has approximately \$630 million appropriated for construction of the project. The agency has never sought additional funds for the project, and according to deposition testimony given by VA executives in April 2014, there were no plans at that time to ask for more money. A KT executive testified at our hearing in June 2014 that KT had already financed \$20 million worth of work for which it had not been paid and projected that this figure could reach \$100 million by December 2014.

We address below the three questions posed by KT.

(1) Did contract modification SA-007 obligate the VA to provide a design that could be built for \$582,840,000?

SA-007 could not be more clear: “The VA shall ensure the A/E (Joint Venture Team) will produce a design that meets their Estimated Construction Cost at Award (ECCA) with use of alternate and other methods as a safety net.” The ECCA was \$582,840,000 at the time that SA-007 was agreed to, and it remained at that number throughout the period discussed in this decision. Because the language is unambiguous on its face, its plain language dictates an affirmative answer to the question. *Coast Federal Bank, FSB v. United States*, 323 F.3d 1035, 1040-41 (Fed. Cir. 2003); *McAbee Construction, Inc. v. United States*, 97 F.3d 1431, 1435 (Fed. Cir. 1996). Use of the words “shall” and “ensure” demonstrates that the VA must make certain that the design will meet the ECCA. *Corey H. v. Board of Education of City of Chicago*, 995 F. Supp. 900, 913 (N.D. 111. 1998) (citing *Webster’s II New Riverside University Dictionary* 434 (1994)).

“Although extrinsic evidence may not be used to interpret an unambiguous contract provision, [the Court of Appeals for the Federal Circuit has] looked to it to confirm that the parties intended for the term to have its plain and ordinary meaning.” *TEG-Paradigm Environmental, Inc. v. United States*, 465 F.3d 1329, 1338 (Fed. Cir. 2006). The extrinsic evidence here confirms that the SA-007 paragraph regarding the ECCA means exactly what it says. The VA’s commitment to produce a design that could be built for the ECCA was the key to the parties’ agreement. During the critical negotiating session, before the contents of this paragraph were broached, the parties were at an impasse - the VA was insisting that the project as then designed be constructed for a specific price, and KT was adamant that unless it could condition its price or have an opportunity to assess costs in light of the then-current design, it would not commit to any price. The ECCA provision broke the impasse: the VA would have the JVT produce a design which could be built for the ECCA, and KT would perform the construction work for the FTP. Without the ECCA provision, KT would not have agreed to do its work for the FTP.

The VA recognized its obligation to require the JVT to produce such a design not only during the negotiations, but also for at least the next seventeen months. SA-007 was signed in November 2011. The next month, the contracting officer complained to the JVT that its design was in excess of the ECCA. Both then and throughout 2012, VA officials expressed concern that the design was over budget, with the budget figures being pegged to either the ECCA or the FTP. In May 2012, for example, the contracting officer wrote, “The Government will work with JVT to incorporate VE items that will bring the cost of the project back to the ECCA.” In January 2013, after the VA received the Jacobs estimate based on purported 100% drawings, the contracting officer told the JVT, “The current design ... exceeds the estimated cost of construction at award (ECCA) of \$582,840,000.00 by an estimated \$199,160,000.00.... [T]he Government ... directs [the JVT] to perform redesign and other services to provide a design within the funding limitations.” The agency then organized the “blue ocean” meeting for the purpose of bringing the design back into conformance with the ECCA. Not until much later, after a VA executive became alarmed by the contracting officer’s January 2013 letter, did the VA ever express a contrary position. This reversal has no bearing on our conclusion because “[i]t is only actions and interpretations before the controversy arises, conduct during performance, that are ‘highly relevant in determining what the parties intended.’” *Liles Construction Co. v. United States*, 455 F.2d 527, 538-39 (Ct. Cl. 1972) (quoting *Dynamics Corp. v. United States*, 389 F.2d 424, 430 (Ct. Cl. 1968)).

The VA now asserts in its brief that the mention of the ECCA in SA-007 “is not a material provision” and that “KT’s proposal of \$604 million for construction of the entire project had no relation to the ECCA.” The agency maintains that KT is obligated to perform construction work for the FTP, altered only by the cost of scope changes and adjustments to the profit percentage pursuant to a clause contained in SA-007. The ECCA provision, according to the VA, is inconsistent with the profit adjustment clause. Further, the VA says, the ECCA was occasionally referred to as \$604 million, rather than \$582 million, so it was not a concrete figure. The VA also leads its brief with a statement from an electronic mail message of a KT employee warning that if the contractor makes its initial FTP proposal, it will be “commit[ting] to something we cannot build” because price reductions of nearly \$31 million could not be achieved from subcontractors.

These contentions are not well taken. The mention of the ECCA in SA-007 is not just material to the agreement - it is critical to the agreement. SA-007 clearly links the ECCA and the FTP, providing that the latter is dependent on the former. Altering the contract price to account for scope changes is not possible, for reasons we discuss later in this opinion. There is no inconsistency between the ECCA provision and the profit adjustment clause; if the VA had produced a design which could be constructed for the ECCA, the profit adjustment clause could have been implemented in accordance with its terms. Even if the ECCA is considered to be \$604 million, rather than \$582 million, as suggested by the VA, that is inconsequential; the agency never came close to providing a design that could be constructed for either amount. Any concern by a KT employee about the contractor's initial FTP proposal was overcome by events: That proposal was not accepted; an entirely different bargain was agreed to by the parties in SA-007.

(2) Did the VA materially breach the contract by failing to provide a design that could be built for the ECCA of \$582,840,000?

As the Court of Appeals for the Federal Circuit has recognized, “Not every departure from the literal terms of a contract is sufficient to be deemed a material breach of a contract requirement.” *Stone Forest Industries, Inc. v. United States*, 973 F.2d 1548, 1550 (Fed. Cir. 1992). “A party breaches a contract when it is in material non-compliance with the terms of the contract.” *Gilbert v. Department of Justice*, 334 F.3d 1065, 1071 (Fed. Cir. 2003) “A breach is material when it relates to a matter of vital importance, or goes to the essence of the contract.” *Thomas v. Department of Housing & Urban Development*, 124 F.3d 1439, 1442 (Fed. Cir. 1997) (citing 5 Arthur L. Corbin, *Corbin on Contracts* § 1104 (1964)). “The standard of materiality for the purposes of deciding whether a contract was breached is necessarily imprecise and flexible. The determination depends on the nature and effect of the violation in light of how the particular contract was viewed, bargained for, entered into, and performed by the parties.” *Stone Forest*, 973 F.2d at 1550-51 (citing *Restatement (Second) of Contracts* § 241 cmts. a & b (quotation omitted)).

The Court and this Board have both considered the factors enunciated in section 241 of the *Restatement* when determining whether a breach is material. These factors are set out in *Lary v. United States Postal Service*, 472 F.3d 1363, 1367 (Fed. Cir. 2006), and *Kap-Sum Properties, LLC v. General Services Administration*, CBCA 2544, 13 BCA 35,446, at 173,832:

In determining whether a failure to render or to offer performance is material, the following circumstances are significant:

- (a) the extent to which the injured party will be deprived of the benefit which he reasonably expected;
- (b) the extent to which the injured party can be adequately compensated for the part of that benefit of which he will be deprived;
- (c) the extent to which the party failing to perform or to offer to perform will suffer forfeiture;
- (d) the likelihood that the party failing to perform or to offer to perform will cure his failure, taking account of all the circumstances including any reasonable assurances;
- (e) the extent to which the behavior of the party failing to perform or to offer to perform comports with standards of good faith and fair dealing.

The VA's breach of its contract with KT, by failing to provide a design which could be constructed for the ECCA, is of vital importance, as it goes to the essence of the agreement. The breach is material under each of the *Restatement* standards.

(a) KT has been deprived of the benefit of working with a design to which the project could be constructed for the ECCA. Both parties recognized that the design was not within the ECCA at the time that SA-007 was agreed to, and the cost estimates kept escalating as time passed. Much of the blame for this situation must be ascribed to the VA; by failing to control the JVT, delaying approval of the design, presenting KT with a design which was allegedly complete but required an enormous number of modifications, failing to process change orders for approximately one year, failing to process JSIs in a timely fashion, and failing to make timely payment to KT, the agency drove up the costs of construction. The VA occasionally complained to the JVT about excessive cost, but it failed to cause the JVT design team to take actions necessary to reduce that cost. Even after convening the “blue ocean” meeting to develop ideas for significant VE cost reductions, the VA implemented few of the

recommendations from the meeting and ultimately directed the JVT to abandon any efforts to include in the design many of the recommendations the agency's own staff had deemed reasonable.

(b) KT cannot be adequately compensated for the VA's failure to provide a design which could be constructed for the ECCA. As KT notes, the agency does not have sufficient funds to pay for construction of the entire project as currently designed and has no plans to ask for more money. Requiring KT to fund additional construction, without the prospect of full payment by the VA, would be manifestly unfair given the significant prospective cost. We also find that because the contract does not incorporate any particular set of drawings and specifications, determining the potential value of changes in scope is impossible. The VA's theory that the FTP stated in SA-007 was premised on the documents as they existed at the time that modification was signed is not valid. "[T]he language used in a contract to incorporate extrinsic material by reference must explicitly, or at least precisely, identify the written material being incorporated and must clearly communicate that the purpose of the reference is to incorporate the referenced material into the contract." *Northrop Grumman Information Technology, Inc. v. United States*, 535 F.3d 1339, 1345 (Fed. Cir. 2008). No documents were included in, attached to, or incorporated by reference in SA-007. The parties cannot determine the difference between the costs of construction under an initial set of plans and the costs under a final set because no initial set of plans is specified in the contract.

(c) While the VA may suffer some forfeiture from its material breach, we find the potential forfeiture to be limited because the agency will retain possession of the land and buildings on which construction has been taking place.

(d) There is little likelihood that the VA will cure its failure, given its insistence that it will neither redesign the project nor seek additional appropriated funds to complete it.

(e) "Every contract imposes upon each party a duty of good faith and fair dealing in its performance and enforcement. Failure to fulfill that duty constitutes a breach of contract, as does failure to fulfill a duty imposed by a promise stated in the agreement. [The Court of Appeals for the Federal Circuit has] long applied those principles to contracts with the federal government." *Metcalf Construction Co. v. United States*, 742 F.3d 984, 990 (Fed. Cir. 2014) (citations and quotations omitted). The duty of good faith and fair dealing requires the Government, as well as other parties to contracts, not only to avoid actions that unreasonably cause delay or hindrance to contract performance, but also to do whatever is necessary to enable the other party to perform. *C. Sanchez & Son, Inc. v. United States*, 6 F.3d 1539, 1542 (Fed. Cir. 1993); *Lewis-Nicholson, Inc. v. United States*, 550 F.2d 26, 32 (Ct. Cl. 1977). To show a violation of the duty of good faith and fair dealing, a party need not prove that the other party to a contract acted in bad faith. *Metcalf*, 742 F.3d at 993 (no specific-targeting requirement); *Sigma Services, Inc. v. Department of Housing & Urban Development*, CBCA 2704, 12-2 BCA 35,173, at 172,591 (citing *Rivera Agredano v. United States*, 70 Fed. Cl. 564, 574 n.8 (2006)).

Applying these principles, we find that the behavior of the VA has not comported with standards of good faith and fair dealing required by law. The agency failed to provide a design that could be constructed within the ECCA because it did not control its designer, the JVT. It paid no heed to VE suggestions for cost reductions which were made by KT and Jacobs (or even those which were accepted by the agency's own medical center personnel following the "blue ocean" meeting). The agency delayed progress of construction, such as by delaying the processing of design changes and change orders, as described under factor (a) above. The agency disregarded cost estimates by KT and Jacobs, even to the point of rejecting a Jacobs estimate because it was developed under restrictions which the agency itself had imposed. The agency adopted as an independent government estimate a document which was neither independent (it was developed by a subcontractor to the JVT, an entity which had a strong interest in the result), nor by the Government (it was by the JVT), nor an estimate (it was by admission of the chief estimator an academic exercise), and the number was so far below any previous estimate as to be of dubious accuracy. The agency did this notwithstanding the testimony of every witness who addressed the matter, including several VA witnesses, that an "independent" estimate should not be made by a party with a vested interest in the outcome. The agency ultimately directed KT to continue its construction work for the FTP, even though the agency refused to fund that work appropriately.

We do not know what the cost of construction of this project ultimately will be. It could be nearly \$769 million (as estimated by KT in December 2013), nearly \$785 million (as estimated by Jacobs in January 2013), more than \$897 million (KT's firm fixed price proposal in March 2013), or \$1.085 billion (KT's estimate in June 2013). It could even be only \$630 million (the JVT/RLB estimate in February 2014), although that appears unlikely because this number is so much lower than all the others presented. Whether it is any of these figures, however, it will be significantly in excess of the ECCA of \$582,840,000. We find that beyond doubt, the VA's breach of its contract with KT was material.

(3) Is KT entitled to stop work?

The Court of Appeals for the Federal Circuit has held that “[u]pon material breach of a contract the non-breaching party has the right to discontinue performance of the contract.”

Stone Forest, 973 F.2d at 1550; see also *Malone v. United States*, 849 F.2d 1441, 1446 (Fed. Cir. 1988) (holding that material breach by Government “provides Malone with a legal right to avoid the contract [and] discharges Malone's duty to perform”); *Kap-Sum Properties*, 13 BCA at 173,833 (citing *Malone*). The Court has explained further, “The choice of remedy is generally with the non-breaching party, and only in exceptional circumstances will equity require the non-breaching party to continue to perform the remainder of the contract.” *Stone Forest*, 973 F.2d at 1552. “[I]f a contract is not clearly divisible, in accordance with the intention of the parties, the breaching party can not require the non-breaching party to continue to perform what is left of the contract.” *Id.*

The VA draws our attention to *Northern Helex Co. v. United States*, 455 F.2d 546 (Ct. Cl. 1972), and *Cities Service Helex, Inc. v. United States*, 543 F.2d 1306 (Ct. Cl. 1976), two cases in which the Court of Claims held that if a contractor continues performance under a contract, without protest, notwithstanding the Government's breach, “the obligations of both parties remain in force and the injured party may retain only a claim for damages for partial breach.” *Cities Service*, 543 F.2d at 1313. The VA's analysis, however, ignores the phrase “without protest” which is part of the teaching of these decisions. The record is clear that KT has been proceeding with the construction (to avoid any possibility of being charged with being in default) under strenuous protest, including the very constructive advancement of VE proposals, throughout the post-SA-007 history of the project. The VA also notes that in its claim, KT asked for the opportunity to suspend performance, rather than to stop performance. Whatever the contractor requested initially is not important. As a matter of law, KT has the right to stop performance.

The appeal is **GRANTED**. As enunciated in this opinion, we afford Kiewit-Turner, A Joint Venture the declaratory relief it seeks.

STEPHEN M. DANIELS

Board Judge

We concur:

HOWARD A. POLLACK

Board Judge

CANDIDA S. STEEL

Board Judge

Footnotes

- 1 The design team was also referred to as “A/E” or “AE,” meaning architect/engineer.
- 2 The project consisted of numerous buildings, and the design (and later, the construction) proceeded more quickly on some buildings than others. Nevertheless, both during contract performance and in briefs, the parties refer to stages of design as if the process was unitary. We follow this practice in this opinion.
- 3 This was merely one instance of VA management problems on the project. The record is replete with instances in which the agency's on-site personnel - project executive, senior resident engineer, resident engineers, contracting officer, and project coordinator for the

medical center - lacked confidence in each other's abilities and respect for each other's actions. Jacobs' Mr. Lynn described this group, prior to a shake-up in June 2013, as the least effective and most dysfunctional staff on any project that he had ever seen.

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