

Contractor Recovers Some, but Owner Recovers
More on a Cost-Plus Contract

by

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The Missouri Court of Appeals for the Southern District recently affirmed a trial court's decision to award some money to the contractor (\$44,153.40) and far more money to the owner on its counterclaim (\$272,292.12). The case is *Matt Miller Company v. Taylor-Martin Holdings, LLC*, 2012 WL 5258713, decided October 25, 2012.

The appellate court determined that under the cost-plus contract in question the contractor could not include thirty percent to cover additional "burden costs" for such items as Social Security and Medicare. This is a significant ruling since many commercial and industrial projects involve cost-plus contracts.

The project was the renovation of a historic commercial building in Springfield, Missouri. The owner (Taylor-Martin Holdings) leased the building being renovated to Inspired Commerce, LLC as the tenant under a 33-year master lease agreement. The general contractor was Matt Miller Company.

The master lease agreement provided that tenant's failure to notify owner of any defective work within twelve months of possession would be "conclusive evidence against Tenant" that the building was in satisfactory condition.

During construction the general contractor was to remove bad mortar and retuck-point. Matt Miller Company failed to do this even though it charged owner \$56,225.01 for labor and another \$5,514.05 for materials for such tuck-pointing work.

Under a cost-plus contract the owner pays all contractually agreed contractor costs plus some additional agreed amount to cover overhead and profit.

This particular contract defined the reimbursable costs of the work as being "all costs of labor, all costs of materials, supplies, fixtures, equipment and appliances" and all other costs directly incurred for the project. This specifically included wages of workers directly employed to work on the project and wages and salaries of supervisors when stationed at the site.

The contract expressly excluded as a reimbursable cost any salary or other compensation of contractor's personnel other than those specifically set out as a reimbursable cost. These are typical definitions for what costs are and what costs are not to be paid by the owner.

At some point during construction the owner became concerned about the contractor's labor charge and near the end of the project requested an audit. Typically, cost-plus contracts include a provision allowing an owner to audit contractor charges to verify they are in compliance with the contractual meaning of what costs are reimbursable.

The contractor claimed at trial that it was entitled under this contract to recover a thirty percent "burden rate" for construction labor on top of the hourly rate it paid to its workers to cover Social Security, Medicare, unemployment, worker's compensation and payroll processing. The appellate court concluded that the contract did not allow for these additional charges.

At trial the owner testified that the absence of proper tuck-pointing would be costly to correct, in excess of \$311,000. Thus, the court allowed evidence on how much the lack of tuck-pointing reduced the overall value of this historic building. Missouri law provides that if the damage to property is small, then the cost to repair is the correct measure of damage.

If the cost to repair is large compared to the overall value of the building, then the correct measure of damage is the diminution in the value of the building, comparing the value of the building as built to what its value would have been if built pursuant to the contract.

The owner testified that the diminution in the value of the building due to the lack of tuck-pointing was \$450,000.

The contractor argued that the tenant did not complain to the owner within one year of occupancy that there were construction problems. Thus, under the master lease the owner waived any claim it had against the contractor for such defects.

The appellate court decided instead that the lease did not transfer all of the owner's property rights nor preclude the owner's claim for poor construction.

The contractor also argued that since it recovered \$44,153.40 on its mechanic's lien claim to compensate for substantial completion, it was the prevailing party and under the contract it should recover its attorney fees. The contract provided that if either party brought an action for breach then the contractor shall recover reasonable attorney fees.

Despite the seemingly one-sided wording of this attorney fee provision in favor of the contractor, the appellate court held that a party who is first to breach a

contract cannot then enforce the contract against the other non-breaching party. In this case the contractor had breached the contract by overcharging and not doing the tuck-pointing. Thus, it could not recover under the attorney fee provision.

In the end, the Southern District affirmed the award to owner of \$197,112.56 for the diminution in the value of the building and an additional \$75,179.33 for improper billing by contractor. After offsetting the contractor award, this left the owner with a net recovery of \$228,138.72.

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