United States Court of Appeals, Federal Circuit.

No. 99-1309.

CENTEX BATESON CONSTRUCTION CO.
Appellant,

v.

Togo D. WEST, Jr., Secretary of Veterans Affairs,
Appellee.

July 6, 2000.

Before **PLAGER, CLEVENGER**, and **SCHALL**, Circuit Judges.

DECISION

SCHALL, Circuit Judge.

*1 Centex Bateson Construction Co. ("Bateson") appeals the decision of the Department of Veterans Affairs Board of Contract Appeals ("Board") that denied claims for certain impact costs that were submitted by Bateson on behalf of its electrical subcontractor, Dynalectric Co. ("Dynalectric"), under Contract No. V 101C-1567 between Bateson and the Veterans Administration, the predecessor to the Department of Veteran[s] Affairs ("VA"). *Centex Bateson Constr. Co.*, VABCA Nos. 4613 and 5162-65, 99-1 B.C.A. (CCH) ¶ 30, 153 (Dec. 3, 1998) ("Centex II"). The Board held that "Supplemental Agreements" between Bateson and the VA resolved all of Bateson's claims for impact costs that were knowable at the time the agreements were executed. *See id.* at 149,255. The Board also held that Bateson had failed to meet its burden of establishing that it was entitled to recover those impact costs that were unknowable at the time of the Supplemental Agreements. *See id.* at 149,262. Because the Board did not err in holding that the Supplemental Agreements covered all impact costs that were knowable at the time of the agreements, and because the Board's holding that Bateson failed to prove its claim for unknowable costs is supported by substantial evidence, we affirm.

DISCUSSION

I.

Contract No. V101C-1567 was for the construction of the VA's Medical Center in Houston, Texas. Bateson was awarded the contract on May 29, 1987 for the fixed price of $172,690,000. Eventually, modifications to the contract through April of 1995 increased the contract price by $9,767,730.

Many of the contract modifications resulted from a system Bateson implemented to address requests for information ("RFIs") from its subcontractors relating to questions and problems encountered on the project. A RFI, which would identify, for a particular item of work, any anticipated costs above the contract price, would either be resolved by Bateson or forwarded to the VA for a response. The VA evaluated each RFI it received, and if it determined that additional costs could result from the matter that was the subject of the RFI, it would issue a request for proposal ("RFP") for the work or indicate one was forthcoming.

To respond to RFIs and corresponding RFPs, Bateson and the VA entered into Supplemental Agreements to the contract, each of which took the form of either a Field Supplemental Agreement ("FSA") or a Central Office Supplemental Agreement ("COSA"). Bateson then executed subcontract supplemental agreements with the affected subcontractor or subcontractors. The individual primarily involved in this process for Bateson was Bruce W. Lady, a Bateson Vice-President. Bateson and the VA began to execute Supplemental Agreements in early 1988. Each Supplemental Agreement included the following standard language:

> This Supplemental Agreement constitutes full and complete compensation
> due to the Contractor for all costs, direct and indirect, resulting from the modification set forth herein with the exception of the reservation listed
> below:
> *2 Reference J.W. Bateson Company, Inc. letter dated January 5, 1988, entitled "Reservation of Rights on Change Orders and the Senior Resident Engineer's letter, dated March 24, 1988, concerning same."

The January 5, 1988 letter from Bateson read as follows:

> It should be expressly understood that all Amendments/Modifications
>
> will be executed by J.W. Bateson Company, Inc. for full compensation for all money and time associated with the changed work, including

> all
> direct and indirect costs, but the contractor expressly reserves the right
>
> to seek additional time and compensation at a later date for impact or suspension of work.
>
> "Impact costs" shall be deemed to include, but not by way of limitation,
> extended home office overhead; extended jobsite overhead; idle labor; idle equipment; escalated labor, material, and equipment costs; loss of productivity; inefficiencies, dilution of supervision; stacking of trades; extended warehouse and other storage costs, and other time related costs recognized by boards and courts.

The second letter referenced in the Supplemental Agreements, the VA's response of March 24, 1988, stated:

> Your January 5, 1998 letter ... has been reviewed and found to be acceptable for incorporation in the mutually signed SF-30 supplemental agreements with the following understanding: The Veterans
> Administration does not necessarily agree with your definition/interpretation
> of "Impact Costs."
>
> The Veterans Administration's agreement to the language in your January 5, 1988 letter in no way waives the ten percent linutation on overhead related directly to supplemental work.
>
> We trust the above meets with your satisfaction and that this agreement will facilitate future execution of supplemental agreements.

II.

The claims at issue involve Bateson's electrical subcontractor, Dynalectric. Dynalectric initiated over 700 RFIs, submitting approximately one RFI for every $30,000 worth of electrical work. In most cases, in response to a Dynalectric RFI, the VA issued a RFP, which eventually was resolved through either a FSA or a COSA. The VA paid Bateson, for the benefit of Dynalectric, the amounts reflected in the FSAs and COSAs.

After the project was completed, Bateson submitted to the contracting officer, on behalf of Dynalectric, a claim for an equitable adjustment. Bateson asserted that Dynalectric was due $3,347,398 on account of labor inefficiencies and other impact costs arising from some 1,561 events-reflected in RFIs from Bateson to the VA and subsequent FSAs or COSAs-that changed the contract. The claim was denied by the contracting officer.

Bateson timely appealed the VA's denial of Dynalectric's claim to the Board. The Board grouped the 1,561 events at issue into 63 appeals and then consolidated the appeals into five separate groups for hearing purposes. The damages claimed in the five groups of appeals were separated into six specific categories of impact: Type A-Direct Labor Damages; Type B-Impact on Changed Work; Type C-Impact on Unchanged Work; Type D-Stop Impact; Type E-Unplanned Go-Back Impact; and Type F-Office Impact.

*3 The group of appeals that is before us, which is the first group to reach this court, consists of five appeals relating to some 104 events. Each of the five appeals alleged a different type of impact, as well as cumulative impact. The total amount claimed in this first group of appeals was $572,129. No Type A damages were claimed in this first group of appeals.

Both Bateson and the VA moved for partial summary judgment. Bateson claimed that, as a matter of law, the plans and specifications for certain contract tasks were defective. The VA responded that the plans and specification were not defective and that, in any event, the Supplement Agreements already had provided Bateson with the additional compensation it was seeking. The Board denied both motions, holding that material facts were in dispute. *See* ***Centex Bateson Constr. Co.,*** VABCA Nos. 4613, and 5162-65, 97-1 B.C.A. (CCH) ¶28,915 at 144, 148 (Apr. 16, 1997) ("Centex I").

In due course, the Board held a seventeen-day hearing, which was followed by post hearing briefing. Thereafter, in its decision, the Board held that the claims at issue (under categories B, D, E, and F) were barred by Supplemental Agreements. *See* ***Centex II***, 99-1 B.C.A. (CCH) ¶30,153 at 149,253-57. The Board focused on whether the claims at issue survived the pertinent Supplemental Agreements, i.e., whether the Supplemental Agreements served as accords and satisfactions for the Dynalectric claims. *See id*. at 149,253-54. The Board concluded that the only costs that survived the Supplemental Agreements were those costs that were reserved by Bateson and the VA. *See id.* at 149,254. Based upon the Supplemental Agreements and the two letters that were incorporated into them, the Board determined that the meaning of the term "impact costs" was

unclear and that, consequently, the Supplemental Agreements were ambiguous on the question of what matters were "reserved," or excluded, from their coverage. See id.

Turning to extrinsic evidence, the Board determined that "impact costs," the costs Bateson claimed it reserved for Dynalectric for later determination, included only those costs "unknowable" to Bateson at the time of the Supplemental Agreements. *See id.* at 149,254-55. The Board then determined that the costs asserted in claim categories B, D, E, and F either were known or should have been known at the time of the Supplemental Agreements, and that Dynalectric already had been compensated for these costs via Supplemental Agreements. *See id.* at 149,255-57. With regard to costs claimed under category C (impact on unchanged work), the Board determined that these costs were unknowable at the time of the Supplemental Agreements, but that Bateson had failed to prove that the VA was liable for them. *See id.* 149,255-62. Bateson's appeal was, therefore, denied by the Board. *See id*. at 149,262. Bateson, on behalf of Dynalectric, appeals. We have jurisdiction pursuant to 28 U.S.C. § 1295(a)(10).

III.

*4 Contract interpretations is a question of law. *See* ***Grumman Data Sys. Corp. v. Dalton,*** 88 F.3d 990, 997 (Fed.Cir.1996). Whether a contract term is ambiguous also is a question of law. *See id*. We review questions of law such as these without deference to the Board's decision. *See* ***Fortec Constrs. v. United States,*** 760 F.2d 1288, 1291 (Fed.Cir.1985). The parties' intent in entering into a contract is a question of fact. *See* ***Dureiko v. United States,*** 209 F.3d 1345, 1356 (Fed.Cir.2000). A Board decision on a fact issue cannot be set aside unless it "is fraudulent, or arbitrary, or capricious, or so grossly erroneous as to necessarily imply bad faith, or if such decision is not supported by substantial evidence." 41 U.S. C. § 609(b).

Bateson's January 5, 1988 letter, incorporated into the Supplemental Agreements, expressed Bateson's understanding that all Supplemental Agreements to the contract were "for full compensation for all money and time associated with the changed work, including all direct and indirect costs." However, as seen, Bateson "expressly reserve[d] the right to seek additional time and compensation at a later date for impact or suspension of work," a reservation to which the VA agreed in its March 24, 1988 letter, but with some qualification. The parties' dispute grows out of this qualification. Bateson claims that all of the costs at issue in this appeal are "impact costs" and that its January 5 letter explicitly identified and reserved those costs, whether or not they were

"knowable" at the time of the Supplemental Agreements. According to Bateson, since it reserved "impact costs" from being covered by the Supplemental Agreements, it is entitled to claim and recover such costs. Citing its March 24 letter, the VA responds that it never agreed to Bateson's proposed definition of "impact costs" and that the meaning of "impact costs" is ambiguous. With this ambiguity, the VA contends, extrinsic evidence should be examined, which, the VA asserts, indicates that only "unknowable" costs were reserved by Bateson.

In interpreting a written agreement, we first must determine whether the document at issue clearly embodies the understanding between the parties. *See* ***Harris v. Department of Veteran Affairs,*** 142 F.3d 1463, 1468 (Fed.Cir.1998). Bateson defined "impact costs" in its January 5, 1988 letter, which was incorporated into the Supplemental Agreements. The VA responded on March 24, 1988, noting that it had "reviewed and found [Bateson's letter] acceptable for incorporation in" the Supplemental Agreements. The VA, however, qualified its acceptance. In the second paragraph of its letter, the VA stated that it did "not necessarily agree with [Bateson's] definition/interpretation of 'Impact Costs."' In the next paragraph, the VA indicated that its "agreement to the language in Bateson's] January 5, 1988 letter in no way waives the ten percent limitation on overhead related directly to supplemental work." The VA concluded its letter with the hope that its response "meets with [Bateson's] satisfaction and that this agreement will facilitate future execution of supplemental agreements." Thereafter, Bateson and the VA entered into Supplemental Agreements that incorporated the exchange between the parties that is reflected in the January 5 and March 24 letters.

*5 Bateson argues that the VA, in response to Bateson's letter, agreed with Bateson's definition of "impact costs" with only one reservation-that overhead costs be capped at 10%. We do not agree. Contrary to Bateson's assertion, the VA's disagreement went beyond capping overhead costs. The VA expressed two separate concerns in two separate paragraphs in its March 24 letter. First, the VA noted its general disagreement with Bateson's definition of "impact costs." Next, in a separate paragraph, the VA specifically stated that it would not waive the 10% cap on overhead costs. The language of the VA's letter does not support the assertion that the VA agreed with Bateson's definition of "impact costs," with its only reservation being a 10% cap on overhead costs. Although the January 5 and March 24 letters reflect an understanding between Bateson and the VA that some costs were to be excluded from the coverage of the Supplemental Agreements, the letters do not explain the nature of those costs. That is because the letters provide no clear meaning for the critical term "impact costs." "Impact costs,"

when looking solely at Bateson's letter and the VA's response, can have multiple interpretations. Therefore, the term "impact costs" is ambiguous. *See* ***Massie v. United States,*** 166 F. 3d 1184, 1189 (Fed. Cir.1999) (noting that if a term is susceptible to more than one reasonable interpretation, then the term is ambiguous).

"If there is an ambiguity in the formation of the agreement or during its performance, we implement the intent of the parties at the time the agreement was struck." ***Harris,*** 142 F.3d at 1467. We turn to extrinsic evidence to determine the parties' intent and the meaning of an ambiguous term. *See* ***McAbee Constr., Inc. v. United States,*** 97 F.3d 1431, 1434-35 (Fed.Cir.1996). The meaning of a contract term is determined by interpreting the contract the way a reasonable person, familiar with all the facts and circumstances surrounding the contract's formation, would interpret it. *See* ***Hol-Gar Mfg. Corp. v. United States,*** 351 F.2d 972, 975 (Ct.C1.1965). We conclude that the Board correctly held that it was the intent of the parties that each Supplemental Agreement cover all "knowable" costs at the time of its formation and that each Supplemental Agreement reserve to Bateson the right to recover all "unknowable" costs. It is these "unknowable" costs that are the costs, including "impact costs," reserved in the Supplemental Agreements.

The Board's determination of the parties' intent is supported by substantial evidence. According to Bateson, it is entitled to the costs it defined as "impact costs" in its January 5 letter-extended jobsite overhead, idle labor, escalated labor, loss of productivity, inefficiencies, dilution of supervision, and stacking of trades. The Board's finding that the parties intended for only "unknowable" costs-of whatever kind-to be reserved, however, is supported by the fact that a Supplemental Agreement was often executed after work covered by the agreement had been completed. Thus, most direct and indirect costs, which were knowable at the time of contract formation, could be included in the Supplemental Agreements. [FN 1] Further, Mr. Lady testified before the Board that Bateson reserved "impact costs" because it was "impossible, particularly with the complexity of a hospital ... to determine the total impact of things as they're happening." In our view, "unknowable" costs are costs that are impossible or too complex to determine-the type of costs that concerned Mr. Lady and Bateson.

> FN 1. For example, the Board found that many of the FSAs and COSAs at issue included pricing that reflected changes in the labor pricing methodology earlier accepted by the VA.*See* ***Centex II,*** 99-1 B.C. A. (CCH) ¶30,153 at 149,254-55. Thus,

> any labor cost changes of which Bateson and Dynalectric had knowledge could be, and in most cases were, included in the Supplemental Agreements.

*6 Moreover, if Bateson or Dynalectric knew, or should have known, of particular costs at the time of a Supplemental Agreement, the VA could reasonably conclude that the Supplemental Agreement would include such costs. Both Bateson's and the VA's clear intent was to make the Supplemental Agreements binding equitable adjustments for the contract changes the agreements covered. Bateson's assertion that the parties agreed to allow certain costs, even if they were "knowable," to be claimed at a later date runs contrary to this clear intent. If Bateson were able to reprise a Supplemental Agreement based on information available at the time of the agreement's initial pricing, the Supplemental Agreement's purpose to render a degree of finality to the parties' resolution of the contract change embodied in the agreement would be rendered meaningless. Put simply, it was reasonable for the VA to conclude that a Supplemental Agreement would resolve all costs that Bateson and Dynalectric could determine at that time for the particular event at issue. In sum, we see no error in the Board's interpretation of the term "impact costs" and the scope of costs covered by the Supplemental Agreements.

Bateson argues that only the VA's subjective intent supports this interpretation. However, Bateson's intent also supports the Board's conclusion, considering that Mr. Lady's testimony was to the effect that Bateson was concerned with reserving costs that were impossible to determine ("unknowable" costs). The objective intent of the parties, i.e., how a reasonable person, in light of surrounding facts and circumstances, would interpret the contract, also supports the Board's conclusion. It does not appear reasonable to us that the VA would agree to allow a contractor to adjust its costs in a Supplemental Agreement, and then allow the costs to be adjusted again at a later date to include costs that were knowable at the time the Supplemental Agreement was executed. Under these circumstances, where Supplemental Agreements were being made to cover contract changes, no **reasonable person would believe that** a contractor could choose to leave out, and later claim, direct or indirect costs that were within that contractor's power to determine at the time of the formation of the Supplemental Agreements.

Bateson's final argument is that the elements required to establish an accord and satisfaction are not present. Again, we do not agree. As noted above, the Supplemental Agreements, interpreted in light of the parties' intent, cover all costs knowable to the parties at the time of their formation. *See* ***Edward R.***

Marden Corp. v. United States, 803 F.2d 701, 705 (Fed.Cir.1986) (noting that "the cardinal rule of contract construction [is] that the joint intent of the parties is dominant if it can be ascertained"). Additionally, each Supplemental Agreement amounted to a "mutual agreement between the parties in which one pays or performs and the other accepts payment or performance in satisfaction of a claim or demand which is a bona fide dispute." ' ***Brock & Blevins Co. v. United States,*** 343 F.2d 951, 955 (Ct.C1.1965) (quoting ***Nevada Half Moon Mining Co. v. Combined Metals Reduction Co.,*** 176 F.2d 73, 76 (10th Cir.1949)). Bateson would, on behalf of Dynalectric, notify the VA through RFIs, of any changes and additional costs encountered, creating, de facto, a bona fide dispute. The VA would respond to these RFIs, and a Supplemental Agreement would provide compensation in exchange for the additional work, thus extinguishing any claim as to a cost of the contract change that was covered by the Supplemental Agreement. The requirements for accord and satisfaction were met.

*7 With the Supplemental Agreements covering all knowable costs, the Board correctly determined that Bateson had already been compensated for the costs in categories B, D, E, and F. The Board's determination that all of these costs were knowable at the time the Supplemental Agreements were formed is supported by substantial evidence. Thus, the costs in categories B, D, E, and F claims were properly determined to be barred by the Supplemental Agreements. Finally, the Board's conclusion that category C costs, although unknowable at the time of the formation of the Supplemental Agreements, were not caused by any contract changes is supported by substantial evidence.

For the foregoing reasons, the decision of the Board denying Bateson's appeal is affirmed.

Each party shall bear its own costs.

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