



# Legal Brief

by Timothy J. Woolford, Esquire

## The basics of delay claims for home office overhead using the Eichleay Formula

*Home office overhead claims are often misunderstood*

Many construction projects are not completed on time for a variety of reasons. When a delay occurs, there are almost always financial consequences. Frequently, contractors and subcontractors assert claims for additional costs as a result of the delayed completion or extended performance period. One common component of such claims is a request for home office overhead damages. This claim is often misunderstood, and issues sometimes arise concerning the contractor's entitlement to these costs.

When a contractor submits a bid, it usually includes a value for both job site overhead as well as home office overhead. When a contractor maintains a home office, it expects to recover the cost of the home office through its general overhead and profit on the various projects. Home office overhead includes all of the costs needed to operate the business such as the mortgage payments or rent, utilities, salaries of management and clerical personnel, phones, computers, copy machines, taxes, insurance, automobiles, trade licenses, fees and the like.

When a project is delayed, it often prevents the contractor from accepting other

work. As a result, home office overhead is spread across fewer projects and diminishes the contractor's ability to recover that overhead, thus lowering profitability. For example, if a contractor expects to bid five projects for \$1 million each and includes \$40,000 in each bid to cover home office overhead, the contractor expects to recover \$200,000 across these five projects. If

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delays on a project prevent the contractor from performing one of the five projects, it loses the ability to recover \$40,000 in home office overhead. The delayed project is now forced to absorb more home office overhead than it was estimated to absorb.

By far, the most prevalent method for cal-

culating these damages is through the Eichleay formula, an imperfect mathematical calculation which attempts to equitably determine allocation of unabsorbed home office overhead to allow fair compensation for owner-caused delay. The Eichleay formula creates a daily, or per diem, rate for overhead costs attributable to a single project, multiplying the rate by the number of days of delay to arrive at a total home office overhead claim.

In order to recover using the Eichleay formula, a contractor must prove three elements:

- 1) an owner-caused delay extended the contract completion date;
- 2) the contractor was required to be "on standby" for an uncertain period of time; and
- 3) the contractor was unable to take on replacement or substitute work during the delay.

The most difficult element to satisfy is the second – proving that the contractor was

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on standby. Most courts have required the contractor to prove that work was actually suspended for an uncertain period of time and that the contractor was forced to be on standby, meaning that it could be ordered to return to work at a moment's notice. Often, this element cannot be satisfied because, although there was a delay, work was never actually halted or suspended altogether.

In one recent case involving a federal project for the Air Force, the court denied a home office overhead claim under the Eichleay formula because, although the government had issued a written order suspending the work for an indefinite duration, the order was silent as to whether the contractor was required to return to work at a moment's notice. Other courts


have been somewhat less rigid and have allowed recovery if the contractor proves there was a delay of indefinite duration during which it could not bill substantial amounts of work and at the end of which it was required to be able to return to work immediately at full speed.

While the Eichleay formula has been expressly adopted in the federal court system, it has yet to be either adopted or rejected by Pennsylvania courts. However, it has been accepted by the Pennsylvania Board of Claims, an administrative court that hears contractor claims against various state agencies, including DGS, the State System of Higher Education and PennDOT.

Unless a Pennsylvania appellate court rules that the Eichleay formula cannot be used, it is likely to remain the most

prevalent method for calculating home office overhead. As a result, all contractors and subcontractors should familiarize themselves with it.

This is particularly true because, when a large project is delayed for a significant period of time, the unabsorbed home office overhead damages can be substantial.

There are other methods of calculating this loss, but the Eichleay formula is the most prominent. While not perfect, the formula does provide a reasonable method to measure a very real, but difficult-to-establish, loss caused by project delay. If you are considering the submission of a claim using this formula, it is recommended that you consult with counsel to make sure the claim is well-supported and accurate. 

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