CLAIMS FOR HEAD OFFICE OVERHEADS AND PROFIT

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Claims for lost contributions towards head office overheads, and the loss of opportunity to earn profit, are commonplace in the construction industry when a Contractor has experienced an Employer delay event.

Whilst head office overhead contributions are generally recoverable through contract mechanisms, loss of profit is ordinarily framed as damages for breach of contract.

This article considers claims for head office overheads and loss of profit following the decision in Fluor v Shanghai Zhenhua Heavy Industry Co. Ltd (formerly known as Shanghai Zhenhua Port Machinery Co. Ltd - hereafter referred to as “SPMC”).

Fluor was engaged as the main contractor on the Greater Gabbard Offshore Wind Farm, and ZPMC manufactured and supplied the monopiles and transition pieces to Fluor.

In January 2018, Mr Justice Edwards-Stuart gave judgement on the quantum issues, following his earlier decisions on liability, as part of a long-running dispute between the parties.

Amongst the numerous quantum issues presented, the January 2018 decision considered “the correct approach to the recovery of ancillary costs such as head office overheads?” but does not conclude the amount due for overhead and profit. Fluor was directed to advance further submissions in support of this head of claim, and this latest judgement was decided in March 2018.

SOCIETY OF CONSTRUCTION LAW DELAY AND DISRUPTION PROTOCOL 2ND EDITION

The SCL Delay and Disruption Protocol makes clear that a Contractor should aim to keep detailed records of the head office overheads that it has not recovered, as well as the profits it has not earned.

As a secondary position, and where records cannot be, or haven’t been, kept, the SCL Delay and Disruption

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i [2018] EWHC 490 (TCC)
ii [2018] EWHC 1 (TCC)
iii [2018] EWHC 1 (TCC), Paragraph 30
Protocol endorses the use of either the Emden or Eichleay formulae to calculate the likely sums due.

WALTER LILLY V MACKAY

A helpful starting point relating to the recovery of head office overheads and profit was at paragraph 543 of Walter Lilly v Mackay\(^iv\); Mr Justice Akenhead concluded that:

a) A contractor can recover head office overheads and profit lost as a result of delay on a construction project;

b) The contractor must prove it would have won projects which would have returned a profit and/or contribution to head office overhead costs;

c) Formulae (such as Emden) are a legitimate and helpful method / approach to ascertain head office overheads and profit; and,

d) Ascertainment does not have to be absolute (i.e., some level of ‘assessment’ is permissible).

FLUOR V ZPMC

Fluor accepted that it could not claim profit, but advanced a claim for overheads at a rate of 4%, which was calculated as follows:

\[
\frac{\£374.735m \text{ (Project Cost for 2009)}}{\£657.000m \text{ (Company Turnover for 2009)}} = 57\%
\]

Total overheads for 2009 (\£22.184m) \times 57\% = \£12.645m

Add allowance for specific overheads of \£1.341m = \£13.986m

\[
\frac{\£13.986m \text{ (Proportion of overheads for 2009)}}{\£374.735m \text{ (Project Cost for 2009)}} = \text{c.}4\%
\]

Mr Justice Edwards-Stuart appears to be at odds with Mr Justice Akenhead’s approval of the use of formulae in Walter Lilly v Mackay and rejected Fluor’s claim, stating that he was “not prepared to pluck a figure out of the air”.

Although Fluor did not advance such a case, Mr Justice Edwards-Stuart added an additional strand to the recovery of non-project specific costs and determined that a contractor could claim for the thickening of head office overheads.

\(^iv\) [2012] EWHC 1773 (TCC)
RECORDS, RECORDS, RECORDS

Once again, this case highlights the importance of keeping detailed, contemporaneous and accurate records, including:

- A list of tenders won, lost and rejected;
- A list of profit margins achieved on individual projects;
- Records of overhead costs split into:
  - ‘Dedicated overhead’ costs which are incurred as a result of the Employer delay event; and,
  - ‘Unabsorbed overhead’ costs which are incurred regardless of the quantity of work carried out.

If you would like to engage DGA to assist your business with the calculation of losses discussed in this article, please contact your nearest office.
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