



STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS

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Ms. Beverly E. Najarian
Director
Department of Administration
One Capitol Hill
Providence, RI 02908


Re: Confidential Attorney Client Work Product
Report on the Barrington River Bridge Settlement

Dear Director Najarian:

Please find enclosed the above captioned report for your consideration and review. The report was prepared by the following individuals at the Department of Administration: Brian P. Stern, Esq., Executive Director, Louis A. DeQuattro, Jr., Esq., CPA, Chief Legal Counsel, Michael Mitchell, Esq., Deputy Chief Legal Counsel, and Everett C. Sammartino, Jr., Esq., Internal Audit Manager.

Please let me or Brian Stern know if you have any questions or concerns.

Sincerely,


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**REPORT ON THE BARRINGTON RIVER BRIDGE SETTLEMENT
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I. Introduction

This report documents the circumstances surrounding the proposed settlement to resolve the two claims submitted by Shire Corporation ("Shire") against the Rhode Island Department of Transportation (the "RIDOT") in connection with the following construction project: RI Contact # 2003-CB-045/ Federal Aid Project No. BRO-0123 (004)/ Replacement of Barrington River Bridge No. 123 (the "Project").

From the time the Barrington Bridge project was awarded to Shire in 2003 there have been a series of issues and delays that need to be addressed to allow this project to be completed. During the past three years Shire, the RIDOT, the Rhode Island Department of Administration (the "DOA") and the United States Federal Highway Administration (the "FHWA") have been investigating these issues and delays. In the past eighteen months, as a result of the settlement of the claims surrounding the Point Street Bridge claim, the bonding company for Shire Corporation has also become involved in the discussions surrounding these issues and claims.

Shire has made a detailed submission to the RIDOT detailing the basis for its claims. RIDOT has reviewed these claims with the assistance of the consulting firm and DOA has conducted an independent review of the issues and claims. After the RIDOT and DOA reviewed their internal findings it was then determined by the DOA and the RIDOT, with notice to the FHWA, that the claim reports and documents would be submitted to legal counsel to report on any legal claims or potential exposure and negotiate a settlement with counsel for Shire and the Bonding company. The FHWA agreed to attend these meeting(s) to observe but made no commitment to fund any settlement agreed to by the parties.

II. Description of the Project and Claims

(i) The Project

The Barrington Bridge construction project consists of two phases. Phase I is the construction of a new bridge from the intersection of Rt 114 and Matthewson Road to the

REPORT ON THE BARRINGTON RIVER BRIDGE SETTLEMENT
CONFIDENTIAL ATTORNEY CLIENT WORK PRODUCT

intersection of Rt. 114 and New Meadow Road in the Town of Barrington. Phase II consists of the demolition of the existing "temporary" bridge. The Project is funded 80% by Federal Highway and 20% by the State.

Shire was awarded the Project on October 21, 2003 with a contract price of \$10.3 million and an original completion date of September 6, 2006. To date, in addition to regular progress payments, the RIDOT has approved change orders valued at \$3.5 million with the concurrence of FHWA, yet the Project is only 30% complete, and the Project is nearly thirty (30) months behind schedule due to unresolved design/construction issues.

The Project has been plagued by with numerous problems: e.g. differing site conditions, excavation issues, utility issues, permitting issues, etc. The cornerstone of the delay issues relates to the east approach to the Barrington Bridge. Shire's means and methods of construction were to use the east approach as the staging area for construction which was an integral part of Shire's critical path. This critical work required to set the "staging" was to be completed by the end of January 2004. Due to a late notice to proceed issued by the RIDOT, environmental permitting constraints and the constructability issue discussed below, the staging work (demolition and installation of sheet piling) was not completed.

On March 18, 2004, Shire notified the RIDOT that a portion of the sheeting at the east approach could not be installed as designed because of the conflict with the existing concrete walls. Shire believed installing the sheeting through existing concrete walls would create an unsafe condition on the roadway. Shire requested direction from the RIDOT on how to proceed with construction. Between March 2004 and August 2006 there were numerous discussions and exchanges of information between Shire and the RIDOT as to the east approach problem and the best construction method. The RIDOT consistently took the position that the bridge could be built as designed. This issue went unresolved until mid-August 2006 when the RIDOT's consulting engineer, Haley-Aldrich, determined that differing site conditions prevented construction of the east approach in accordance with the original design (the RIDOT did not request an expert

REPORT ON THE BARRINGTON RIVER BRIDGE SETTLEMENT
CONFIDENTIAL, ATTORNEY CLIENT WORK PRODUCT

opinion from Halely-Aldrich until July 2006). Therefore, the RIDOT must redesign the east approach to accommodate the actual subsurface site conditions for Shire. It will take additional time for Shire to review the new design, provide pricing for construction and submit an updated construction schedule.

It is important to emphasize that Shire's original plan was to stage construction at the east approach which was an integral part of Shire's critical path. Due to the nearly 30 month delay in resolving the design issue, Shire could not construct the new bridge as planned in its original schedule. Shire mitigated certain claims by doing work out of sequence and doing all non-critical work to the substructure as no work could be done on the superstructure (the main roadway that connects the east and west abutments) which is the main part of the job. Once Shire's work is above the water line, the superstructure can be built in accordance with the original design.

The work on the east approach constitutes approximately 20% of the Project. Without final resolution of this issue, Shire cannot complete the Project and will soon need to stop work completely.

(ii) The Claims

Shire has submitted two claims to RIDOT that total more than \$13,100,000.

Claim 1 was submitted by Shire in April 2005 requesting a new completion date of June 2008 from the original completion date of September 2006. The claim was supplemented to request damages in the amount of \$7.1 million. Claim 1 is comprised of all damages in connection with delay through August 2005.

As the RIDOT's review of Claim 1 went unresolved for 16 months, Shire submitted a second claim (Claim 2) in June 2006, to capture the delay impact from September 2005 through May 2006. According to Shire the lengthy delay will require the entire project to be re-sequenced if the east approach design issue goes unresolved. In

**REPORT ON THE BARRINGTON RIVER BRIDGE SETTLEMENT
CONFIDENTIAL ATTORNEY CLIENT WORK PRODUCT**

essence, Shire anticipates finishing the Project in a manner not contemplated by the original bid plans assuming no resolution of the east approach constructability issue. Shire's worst case scenario estimates that the Project completion date would be pushed out to July 2010, and per Shire's surety, the estimated damages for Claim 2 will be approximately \$6,000,000 over and above Claim 1.

It should be noted that as Claim 2 ends in May 2006, there is additional exposure to the State until such time as the claim is resolved. However, this additional exposure is addressed in the proposed settlement.

III. Claim Review and Analysis

In July 2005, the RIDOT hired the consulting firm of PMA to perform an analysis on Claim 1. PMA researched the legitimacy of Claim 1 through interviews with the RIDOT personnel and records. The RIDOT engineering staff then utilized PMA's analysis to develop its own conclusion on Claim 1. The RIDOA Legal and Bureau of Audit staff examined Shire's submission along with the RIDOT's analysis to develop a final analysis based on the legal issues and factual issues not considered by the RIDOT.

Below is a table that compares RIDOA's assessment against Shire's submission and RIDOT's analysis. Following the table is a narrative addressing each category.

<u>Category</u>	<u>Shire Claimed Amounts</u>	<u>RIDOT</u>	<u>DOA</u>
1. Extended Job-Site Overhead	\$2,178,778	\$398,520	\$1,419,931
2. Equipment Cost	2,795,430	675,352	1,141,921
3. Labor Escalation	451,197	0	315,838
4. Material Escalation	195,634	207,346	195,634
5. Subcontractor	60,658	89,903	42,181

REPORT ON THE BARRINGTON RIVER BRIDGE SETTLEMENT
CONFIDENTIAL ATTORNEY CLIENT WORK PRODUCT

Escalation			
6. Additional Labor Cost	995,612	0	696,928
7. Muck Excavation Delay	(172,999)	0	(172,999)
8. 10% Profit	667,731	0	0
Total	<u>\$7,172,041</u>	<u>\$1,371,121</u>	<u>\$3,639,434</u>

1. Extended Job-Site Overhead. Shire utilized a modified "Eichleay Formula" approach to determine the costs for this category. The Eichleay Formula is an industry accepted method for determining home office overhead costs associated with prolonged construction project delays. As evidenced through Federal and State case law from several jurisdictions as well as the Arbitrator's Decision in *Shire v. RIDOT - Newport Marine Facilities Delay Damages Claim*, contractors are routinely awarded home office overhead costs resulting from lengthy delays. It should be noted that the governing authorities have awarded home office overhead despite contrary language in State contracts. In addition to this authority, Federal Highway Administration (FHWA) contract administration guidance states that FHWA will participate in home office overhead costs in cases where the owner has caused the delay during which time the overhead could not be charged off to other earnings and the contractor was prevented from doing other work which could have been allocated overhead. The guidance further states that FHWA will participate under these circumstances regardless of whether a state specification disallows overhead costs (RIDOT does have such a specification and limits recovery of overhead to 10% of other delay costs).

Applying the governing authority noted above to the prolonged delay of the Project, it is likely that a court would award home office overhead to Shire. Therefore, the DOA included these costs when estimating damages due to Shire.

The DOA reduced Shire's claimed amount for this category by lowering employee and field office charges and eliminating vehicle & equipment and consulting charges as these charges do not qualify as home office overhead costs. The DOA also

REPORT ON THE BARRINGTON RIVER BRIDGE SETTLEMENT
CONFIDENTIAL ATTORNEY CLIENT WORK PRODUCT

eliminated Shire's request for the 10% Blue Book specification profit amount as that would result in double payment to Shire since overhead costs are being awarded.

The RIDOT's number is substantially lower as it did not consider case law precedent or arbitration awards regarding the awarding of overhead costs and instead applied the 10% rule in accordance with the Project's contract specifications.

2. Equipment Cost. The DOA reduced this item by eliminating operating cost as Shire's claim is for idle time. Shire is only allowed 50% of the published Blue Book Rental Rate for idle time as accepted by FHWA.

3. Labor Escalation. Shire has claimed it should recover on this item based on the fact that the percentage of the Project remaining is 85%. The RIDOT's records indicate that the Project is 30% complete so it is more reasonable to apply 70% to this item.

4. Material Escalation. This item has not been changed as contractor's amount can be considered reasonable.

5. Subcontractor Escalation. Same logic as item 3 above.

6. Additional Labor Costs. Same logic as item 3 above.

7. Mud Excavation Delay Claim. There is no change to this item this amount has already been paid by a contract change order.

8. 10% Profit. This item has been eliminated as Shire is recovering this amount in the other categories above, otherwise, Shire would be double paid.

In connection with Claim 2, neither the RIDOT or the RIDOA was provided with a detailed claim submission by Shire. However, it is reasonable to conclude that Shire would be successful on the merits as all delays from Claim 1 continue into the Claim 2

REPORT ON THE BARRINGTON RIVER BRIDGE SETTLEMENT
CONFIDENTIAL ATTORNEY CLIENT WORK PRODUCT

time period. Further, it is reasonable to assume that if the RIDOT does not resolve the east approach design/constructability issue, Shire will be forced to resequence all critical path work to finish the job.

IV. Legal Liability and Damages

In the event that that Shire's Claims 1 and 2 are litigated rather than settled administratively, the RIDOT will be at a disadvantage in regards to liability which may undermine any defense the RIDOT has to Shire's claims for monetary damages. The following briefly addresses the material legal issues.

1. Cardinal Change. Shire can argue that a cardinal change has occurred with this Project which would be a material breach on the part of the RIDOT. The factors that result in a cardinal change are: (1) 30% in change orders, excluding delay claim (will be over 80% with proposed settlement); (2) new design for east approach to change 20% of the original project; (3) admission of over 600 delay days.
2. Bad Faith. The RIDOT can be found to have acted in bad faith by (1) failing to resolve the east approach issue in a timely manner (30 month review appears unreasonable); (2) failure to resolve Claim 1 in a timely manner (16 month review is unacceptable due to the magnitude of the claim and the fact that the RIDOT should have known that Shire was entitled to a time extension early in the review process); (3) failure to resolve issues timely (at the time Shire submitted Claim 1, April 2005, Shire also updated its schedule with a new completion date of June 2008, with no objection from the RIDOT—de facto acceptance).
3. Litigation Issues. (1) Prior to filing suit in Superior Court, Shire must exhaust its administrative remedies by submitting a formal claim under Blue Book Section 105.18. Submission and review of a formal claim will delay matters longer and increase costs; (2) it may take 3 to 5 years for a lawsuit to reach final judicial determination and would consume significant economic and human resources

REPORT ON THE BARRINGTON RIVER BRIDGE SETTLEMENT
CONFIDENTIAL ATTORNEY CLIENT WORK PRODUCT

RIDOT, RIDOA, Attorney General, and Outside Counsel); (3) Credibility for the State will be a huge issue as Shire will have ample evidence that the RIDOT was inefficient in management over costs, construction and design of the Project; and (4) actual damages are unknown and speculative, costs are unknown and speculative, and Shire would be entitled to prejudgment interest under R.I. Gen. Laws §37-13.1-1(b).

4. Damages: In the event of a lawsuit, it is our estimate that it will likely cost the State over \$1 million to litigate this matter whether the suit is favorable to the State or not. The costs for litigation may include but not be limited to, Outside Attorney fees, Consultant fees, and costs for personnel from DOA, RIDOT and the Attorney General. Further, based on R.I. Gen. Laws §37-13.1-1(b), Shire would be entitled to prejudgment interest starting from the date suit is filed. Per the statute, the interest applied is the weekly average one year constant maturity treasury yield. The rate is currently is 5.07%. For purposes of our analysis below, we used a rate of 6% which we believe is reasonable based on expected movement in the market. We also estimated that the suit would be resolved in five years. The analysis below is an estimate of what the monetary cost of lawsuit would be in totality.

	<u>Shire</u>	<u>RIDOA</u>
Estimated Damages	\$7,172,044 to \$13,172,044*	\$3,639,434 to \$6,188,240**
Estimated Costs	1,250,000	1,250,000
Estimated Prejudgment Interest	2,425,769 to 4,455,118	1,230,950 to 2,093,021
Total	<u>\$10,847,812 to \$17,627,162</u>	<u>\$6,029,063 to \$8,281,261</u>

* Includes Shires estimate of an additional \$6,000,000 for Claim 2.

** Since Shire has not submitted a full detailed analysis on Claim 2, we did not have precise data to analyze, however, assuming Shire follows the same methodology used in

REPORT ON: BARRINGTON RIVER BRIDGE SETTLEMENT
CONFIDENTIAL ATTORNEY CLIENT WORK PRODUCT

Claim 1, we earmarked our estimate for damages by applying the ratio of our calculated damages on Claim 1 to Shire's claimed damages in Claim 1 (approximately 42%).

5. Other Factors to Consider. In the event that Shire's claims are not resolved through administrative settlement, then it is probable that Shire will discontinue work on the Project. Termination by Shire would require the RIDOT to rebid the remaining work on the Project. A rebid of the Project means months of delay and a further increase in construction costs. The RIDOT current estimates for additional construction costs above the original contract is approximately \$2 million. It is also likely that Shire will sue for lost profits on the original contract price and for other damages not yet revealed. (damages to business, etc.).

V. Non-Legal Issues to Considered

The following non-legal issues were also considered in connection with the proposed settlement:

1. If Shire's claims head to court, the public disclosure of the facts and circumstances surrounding management of the Project would create unfavorable publicity for the State and FHWA.
2. The Project will suffer more delays and continue to increase construction costs.
3. The political leaders and constituents of the Town of Barrington will not be pleased with continued delays on the Project.
4. The Warren Avenue Bridge project will be completed before the Project although the Warren Avenue Bridge project was awarded in the spring of 2006.

VI. Proposed Settlement

REPORT ON THE BARRINGTON RIVER BRIDGE SETTLEMENT
CONFIDENTIAL ATTORNEY CLIENT WORK PRODUCT

The proposed settlement is broken down into two parts:

Part I. The State will pay Shire \$5.3 million to absolve the State from any further liabilities in connection with Claims 1 and 2. The new Project completion date will be October 31, 2008, exclusive of dealing with the east approach design/construction issue which is handled in Part II below. This portion of the settlement controls the amount of expenses and damages the State could possibly incur.

Part II. The parties will agree on a very detailed and specific process to develop an agreement on new design and related construction costs in connection with the east approach. The process will include milestones for the RIDOT to provide Shire with a new design for the east approach and for Shire to price the new design work and develop a new schedule. Shire's surety proposes giving the RIDOT three options to select from for completion of the work (different pricing and schedules). In the event that disputes or issues arise in connection with this process, the parties will agree to a fast track decision by an independent party. The parties will split the costs of the independent review. Such costs shall not be charged to the Project.

The parties will also agree on a process to manage the remainder of the Project. As there is no more float left to complete the Project, tight deadlines must be met. A thorough management process will be in place until Shire is working above the waterline since all subsurface work on the Project is complicated and critical to finishing the Project. Surface work on the Project is less complicated and does not need an extra layer of management. The review process shall include: (1) an executive oversight committee that meets monthly until the Project is out of water and on land; (2) fast track decision making (certain change orders shall be approved in the field); and (3) disputes shall be resolved by independent party (costs of such disputes to be shared equally between Shire and State and not charged to the Project).

REPORT ON THE BARRINGTON RIVER BRIDGE SETTLEMENT
CONFIDENTIAL ATTORNEY CLIENT WORK PRODUCT

Part II of the settlement goes a long way towards controlling the management and direction of the Project to make sure that further delays do not occur.

VII. Federal Highway Participation on Claim

Barrington Bridge is a so-called Federal participation (80%/20%) project. FHWA regulations (23 CFR 635.124) obligate FHWA to participate in contract claim awards and settlements except when FHWA determines that the State has acted with either gross negligence or participated in intentional acts or omissions, fraud, etc.

From the outset THE RIDOT kept FHWA fully apprised of all developments on the Barrington Bridge Project. The FHWA has had ample opportunity to review Shire's claim and to participate in discussions regarding both resolution of the claim and completion of the Project. During this process the FHWA has neither objected to the RIDOT's handling of the claim, nor insisted upon an audit of Shire's actual costs. Because the claim arises from unforeseen subsurface site conditions which necessitate a partial redesign the State expects FHWA to participate in settlement. In the event that the RIDOT determines that its project design consultant has any liability for not identifying the site conditions which gave rise to Shire's claim, then the RIDOT shall seek contribution or indemnification from the design consultant.

VIII. Conclusion

The proposed settlement above is the best solution to resolve Shire's claims against the State. The settlement allows the State to cap its exposure to increased monetary damages and regain management control of the Project.