IN THE COURT OF APPEALS OF IOWA

No. 3-194 / 12-1565
Filed April 24, 2013

TEAM TWO, INC.,
Plaintiff-Appellee,

vs.

CITY OF DES MOINES, IOWA,
Defendant-Appellant.

Appeal from the Iowa District Court for Polk County, Brad McCall, Judge.

The City appeals following a jury verdict finding it breached the terms of a contract with a billing contractor, Team Two, Inc. **AFFIRMED IN PART, REVERSED IN PART, AND REMANDED.**

Steven C. Lussier, Assistant City Attorney, Des Moines, for appellant.

Benjamin M. Clark and Louis R. Hockenberg of Sullivan & Ward, P.C., West Des Moines, for appellee.

Heard by Vogel, P.J., and Vaitheswaran and Bower, JJ.

VOGEL, P.J.

The City of Des Moines appeals a jury verdict finding it breached the terms of its contract with Team Two, Inc., an ambulance billing contractor. At trial Team Two asserted the City breached the express terms of the written contract or, in the alternative, breached the implied covenant of good faith and fair dealing. The jury agreed and awarded Team Two past and future damages. On appeal, the City contends substantial evidence does not support a finding that it breached the implied covenant of good faith and fair dealing. It therefore claims the court erred in giving the jury a general marshaling instruction and a general verdict form, which did not require the jury to show whether it based its verdict on a breach of a specific term of the contract or on a breach of the implied covenant. The City also contends the jury should not have been permitted to award future damages because this case involved only a partial breach.

Because we find sufficient evidence supports the finding that the City breached the implied covenant of good faith and fair dealing by implementing a write-off policy of the accounts Team Two worked prior to the termination of the contract, we affirm the jury's verdict and conclude the court did not err in submitting a general verdict form and a jury instruction with alternate theories. However, we reverse the jury's award of future damages because the only remaining duty in the contract is the payment of money in installments to Team Two by the City, and there was no acceleration clause. We remand the case to the district court for the entry of an equitable order to ensure the City pays Team Two a percentage of future collections received by the City on pre-2010 accounts.

I. BACKGROUND FACTS AND PROCEEDINGS.

Team Two is an ambulance billing contractor, which since 1996 contracted with the City of Des Moines to provide billing services for the ambulance runs the City performed. Josh Engman took control of Team Two in 1998 and was the main employee performing the billing work for the City. In 2004 the City issued a Request for Proposal to solicit bids from businesses to conduct the ambulance billing services. Team Two submitted a bid, and the City accepted Team Two's proposal. A written contract was signed in January 2005, which was effective October 1, 2004. The contract was for three years with two one-year renewal options, which were executed.

Team Two was to bill for the City's ambulance service. After a patient was transported by ambulance, Team Two would download data from the fire department's computer system. It would then obtain the patient and insurance information, perform the medical coding work, and initiate the billing process. If the patient had insurance, the insurance company would be billed accordingly, and if the patient did not have insurance or did not provide insurance information, the patient would receive a bill directly. If the data Team Two received was incomplete, it would need to track down the required information from the City or from the hospitals. After the first billing went out, Team Two would follow up every thirty days until the bill was paid, including billing the patient for his/her portion after the insurance payment was received. If no payment was received within ninety days from the invoice date and there was no reasonable expectation of payment, the contract provided for Team Two to send the account information to the City's collection agency.

In January 2009, the City began participating in the Iowa Income Offset Program. Instead of sending past due accounts to the collection agency, a list of the delinquent accounts within set parameters was provided to the State. The State then ran a search of individuals who are owed money from the State, such as those receiving a tax refund, against the list of delinquent accounts provided by the City and other government creditors. If there was a match, the State notified the City, and the City sent a letter to the debtor, informing the debtor of the amount owed and the hold that had been placed on the money. Initially the letter gave the debtor Team Two's phone number to contact with any questions, however, that phone number was changed to the City after the contract with Team Two terminated. After fifteen days, if no response from the debtor was received, the City contacted the State, and the funds were released to the City. When the State remitted the money to the City for the payment of the debt, the State charged the City a $7.00 administrative fee, which was initially passed on to the individual owing the debt.[1] There was no charge for the Income Offset Program if no collection occurred.

During the term of the contract, Team Two invoiced the City monthly based on the collections received in the previous month. Regardless of when the initial billing was done, Team Two received a percentage of the amount collected in the month following the collection. Team Two billed the City for its percentage based on the rate in the contract that was effective when the ambulance run was made. The rate that was applied to ambulance runs under the 2004 contract was

[1] At the time of trial, the City had recently begun absorbing the $7.00 fee instead of passing it on to the debtor.

five percent, though it was higher in previous years. The percentage was also applied to funds received in the preceding month from the collection agency and later the income offset program. Team Two received the collection information for each month from the City, it posted the payments received to the various account records, and then it invoiced the City based on the collections received.

The contract between Team Two and the City terminated on September 30, 2009, but the parties agreed to an extension until December 31, 2009, in order to conduct another request for proposal process. Team Two was not awarded the new contract beginning January 1, 2010.

In the contract at issue in this case, there was a ninety-day dual collection transition period where Team Two continued working on the accounts for ambulance runs up to and including December 31, 2009. The new contractor started billing ambulance runs beginning January 1, 2010. Team Two continued to do the follow up and records receipts on the pre-2010 accounts until March 31, 2010, at which time it was the intent of the City to have the pre-2010 account data transferred to the new contractor. However, the transfer of data never occurred due to computer system complications.

There were initial discussions about entering into a new contract between the City and Team Two so that Team Two could continue working the pre-2010 accounts. During the negotiations, Team Two continued to work the accounts through April 2010. However, when negotiations broke down, the City directed Team Two to provide the pre-2010 account data to the City, and Team Two's access to the accounts was terminated. Team Two was paid for its work through the end of April 2010. Because the City did not provide Team Two access to the

collection information to determine how much money had been received on the pre-2010 accounts and refused to pay Team Two a percentage of the collection received on those accounts, Team Two filed suit on June 25, 2010.

During the course of the lawsuit, Team Two became aware of a new "write-off policy" the City had implemented beginning January 2012. The write-off policy removed accounts from collections if the date of service was prior to 2005 and the account had no activity for three or more years or if the account had had no activity for five or more years. This write-off policy removed 12,355 accounts, totaling $5,321,096 in receivables, from collection activity. When Team Two became aware of this write-off policy, it amended its complaint to add a claim of a breach of the implied covenant of good faith and fair dealing. It also sought to enjoin the City from continuing its write-off policy and asked for a declaratory judgment to continue to receive a percentage on account collections in the future from pre-2010 accounts it had serviced.

The case proceeded to a jury trial. The City filed a motion in limine asking the court to prohibit Team Two from presenting an expert opinion on the future value of the collections on the pre-2010 accounts. The court initially overruled the motion. However, the court revisited the motion during the second day of trial stating that it would now sustain the motion and submit interrogatories to the jury in order to determine whether an order for specific performance should be entered regarding the future damages. The court revisited the issue again when the City asserted under the termination provision of the contract, it needed to show that the money that was coming in on the pre-2010 accounts after the termination of the contract was a result of the City's efforts and not Team Two's

efforts prior to the termination of the contract. The court ruled the City needed to make an election; if the City offered evidence of the City's work to collect the accounts after the termination of the contract, the City opened the door for Team Two to offer evidence of future damages. When the City insisted that the subsequent work by the City was relevant to the termination provision of the contract, the court allowed Team Two to present evidence related to its entitlement to future damages including the projected future amount.

The jury was asked in the verdict form whether the City breached the contract, "either by failing to perform a specific term thereof or by breaching its duty of good faith." The jury responded, "Yes." The jury stated that the breached caused damage to Team Two in the amount of $34,300 for "past lost contract payments" and "$69,999 or as stated" for "future lost contract payments." The City filed a motion for judgment notwithstanding the verdict and a motion for a new trial. After a hearing, the court denied both motions. The City appeals.

II. SCOPE AND STANDARD OF REVIEW.

A breach of contract claim, which is tried in the district court at law, is reviewed for the correction of errors at law. *NevadaCare*, *Inc*. *v*. *Dep't of Human Servs*., 783 N.W.2d 459, 465 (Iowa 2010). When the claim made on appeal is that substantial evidence does not support the verdict, we review the claim in the light most favorable to the nonmoving party, which in this case is Team Two. *Royal Indem*. *Co*. *v*. *Factory Mut*. *Ins*. *Co*., 786 N.W.2d 839, 846 (Iowa 2010). "Evidence is substantial when a reasonable mind would find the evidence adequate to reach the same findings." *Tredrea v*. *Anesthesia & Analgesia*, *P*.*C*., 584 N.W.2d 276, 280 (Iowa 1998).

The City's claim regarding the award of future damages is a legal question. *Summy v. City of Des Moines*, 708 N.W.2d 333, 340 (Iowa 2006). "Under Iowa law, a court is required to give a requested instruction when it states a correct rule of law having application to the facts of the case and when the concept is not otherwise embodied in other instructions." *Id.*

III. SUBSTANTIAL EVIDENCE.

In its first claim on appeal the City asserts substantial evidence does not support a finding that it breached the implied covenant of good faith and fair dealing. The express contract language at issue in this case stated, "In the event of termination pursuant to this section or upon expiration of the term of this Contract, payment shall be made by the CITY for collections received by the CITY resulting from services rendered by the CONTRACTOR prior to the date of termination."

Team Two asserted that this provision entitled Team Two to a percentage of future collections received by the City on accounts Team Two created during the contract—the pre-2010 accounts. It was the City's position that the term "resulting from services rendered" meant Team Two was entitled to a percentage but only on the money that was collected as a direct result of only Team Two's efforts. The City argued the money received after the termination of the contract was largely the result of the income offset program or the City's efforts, not Team Two's efforts.

Team Two's amended petition, asserting a breach of the implied covenant of good faith and fair dealing, was based exclusively on the City's development and implementation of a write-off policy during the course of the litigation.

However, the implementation of such a policy could only be considered to be a breach of the implied covenant if Team Two had a right or an interest in a percentage of the money that could have been collected but for the write-off policy. Before the City could breach the covenant of good faith and fair dealing by implementing the write-off policy, the jury first needed to find that Team Two was entitled to a portion of the money collected from the accounts that were written off despite the termination of the contract. If Team Two was not entitled to future payments under the contract on accounts it created and billed prior the termination of the contract, then the City did nothing that could be interpreted as a violation of the implied covenant by writing off any or all of its pre-2010 accounts after the contract with Team Two terminated.

The jury answered "Yes" to the court's question of whether the City breached the contract with Team Two "either by failing to perform a specific term thereof or by breaching its duty of good faith." As stated above, the two issues are interconnected. The jury could not have found a breach of the implied covenant without first finding a breach of a specific term of the contract. On appeal, the City does not allege that there is insufficient evidence to support the finding that it breached an express term of the contract. Therefore, in analyzing the substantial evidence to support the finding of a breach of the implied covenant, we build upon the foundation that upon termination of the contract the City had an express obligation to pay Team Two a percentage of the collections the City received on the accounts Team Two created and billed during the contract.

"An implied duty of good faith and fair dealing is recognized in all contracts." *Bagelmann v. First Nat'l Bank*, 823 N.W.2d 18, 34 (Iowa 2012). "Good faith performance or enforcement of a contract emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party." Restatement (Second) of Contracts § 205 cmt. a (1981). "[B]ad faith may be overt or may consist of inaction, and fair dealing may require more than honesty." *Id.* at cmt. d.

> "The underlying principle is that there is an implied covenant that neither party will do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract." This implied covenant generally operates upon an express condition of a contract, the occurrence of which is largely or exclusively within the control of one of the parties

Am. Tower, L.P. v. Local TV Iowa, L.L.C., 809 N.W.2d 546, 550 (Iowa Ct. App. 2011) (citation omitted). The covenant does not "give rise to new substantive terms that do not otherwise exist in the contract." *Bagelmann*, 823 N.W.2d at 34. "'[I]nstead, the duty of good faith is meant to give the parties what they would have stipulated for at the time of contracting if they could have foreseen all future problems of performance.'" *Am. Tower*, 809 N.W.2d at 550 (citation omitted).

We, like the district court, find substantial evidence to support a finding that the City breached the implied covenant of good faith and fair dealing by implementing the write-off policy. As stated above, we start with the foundation that the termination provision of the contract expressly required the City to pay Team Two a percentage of the money collected on the receivable accounts Team Two created prior to the termination. Team Two was to be paid five percent of the total ambulance billing collection, "including those received

through the CITY's lockbox, payments received directly by the CITY, payments made to the CITY's collection agency, and, until such time as all payments are directed to the CITY's lockbox, payments made directly to the CONTRACTOR."

Josh Engman testified at trial that throughout the contract term he was paid a percentage of the total amount the City collected regardless of the source of the money. The City initially had him send delinquent accounts—accounts which after ninety days had not been paid and had no reasonable expectation of being paid—to the City's collection agency. Later, the City directed Engman to stop sending the delinquent accounts to the collection agency, but instead to send them back to the City where the accounts would be submitted to the income offset program. Engman complied with the request.

While the City points out that no provision in the contract specifically directs it to send delinquent accounts to the collection agency or the income offset program, we find the contract contained an agreed common purpose that collection efforts would continue on delinquent accounts after the ninety-day period, and Team Two had a justified expectation that the collection on the pre-2010 delinquent accounts would continue after the contract was terminated. Restatement (Second) of Contracts § 205 cmt. a (1981). In the first year of the write-off policy, the City stopped any kind of collection action on 12,355 accounts amounting to approximately $5.3 million in receivables. The City did not discharge that debt but simply stopped taking collection action on the accounts by removing them from the list the City sent to the income offset program. If a payment happened to be made on any of those accounts, it would be applied to the associated debt. Moreover, the City finance director testified those accounts

were "temporarily" taken out of the offset program for the calendar year 2012, but could be put back in the future. Team Two fully performed its obligations under the contract, and the City, through inaction by failing to at least attempt to collect on the delinquent accounts as it had throughout the pendency of the contract, injured Team Two's right to "receive the fruits of the contract." *Am*. *Tower*, 809 N.W.2d at 550. Substantial evidence supports the finding that the City breached the covenant of good faith and fair dealing in the implementation of its write-off policy.

The City also asserts it was error for the court to put both theories of breach—"failing to perform a specific term thereof or by breaching its duty of good faith"—into one global question on the jury verdict form and by combining the theories into one marshaling instruction. The City claims that it suffered prejudice because we, as the reviewing court, cannot now determine which theory the jury accepted and which theory the jury based its award of damages on. As stated above, substantial evidence supports the breach of the implied covenant of good faith, and the City does not challenge the substantial evidence to support the theory that it breached an express term of the contract. In addition, we found the two theories interconnected. Because substantial evidence supports both theories, it was not error for the district court to submit a general verdict form or to instruct on both theories in one marshaling instruction. *Cf*. *Gordon v*. *Noel*, 356 N.W.2d 559, 565 (Iowa 1984) (remanding a case for a new trial where the court erred in submitting one of several theories to the jury and the jury returned a general verdict).

IV. FUTURE DAMAGES.

The City's next claim on appeal is that the court erred in instructing the jury that it could award future damages in this case. The City asserts under the common law, as stated in Restatement (Second) of Contracts section 243(3) (1981),[2] future damages are not recoverable in a case of a partial breach.

The City asserts both parties agreed Team Two fully performed its obligations under the contract. The only question to be decided was whether the contract required the City to pay Team Two a percentage of the collections received after Team Two stopped performing services. If the jury believed Team Two's claims, the only remaining duty was for the City to pay a percentage of collections in installments based on the previous month's collections. There was no acceleration clause in the contract, so the City asserts future damages are not recoverable because it has no obligation to pay Team Two until the collections are received each month.

On the morning of the first day of trial, the court partially agreed with the City, ruling:

> Okay. I'm going to overrule the motion in limine. From the sounds of things, the jury will ultimately be called upon to decide whether or not the plaintiffs are entitled to future damages, in other words, whether under the terms of the contract the city has an ongoing obligation to pay over future receipts or a portion of future receipts to the plaintiff.

---

[2] Restatement (Second) of Contracts section 243(3) provides:

> Where at the time of the breach the only remaining duties of performance are those of the party in breach and are for the payment of money in installments not related to one another, his breach by non-performance as to less than the whole, whether or not accompanied or followed by a repudiation, does not give rise to a claim for damages for total breach.

> The issue that I have not yet determined is whether or not the jury will be fixing the amount of those future damages, or whether they will simply determine entitlement to future damages and we can and will address that issue in the jury instructions.

The court instructed Team Two to wait on calling its future damages expert, Mr. Lodden, if possible, so that it could determine whether or not the jury would be fixing the amount of damages. On the morning of the second day of trial, the court made a further record on the issue:

> I have had a further opportunity to reflect on the first motion in limine filed by the City of Des Moines. That motion in limine seeks to limit evidence and testimony offered by the plaintiff related to future damages.
>
> I had previously indicated that the motion in limine would be overruled. After further consideration, I have concluded that under the facts and circumstances of this case as the evidence has come in, it would appear that the provisions of Restatement of Contract 2, Section 243, Subparagraph 3, do in fact apply here. Specifically, that subsection states "Where at the time of the breach the only remaining duties of performance are those of the party in breach and are for the payment of money in installments not related to one another, his breach by non-performance as to less than the whole, whether or not accompanied or followed by a repudiation, does not give rise to a claim for damages for total breach."
>
> It is my belief that that provision would apply to prevent a current recovery by the plaintiffs of future anticipated damages under the facts and circumstances presented in the case at bar. It is my expectation, and the plaintiff has pled in the alternative a request for what I will refer to as equitable relief which would in effect order the city to take certain steps in the future as to future income, and I would anticipate submitting interrogatories to the jury so that the jury can make the appropriate factual determinations. And if they make the appropriate factual determinations, to enter such an order for specific performance against the city.
>
> So bottom line, the previous ruling on the motion in limine related to future damages is sustained.

Team Two then sought to make an offer of proof of Mr. Lodden's testimony by submitting the written transcript and videotape of Lodden's deposition, which the court granted. Team Two also sought a ruling from the court to prevent the City

from offering evidence that Team Two had failed in some manner to perform under the contract. Since the City was arguing this was only a partial breach under section 243(3), Team Two argued the City could not then claim the money coming in after the termination of the contract was due to the City's efforts in an attempt to persuade the jury that Team Two should not be entitled to it.

The court agreed with that view; however, the City protested, asserting it was not arguing Team Two still had obligations under the contract after it was terminated. Instead it was offering the evidence of the City's work to collect money after the contract terminated to prove under section 10 of the contract, the money, if any, Team Two would be due, must be money that "resulted from" its work as opposed to the City's work. So long as the City did not argue Team Two had any obligation under the contract to continue to try to collect on the pre-2010 accounts, the court would allow the City to put on evidence of the work it was doing to collect on the accounts after the contract was terminated.

Later that morning during the questioning of the City's treasury manager, a further discussion was held between the parties and the court regarding the evidence of the City's efforts to collect on the pre-2010 accounts after the termination of the contract. The court had counsel look at the proposed jury instructions, and stated:

> The third element of each of those is that the plaintiff has done what the contract requires.
>
> I'm inclined to believe that if you want to keep out of evidence future damages testimony by the plaintiff, that that particular element of the marshaling instruction needs to say the evidence establishes that plaintiff fulfilled all of its obligations under the contract. That is no longer an element that the plaintiff must establish, would you agree?

The City disagreed with the court's articulation of the issue, again asserting that in order to prove Team Two was not entitled to future payments under section 10, it had to show that the money coming in after the termination of the contract was not "resulting from" Team Two's "services rendered," but through the City's efforts either through collection actions or the income offset program. The court stated: "I think you, by getting into that, open the door to the future damages issue. And you need to make an election, you need to decide whether you want to open that door or not." The court went on to say:

> You see, if you—if you argue that the reason this income is now coming in is because the city is doing work that while the contract was in effect Team Two was doing, then this is no longer a situation where the only remaining duties of performance are those of the party in breach. It's a situation where there were—you are arguing duties and responsibilities on the part of the plaintiff and that opens the door to the future damages testimony, which you may then rebut by arguing that, well, you would have had expenses if you had this future responsibility and those expenses should be offset against the income you would have received.

The City's attorney stated it was the City's position that the subsequent work by the City was relevant to the interpretation of section 10, and thus, it would continue to offer evidence of the work the City was performing to collect on those accounts. The court then ruled that under the circumstances, Team Two would be permitted to present evidence and testimony related to future damages.

The City objected to the court's inclusion of an instruction to the jury regarding future damages, and after the jury returned a verdict awarding $69,999 in future damages, the City filed a posttrial motion seeking a new trial based on the alleged error of the court in submitting the issue of future damages to the jury. The court denied the motion.

Team Two claims the award of future damages was proper because the City insisted on presenting evidence of the work it was doing to collect the pre-2010 accounts after the termination of the contract. Team Two asserts "the implication from that evidence is that Team Two is *not* performing the work required under the Contract, and has somehow not performed all of its remaining duties." While Team Two acknowledges the City never argued Team Two had unfulfilled obligations under the contract, Team Two claims the jury could still have drawn this inference and awarded future damages based on a total breach rather than a partial breach.

While both the district court and the parties use Restatement (Second) of Contracts section 243(3) to support or oppose the award of future damages in this case, we note subsection three of section 243 has not been specifically adopted by our supreme court, and we need not adopt it here in order to reach the conclusion that the district court erred in submitting the issue of future damages to the jury. Under the contract, the monthly payment to be made to Team Two is based solely on the amount collected the prior month by the City. Both parties agreed that Team Two had no further obligation to continue to perform any type of service under the contract, so the only remaining obligation is for the City to pay. The contract in this case contains no acceleration clause. The City is not obligated to pay until money is collected on the pre-2010 accounts in a given month.

The case of *Andrew v. Stearns*, 244 N.W. 670, 670–71 (Iowa 1932), involved the breach of an installment contract where the only duty that remained was for the breaching party to pay money in installments. When the defendant

failed to pay the first installment, the plaintiff sued for that installment plus the interest due. *Andrew*, 244 N.W.2d at 670. The district court entered judgment in favor of the plaintiff. *Id.* When the defendant failed to pay the second installment, the plaintiff sued again for the second installment plus the interest due. *Id.* The defendant alleged the first action provided the plaintiff all the relief he was due under the contract and sought to have the action dismissed. *Id.* at 670–71. The supreme court ruled that the second action was proper, noting there was no acceleration clause and the only amount due in the first action was the amount of the first installment payment. *Id.* at 671. The court explained that if the plaintiff had tried to sue on all installment payments in the first action, the defendant could have objected that any request beyond the first installment was premature. *Id.*

The same analysis applies in this case. At the time of trial in this case, the City had collected a certain amount on the pre-2010 accounts and failed to pay that amount to Team Two. Judgment was properly entered on the amount currently then owing on the amount collected. However, until such time as the money is collected on the pre-2010 accounts going into the future, the City has no obligation to make payment on the contract because there is no acceleration clause. The amount due into the future depends wholly on the amount of money recovered by the City each month on the pre-2010 accounts. While Team Two's expert, Lodden, projected the amount based on historic patterns of collection, any attempt to collect that money in advance is premature.

Equitable relief is available to Team Two to ensure that the City continues to make the payments as the money is collected. *See Janssen v. N. Iowa*

Conference Pensions, *Inc*., 166 N.W.2d 901, 907 (Iowa 1969) ("A decree of specific performance rests in the sound discretion of the court. Its object is to best effectuate the purposes for which the contract was made, and it should be granted upon such terms and conditions as justice requires."); *see also* Restatement (Second) of Contracts § 359 cmt. b (1981) ("The fact that damages would be an adequate remedy for failure to render one part of the promised performance does not preclude specific performance of the contract as a whole. In such a case, complete relief should be granted in a single action and that relief may properly be a decree ordering performance of the entire contract if the other requisites for such relief are met."). However, Team Two was not entitled to an award of a fixed amount of future damages based on Lodden's projections.

We vacate the jury's verdict with respect to its award of future damages to Team Two and remand the case for the district court to craft an order of equitable relief to ensure the City pays Team Two its percentage of the City's future collections as received on pre-2010 accounts.

AFFIRMED IN PART, REVERSED IN PART, AND REMANDED.