BRADLEY ARANT BOULT CUMMINGS LLP **First Quarter 2010**

CONSTRUCTION AND PROCUREMENT LAW NEWS

Recent federal, state, and local developments of interest, prepared by the firm's Construction and Procurement Group:

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Your Work Stinks! – Insurance Coverage for Odor Remediation as "Physical Injury to Property"

An insurer has two principal duties arising from a Commercial General Liability (CGL) policy. The first is the duty to provide a defense for its insured (duty to defend) and the second is the duty to pay for covered losses (duty to indemnify). Generally, courts require an insurer to defend cases where a reasonable view of the facts alleged could render the insurer responsible, even if the facts necessary to prove coverage are not known when the insured is sued. The practical effect of a broad duty to defend, coupled with a narrower duty to indemnify, is that insurance companies often end up paying for losses where coverage is questionable when the cost of the defense would be close to or higher than the amount of the alleged loss.

The United States Court of Appeals for the First Circuit – one of the eleven circuit courts just below the U. S. Supreme Court in the federal system – recently held that an odor allegedly caused by defective carpeting in a building could constitute "physical injury to property" such that an insurer has a duty to defend under the terms of a CGL policy. The impact of this ruling is that CGL insurance carriers faced with similar allegations must provide a defense, though not necessarily indemnity for the underlying damages, to their policy holders.

In *Essex Insurance Company v. Bloom South Flooring Corporation*, a general contractor was an additional insured on its subcontractor's CGL policy. The subcontractor was responsible for installing carpet in an office building, which required testing and cleaning an existing concrete floor prior to installation. The occupants of the building noticed a foul odor and instructed the general contractor to fix the problem. The general contractor removed the installed carpet and its adhesive, and re-carpeted the floor. This effort did not fix the problem and actually

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made it worse. After disputing the cause of the odors with the subcontractor, the general contractor incurred $1.4 million in remediation costs and sued the subcontractor to recover them. During the course of the remediation, the general contractor demanded a defense from its insurer based on the owner's demands for remediation and indemnity for the costs it incurred. The insurer refused. The general contractor also sued the subcontractor, which again demanded a defense from the insurer. The insurer filed a declaratory judgment action, asking the court to determine it has no duty to defend its insured.

The court began by finding that the odor, which was alleged to have permeated the building, constituted "physical injury" under the policy. Thus, the alleged damage was within the scope of the insured's coverage. Next, the court turned to the business risk exclusions of the CGL policy. It held that the odor damaged the existing concrete floor, which was real estate rather than the subcontractor's "work" or "product." Because the property damage could not be remedied by "the repair, replacement, adjustment or removal" of the insured's work – special air venting was required to remove the odor, in addition to repairs – the "impaired property" exclusion did not apply. These holdings placed the damage arguably within the coverage clause and arguably outside the exclusions, which was all that was necessary to require the insurer to defend its insureds.

When issues arise on a construction project, owners, contractors, subcontractors, and others involved should consider each of their insurance policies and whether damages could be covered by one of the parties' policies. Insurance policies and their exclusions are often complex and are governed by laws which may vary from state to state. Thus, it is always advisable to contact counsel for advice regarding coverage. If there is any possibility of coverage, it is worth putting the insurer on notice to initiate an insured's duty to defend.

By Jonathan Head

Termination for Convenience Clauses: Why They May Be Inconvenient and How to Use Them Effectively

Termination for convenience clauses have become popular provisions in many construction contracts. They allow an owner or contractor to terminate obligations under a contract without alleging any fault. A typical termination for convenience clause might read "Owner may at any time and for any reason terminate the contract at Owner's convenience. At such time, Contractor must cease all activities under the contract." As these clauses have become more common in the construction industry, courts have struggled over their effect and scope. Generally, courts have been unwilling to interpret these clauses as providing an owner carte-blanche power to terminate the contract. Instead, some courts have required a showing of good faith before enforcing a termination for convenience clause. However, few courts have explained the extent of this good faith obligation.

In *Questar Builders, Inc. v. CB Flooring, LLC,* the Court of Appeals in Maryland confronted this issue. The court found that the duty of good faith which the court held was implied in termination for convenience clauses afforded owners discretion to terminate a contract so long as termination followed the reasonable expectations of the contractor.

In this case, a general contractor for a luxury apartment project subcontracted the flooring installation. The subcontract included a termination for convenience clause. Before the subcontractor started its work, the general contractor terminated the subcontractor citing the convenience clause. In response, the subcontractor filed suit for breach of contract. One of the general contractor's primary defenses focused on the validity of the termination for convenience clause.

The court considered whether the general contractor had exercised good faith such that it had a right to invoke the termination for convenience clause. Specifically, it considered the behavior of the contractor in the weeks prior to termination. This gave the judge serious pause because the general contractor contacted another business to organize a proposal for

the floor installation and failed to express any concerns regarding performance to the subcontractor before doing so. The judge determined that the convenience clause did not provide a limitless power to terminate and awarded damages to the subcontractor for the general contractor's breach of contract.

On appeal, the general contractor claimed that the trial court did not provide an adequate explanation of its reading of the convenience clause. The court of appeals agreed and responded by reading a duty of good faith into all termination for convenience clauses. In explaining its rationale, the court looked to the widespread use of the good faith standard across the country. According to the court, a termination for convenience clause affords a general contractor discretion to terminate in the event of some change in circumstances that makes a project economically unfeasible like, for instance, a rapid change in market conditions. However, such discretion must be exercised in accordance with the reasonable expectations of the subcontractor or other party.

As a practical matter, owners and contractors should ensure that they are acting reasonably before terminating another party based on a termination for convenience clause. Otherwise, they may face lawsuits for lost profits and other damages by the terminated party. Attempts by owners or contractors to "shop around" after executing a contract will not be tolerated. Thus, to avoid liability for breach of contract, owners and contractors should be cautious when exercising their right to terminate under a convenience clause.

By Aman Kahlon

Even Minor Defects in Liens Can Result in Contractors Losing Their Lien Rights

Many areas of the law provide a party who makes an error, whether procedural or substantive, with relief to correct the error, generally under principles of fairness and equity. States' lien laws are often not so forgiving. A defect in a lien, even a minor one, can render a lien invalid. Most state courts strictly interpret statutory procedural requirements for liens. Contractors should be aware that the deadline to file a lien is strict, that a lien with a defect will often not be enforced, and that a defective lien cannot be cured once the deadline has passed.

Because of this strict enforcement, attorneys who notice such defects will wait until after the contractor's lien deadline expires and then move to dismiss the lien. Two recent state court cases, one from Illinois and the other from Kansas, remind us that this scenario can happen in residential and commercial projects involving minor defects in liens.

In *Weydert Homes, Inc. v. Kammes*, a general contractor filed an action to enforce a lien on real property for work and materials performed on the construction of a residence in Sycamore, Illinois. Illinois lien statutes require that before any monies are to be paid on a project, "a contractor must provide to the owner a statement in writing, under oath or verified by affidavit, of the names and addresses of all parties furnishing labor, services, material, fixtures, apparatus or machinery, forms or form work and of the amounts due or to become due." In *Weydert*, the owner requested, and the general contractor provided, such a statement. However, the contractor statement was not verified or given under oath (i.e., notarized). The owner argued that because the Illinois lien statutes are strictly construed, this error, regardless how minor, rendered the lien invalid. The trial court agreed and granted the owner's motion for summary judgment as to the lien claim. On appeal, the Illinois Court of Appeals affirmed, holding that the Illinois lien statutes are to be strictly construed and, therefore, because the contractor's statement was not in strict compliance with the statute, the lien filed by the general contractor was invalid.

The same strict compliance lien requirements are evident in commercial projects. In *National Restoration Co. v. Merit General Contractors, Inc.*, a general contractor on a commercial project in Overland Park, Kansas moved for summary judgment dismissing its supplier's lien because the supplier's lien mistakenly noted the general contractor as "Merit Construction Company, Inc." The general contractor's correct corporate name was "Merit General Contractors, Inc." The trial court granted the general contractor's motion for summary judgment as to the lien claim, and the supplier appealed. The Kansas

Court of Appeals affirmed and held that the supplier had notice of the correct corporate name of the general contractor and, therefore, because Kansas law strictly construes its lien law, the supplier's lien was invalid. Because the supplier's time to file a lien had expired, it was unable to amend its lien, and it lost its lien rights entirely.

Contractors beware – before the start of construction review the relevant lien law and pay close attention to the details to ensure that you preserve your rights. Some states like Illinois and Ohio even require pre-construction notice, and the failure to review the lien law and recognize these requirements prior to project commencement can be fatal. In this economy, with many entities filing bankruptcy and many others in financial distress, a valid lien can determine whether or not you will ever receive payment. Moreover, an invalid lien can be the lever for an owner to argue that a contractor or subcontractor has improperly clouded the owner's title, giving the owner a claim against the lien claimant. Because the risk of filing an invalid lien is significant, contractors should seek advice from a construction attorney before starting construction in a new state and should seek assistance when filing liens to ensure compliance with each state's individual nuances.

By Nick Voelker

Not in the Contract, Not Part of the Deal

A recent case out of New York is a good reminder to all contracting parties to pay particular attention to what is (and what is not) included in the final, executed version of their contracts. Contractors and owners should not rely on documents presented and discussed during negotiations when these documents are not included in the signed contract.

In *Century-Maxim Construction Corp. v. One Bryant Park, LLC*, the concrete trade contractor on a skyscraper project in midtown Manhattan sued the developer and construction manager for acceleration damages. The contractor claimed that the construction manager represented at various pre- and post-bid discussions that the work would be completed in three separate phases. It claimed that the construction manager had presented a schedule which reflected this staged plan for construction. According to the contractor, this schedule showed that concrete work would take between 24-27 months, and it showed sufficient float as well as sufficient periods of slowed or suspended steel erection to allow the contractor to keep pace with steel erection, as it was required to do by New York City code.

The contractor claimed that from the outset of the project, the schedule was delayed six months through no fault of its own. As a result, the schedule was compressed and the periods of slowed or suspended steel erection were removed from the schedule. The concrete contractor claimed that it was forced to accelerate its work to keep pace with the steel contractor. It sought $22 million in acceleration damages.

In response, the construction manager and developer argued that the schedule upon which the contractor relied was not referenced in the contract documents. The contract contained a clause stating that the parties were not relying on any previous conversations, agreements, or documents, other than those specifically mentioned (a merger clause). It also contained provisions which directly contradicted the concrete contractor's allegations regarding the schedule. So, the construction manager and developer argued that this alleged schedule could not be the basis for an acceleration claim.

The concrete contractor's acceleration claims were dismissed. The court held that the contractor was not entitled to rely on a document which was not referenced or incorporated into the contract, especially in the situation where the contractor's allegations regarding this schedule were directly contrary to the plain terms of the contract. This should be a reminder to all owners and contractors to be sure to base your price and plan for construction on the documents which are included in the executed contract. It is a risky proposition indeed to rely on representations made during negotiations of a contract, especially when these representations are not included in the final, executed contract.

By Luke Martin

Site Inspection Clauses: Preventing Loss for Those Unexpected Conditions

Many owners attempt to shift the risk (and extra costs) associated with unexpected project conditions to the general contractor by inserting site inspection clauses in their contracts. Typically, owners provide contractors a preliminary report of the site conditions in bid packages, but include a clause in the subsequent contract stating that the contractor has reviewed and familiarized itself with the project site, is aware of project conditions, and that it assumes full responsibility for any site conditions it may encounter. If there is no "differing site condition" clause in the contract, this provision attempts to push the risk of unknown site conditions to the contractor. The enforcement of these risk shifting clauses has been called into question by a recent case in Texas.

In *Mastec North America v. El Paso Services*, the general contractor who installed a gas pipeline (Mastec) sued the owner (El Paso) for the extra construction costs it incurred because of an excessive number of pipeline crossings These pipeline crossings did not appear on the drawings the owner provided with the bid package and resulted in almost five million dollars in extra costs. The owner defended the lawsuit by relying on clauses it included in the contract with the contractor which stated that the contractor was familiar with the pipeline route, including all subsurface conditions, and that the contractor agreed to construct the pipeline for a lump sum price regardless of the conditions it encountered. The trial court agreed with the owner and dismissed the case because the contractor had assumed the risk of subsurface conditions and therefore was not entitled to be reimbursed for the cost associated with the pipeline crossings.

The appellate court took a broader view and focused on the owner's representation that it had exercised due diligence to locate any pipeline crossings in the bid documents, which, in actuality, grossly misrepresented the number and location of pipeline crossings. The court also made the determination that the owner was in a much better position to determine the number and location of pipeline crossings. Thus, it reversed the trial court and ordered the owner to reimburse the contractor for the extra installation costs it incurred, despite the risk shifting site inspection clause. The court also indicated that it may be willing to take its logic a step further in the future and find that risk shifting site inspection clauses may not protect the owner when the bid documents misrepresent the nature and amount of the work to be performed.

Risk shifting site inspection clause will likely remain a contentious point between contractors and owners. Special attention should be given to such clauses and hidden conditions to proactively limit the potential problems for both owners and contractors. However, problems will arise because of site conditions and when they do, remember that a risk shifting site inspection clause may not provide the final answer, particularly where the owner makes an affirmative representation, in the contract itself, about a condition or fact which is material to the contract.

By Bryan Thomas

Bradley Arant Lawyer Activities:

Jim Archibald, **Axel Bolvig**, **Doug Patin**, **David Pugh**, **Bill Purdy**, **Mabry Rogers**, **Wally Sears**, and **David Taylor** are named in the 2010 edition of *The Best Lawyers in America* in the specialty of Construction Law.

Axel Bolvig, **Rick Humbracht**, **David Hymer**, **Joe Mays**, **Doug Patin**, **Bill Purdy**, **Mabry Rogers, Wally Sears**, and **David Taylor** have been selected as Super Lawyers 2010 for Construction.

Jim Archibald and **Wally Sears** recently updated the Alabama section of the *State-by-State Guide to Construction Contracts and Claims*.

Keith Covington published an article entitled "Court Revives OSHA's Multi-employer Citation Policy" in the October/November 2009 edition of the *Alabama Construction News*.

Keith Covington was also published in the November 2009 edition of the *Construction Business Owner*.

The article is entitled "E-Verify Now Required for Federal Contractors."

David Taylor's article on Tennessee's retainage law, "Tennessee Retainage Law: Ignore at Your Peril," was published in the January edition of Tennessee Bankers Magazine.

David Taylor's article on dispute resolution entitled "Arbitrating and Mediating Real Estate Disputes" will be published in the March edition of the Institute of Real Estate Management Magazine.

BABC co-hosted the ABC Economic Forecast seminar, titled "2010 Economic Forecast: Where the Projects Are" on October 22, 2009.

Mabry Rogers Attended Princeton University Symposium, "Managing the Challenges of Scarcity: The Critical Path for Global Construction," on November 5-6, 2009.

Keith Covington spoke on November 6, 2009 at the Home Builders Association of Alabama Conference concerning 'Chinese Drywall'.

David Taylor facilitated a 'Construction Financing' meeting of bankers, developers, subcontractors, and general contractors in Nashville on November 12, 2009.

David Taylor recently chaired and spoke at a Tennessee Bar Association seminar entitled "Arbitrating and Mediating Construction Disputes".

Arlan Lewis, Rhonda Caviedes, and **Ed Everitt** recently participated in the ABA Forum on the Construction Industry's mid-winter conference in San Francisco entitled "Government Construction Contracting."

Ed Everitt's article "Mississippi Lien and Bond Law; Make Sure You Know Your Rights," was published in the First Quarter 2010 edition of Construction Mississippi, a special publication of the Mississippi Business Journal.

Bill Purdy, **Wally Sears**, and **Mabry Rogers** attended the annual meeting of the American College of Construction lawyers in San Diego in February. Bill is Program Chair for the meeting to be held in February, 2011.

David Taylor and **Bryan Thomas** will be presenting a session entitled "The Great Debate: Do You Arbitrate" at the national CONSTRUCT 2010 meeting in Philadelphia in May 2010.

It is with mixed emotions that we report that **Jeremy Becker-Welts** and **Mitch Mudano** have left Bradley Arant Boult Cummings. We would like to thank Jeremy and Mitch for their years of service and for the time they dedicated to the firm and its construction clients. We wish both of them the best of luck in their new endeavors.

We would also like to welcome **Aman Kahlon and Avery Simmons** to the firm's construction practice Group. Aman is practicing in our Birmingham office and Avery is practicing in our Charlotte office.

For more information on any of these activities or speaking engagements, please contact Terri Lawson at 205-521-8210.

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NOTES

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CGL Policies Cover Subcontractor Defects in Mississippi

The Mississippi Supreme Court recently settled a significant question regarding insurance coverage on construction projects in Mississippi. In *Architex Association, Inc. v. Scottsdale Insurance Co.*, the court ruled that a general contractor's Commercial General Liability (CGL) policy provides coverage for property damage caused by a subcontractor's defective work, thus bringing Mississippi in line with a growing majority of states which recognize that defective construction may constitute an 'occurrence' under a CGL insurance policy.

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The case arose out of the construction of a Country Inn and Suites in Pearl, Mississippi by Architex Association, Inc. (Architex), the general contractor. Architex hired various subcontractors to perform different aspects of the work. A dispute arose at the end of the project between Architex and the owner, with the owner withholding payment and alleging that Architex and its subcontractors caused property damage by knocking off a false chimney during construction (causing water damage) and failing to install adequate rebar in the foundation concrete. Architex notified its CGL carrier, Scottsdale, of the owner's claims, but Scottsdale declined to provide a defense or coverage under the policy, stating that there had not been an 'occurrence' which would trigger coverage. Architex then filed a third party complaint against Scottsdale for its failure to defend and indemnify under the CGL policy.

In Architex's suit against Scottsdale, the trial court granted summary judgment to Scottsdale, finding that there had been no 'occurrence' under the policy language because Architex's intentional act of hiring subcontractors set in motion the chain of events that led to the defective work. Previous Mississippi cases interpreting CGL policy language (not in the construction defect context) held that an 'occurrence' does not exist where the insured intentionally sets in motion the chain of events that lead to the property

damage. In the construction context, however, this rule can lead to inconsistent and confusing results, as it did in this case. Certainly the act of hiring a subcontractor should not preclude the possibility for CGL coverage. In many instances, hiring a subcontractor is absolutely necessary due to the need for a contractor with specialized knowledge and skill in a specific area, such as an insulator or an electrician.

The Mississippi Supreme Court reversed the trial court. The Court started its analysis by recognizing the purpose of a CGL policy—it is "designed to provide liability protection for the general contractor and [its] subcontractors for accidental, inadvertent acts which breach accepted duties and proximately cause damage to a person or property." The Court decided that an interpretation of Architex's CGL policy that precluded coverage for a subcontractor's defects would undermine the plain language and purpose of the CGL policy altogether. Accordingly, the Court held that the policy covered property damage caused by a subcontractor's defects.

Architex is a win for the entire construction industry because it makes clear that the hiring of subcontractors on a project will not negate coverage under a CGL policy. It makes clear that a claim of defective work by a subcontractor falls within the broad grant of coverage initially afforded by a CGL policy. However, it is important to note that the ruling does not address whether or not such coverage might be excluded under one of the CGL policy exclusions. The fact pattern of every case is different and ultimately must be evaluated in light of the applicable policy language and exclusions to determine whether coverage exists.

By Ed Everitt

Contractor Loses Big on Hurricane – *Force Majeure*

The federal appeals court which supervises the trial courts in Georgia, Florida, and Alabama has ruled—as a matter of law (thus, no trial, no discovery)—that a contractor could not win in its efforts to obtain compensation for *force majeure*, labor shortage, and contract interference claims. The appeals court extended its ruling in an earlier case involving the construction of a Marriott Hotel in south Florida, in applying very harsh risk-shifting provisions of the owner-contractor contract.

The case, *S&B/Bibb Hines PB 3 Joint Venture v. Progress Energy Florida, Inc.*, involved two power plants in Polk County, FL. During the project, four hurricanes struck the job. The contractor finished on time, but sought compensation for the impacts from these hurricanes. It argued that the hurricanes created job shortages and other damages that entitled it to extra compensation.

The court disagreed, citing the *force majeure* clause as expressly disallowing any compensation for such events, and reinforced its decision by citing the "no damages for delay" provision as shifting the risk of delay to the contractor. The court was clear that the owner could have allowed a change order for the hurricanes to the contractor but had no obligation to do so. Because the Owner did not have an obligation to issue a change order, the owner could not be in violation of its implied obligation to act in good faith in administering the contract.

The decision underscores the willingness (and enthusiasm) with which the particular appeals court applies typical risk-shifting clauses in Florida construction contracts, and applies them favorably to owners and against contractors. As the court put it in this case (and in several earlier Florida law cases), "[the contractor] could have increased its prices to reflect the risks it was assuming."

By E. Mabry Rogers

Failure to File a Timely Lawsuit Results in Contractor's Loss

The law requires that claims be brought in a timely manner. The failure to do has a harsh result – no recovery. The specific time period for bringing a claim varies. Because of a misunderstanding of the applicable time limitation and despite a potentially valid claim against the engineer, a Georgia contractor recently suffered this result when it waited more than four years to file a lawsuit against the engineer.

The Georgia Court of Appeals took up the issue of whether a four (4) year statute of limitations for professional malpractice or a six (6) year statute of limitations for breach of contract applied to an owner's breach of contract claim against an engineer for failure to provide competent, professional design and engineering services. In *Jordan Jones and Goulding, Inc. v. Newell Recycling of Atlanta, Inc.*, the Georgia Court held that, although the owner's ("Newell"), claim was couched as one for breach of contract, it was actually a claim for professional malpractice based upon the engineer's ("JJ&G") alleged breach of its contractual duties to provide competent, professional design and engineering services. Therefore, the four (4) year statute of limitations for professional malpractice, not the six (6) year statute of limitations for breach of contract, applied to bar Newell's action against JJ&G.

Newell purchases and processes scrap metal, which it then resells. In 1997, Newell contacted JJ&G regarding design and engineering services for a new automobile shredding facility it wanted to build. Work was completed on the project in September 1999, and in May 2000, Newell informed JJ&G that the pavement around the shredding machine was cracking. In August 2004, Newell sued JJ&G, claiming that JJ&G failed to perform its services with that degree of care, skill, and ability ordinarily expected of a prudent design professional and engineers of similar circumstances.

JJ&G argued that Newell's Complaint asserted a claim for professional negligence, breach of an oral contract or breach of a contract partly written, all of which have a four (4) year statute of limitations in Georgia. The trial court disagreed.

The Court of Appeals reversed, reasoning that the Complaint demonstrated a professional malpractice claim, and all such malpractice claims are governed by the four (4) year statute of limitations.

Each state has its own statute of limitations periods for various causes of action, including case law that may interpret which limitations period applies to a particular set of facts. For this reason, consult an attorney early on to determine when the deadline expires to bring claim under the applicable state law. By failing to do so, you could end up like Newell in this case and be time-barred from bringing an action.

By David Hill Bashford & Nick Voelker

GC's Stinky Sinkhole Indemnity Claim Fails

The Tennessee Court of Appeals recently addressed a not uncommon liability scenario for a construction defect. The owner sued the general contractor, and the general contractor sued the supplier. Unfortunately for the GC, the third-party claim was barred by contractual limitations in the supply contract. The court in *Baptist Memorial Hospital v. Argo Construction v. Hanson Pipe and Products South* thus held that the GC was on its own with its smelly sinkhole problem.

The owner-hospital discovered a sinkhole in its parking lot after the completion of a sewage drainage project. It sued the GC which in turn sued the pipe supplier because it discovered that the internal steel reinforcement for the concrete pipe used in the project was incorrectly positioned. The supplier successfully based its refusal to indemnify upon the express limitations in its supply contract. The GC sued the supplier for *implied* or *equitable* indemnity. In other words, the GC's claim was not based upon the supply contract. The GC maintained that the time period for asserting the implied indemnity claim began to run when the defect was discovered – that is, when the sinkhole started to smell. The supplier argued instead that its supply contract stated that the supplier provided a one-year warranty from delivery only, and that the warranty provided for repair, replacement, or refund only. The supplier thus could not be liable for a general damages claim brought by the owner-hospital outside of one year.

In upholding judgment for the supplier, the Tennessee Court of Appeals first held that the GC could not bypass the supply contract's limitations by simply asserting an implied or equitable (noncontractual) indemnity claim rather than asserting a claim for indemnity under the contract itself. Second, it upheld the remedy provision in the supply contract (the one-year warranty), finding the provision did not "fail in its essential purpose" simply because a defect might

not be discovered within the one-year warranty period (as occurred in this case).

The *Baptist* case emphasizes the need for careful review of supply contracts. Ordinarily, one should be wary of an "exclusive" remedy provision in the warranty clause. In situations in which a product failure reasonably cannot be discovered for a time period well beyond the date of delivery, a contractor should consider and negotiate for the express warranty as an additional remedy, in order to obtain a less stinky result than what the GC received here.

By John Hargrove

Major Provisions of the Patient Protection and Affordable Care Act and their Impact on the Construction Industry

The Patient Protection and Affordable Care Act passed by the current Congress and signed into law by President Obama will reportedly cost $940 billion over the next ten years; will expand coverage to 32 million Americans who do not currently have coverage; and may bring some hospital expansion projects across the country to a screeching halt.

Many of the effects of the health care reform legislation impact the construction industry just like other industries. Construction companies with more than 50 employees will be mandated to provide health insurance coverage or pay a fine in most cases, and construction company owners and employees will be subjected to the same tax increases as other Americans.

The first impact of the new law will be felt by small employers, who will begin receiving a tax credit for insurance costs. Companies with ten or fewer employees making $20,000 or less on average will be eligible for a 50% tax credit on health insurance costs. The credit is phased out for employers who do not meet the size and income thresholds by a formula which takes into account both factors. The credit is completely phased out for employers with more than 25 employees or whose employees' average annual wages exceed $40,000.

In order to facilitate the provision of additional health insurance coverage to millions of Americans, the new law requires that by 2014, all 50 states will have to set up Small Business Health Options Programs or "SHOP Exchanges." These organizations will be used to allow employers with less than 100 employees to pool together to buy insurance. The intent is to reduce costs for coverage by spreading the risk within larger groups. Until the SHOP Exchanges are established, tax credits are available for some small businesses.

Beginning June 21, 2010, individual and group health insurance plans will no longer be able to exclude pre-existing conditions from coverage. Also beginning June 21, 2010, the government will begin a temporary program to reinsure the cost of providing health insurance to early retirees (ages 55 to 64) and their families.

Beginning September 23, 2010, the law will prohibit limitations of the amount of coverage available to an individual in a single year or for a lifetime.

In 2011, the law requires that all W-2's report the value of the health insurance coverage provided to each employee. This will not result in additional tax to the employer or employee at that time, but the reporting requirement may offer a step to taxing health insurance benefits provided by employers.

Specific to the construction and healthcare industries, the health care reform legislation will affect physician-owned hospital projects that are either currently underway or planned for the future.

At present, there are approximately 260 physician-owned hospitals in the United States, and approximately 58 have expansion plans either under construction or on the books. The new laws restrict physician-owned hospitals from adding beds, procedure rooms, or operating rooms. The legislation also reduces Medicare reimbursement for physician-owned hospitals. The congressional reasoning for this prohibition is to prevent doctors from referring the "better" patients to their hospitals or steering them away from public hospitals.

The legislation includes a narrow exception allowing the Secretary of Health and Human Services to

establish a process to apply for an exception to the new law. The community in which the hospital is located must be given input in that exception process. While an exception to this rule is good news, the Secretary is not required to develop and implement the process to obtain an exception until August 1, 2011. The new legislation offers no clear answers for physician-owned hospitals with ongoing expansion projects and has reportedly caused the abandonment of 60 additional community hospitals which will no longer be built, an ironic result of legislation intended to increase access to healthcare.

If you have a construction project affected by the effective hold, you may want to consult your lawyer regarding the exception above, how to apply for it, and whether the process can be expedited.

By Rob Dodson

Contingent Payment Clauses: Know Your State's Policy

A contingent payment clause (sometimes known as a "pay-when-paid" or "pay-if-paid" clause) is a clause which conditions downstream payment to a subcontractor or sub-subcontractor on receipt of payment from the upstream contractor or owner. Thus, in the typical owner-contractor-subcontractor relationship, if a contractor has not been paid by the owner for work performed by the subcontractor, the contractor has no obligation to pay its subcontractor. The interpretation and enforceability of such "contingent payment" clauses varies from state to state. Recently, The United States Court of Appeals for the Fourth Circuit confirmed that, in Virginia, unambiguous pay-when-paid clauses are valid conditions to payment to lower-tier contractors.

In *Universal Concrete Products Corp. v. Turner Construction Company*, the general contractor included an *express* pay-when-paid clause in its subcontract with its concrete subcontractor. This clause made payment from the owner to the general contractor an *express* "condition precedent" to payment from the general to its subcontractor.

When the subcontractor substantially completed its work in March, 2008, the real estate market had soured. The owner did not pay the general contractor, and, as a result, the general contractor did not pay the subcontractor. When the subcontractor sought payment for its work, the general contractor refused, citing the pay-when-paid provision in the subcontract.

The subcontractor sued alleging that the pay-when-paid clause was ambiguous and therefore should only be interpreted as setting the time for payment (a concept adopted by some state courts). The Court rejected this argument, reasoning that the pay-when-paid clause was unambiguous and, because it is the policy of Virginia courts to allow parties to form contracts without government interference, the clause was to be enforced, barring the subcontractor from recovery from the general contractor.

The court's decision is good news for general contractors in Virginia and bad news for lower tier subcontractors. For those outside Virginia, the court's decision is a reminder to general contractors and subcontractors to perform due diligence prior to contract negotiations. General contractors which want to include contingent payment clauses in their contracts should determine beforehand how the respective state's courts interpret and enforce such provisions. Some states require specific "condition precedent" language in the clause before they will enforce the clause as written; some interpret the clause as a timing mechanism requiring payment after a reasonable time, even if the owner does not pay the general contractor; others will not enforce contingent payment clauses at all. Likewise, subcontractors should be aware of the implications of contingent payment provisions, especially in this market where owners are facing difficulties obtaining financing for their projects.

By Jonathan Cobb

Bradley Arant Lawyer Activities:

Jim Archibald, **Axel Bolvig**, **Doug Patin**, **David Pugh**, **Bill Purdy**, **Mabry Rogers**, **Wally Sears**, and **David Taylor** are named in the 2009 edition of *The Best Lawyers in America* in the specialty of Construction Law.

Jim Archibald and **Wally Sears** recently updated the Alabama section of the *State-by-State Guide to Construction Contracts and Claims.*

David Taylor's article on dispute resolution entitled "Arbitrating and Mediating Real Estate Disputes" was published in the March edition of the Institute of Real Estate Management Magazine.

Jim Smith hosted a seminar on February 26, 2010 sponsored by the Mecklenburg County Bar Association entitled "Technology in the Courtroom: Making Your Case Come Alive."

Bob Symon recently conducted five Seminars on the Federal Acquisition Regulation (FAR). On March 5, 2010 he presented in Washington, DC; on March 9, 2010 he presented in San Diego, CA; on March 11, 2010 and March 26, 2010 he presented in Rockville, MD; and on May 5, 2010 he presented in Brentwood, TN.

Joel Brown presented a teleconference on March 12, 2010 entitled "AIA Doc. A401 Subcontract Doc. (Intellectual Property Rights)."

Mabry Rogers and **David Bashford** have recently presented risk management seminars in Raton, NM, Boulder City, NV, and Tempe, AZ, and **Mabry** presented recently an overview of federal contracts seminar in Ft. Lauderdale, FL.

Joel Brown and **David Taylor** presented a seminar entitled "Bidding Requirements in Federal Contracting" on March 25 for the Tennessee ABC in Nashville, TN

David Taylor presented a "Legal Issues for Management" training class on April 1 for the Tennessee ABC

Stanley Bynum attended the ABA International Law Spring Meeting April 14th -17th in New York, NY.

David Taylor presented a seminar entitled "Tennessee Retainage Laws" on April 7 for the Tennessee AGC in Nashville, TN

David Taylor presented a seminar entitled "What to do When Your Commercial Contractor Stops Working" as part of Bradley Arant Boult Cumming's 9th Annual Commercial Real Estate Seminar on May 9 in Nashville, TN

Joel Brown presented a seminar in Huntsville, AL on May 13, 2010 for the Defense Acquisition University concerning government contracts and intellectual property rights.

David Taylor and **Bryan Thomas** presented a session entitled "The Great Debate: Do You Arbitrate" at the national CONSTRUCT 2010 meeting in Philadelphia on May 14, 2010.

David Pugh, Michael Knapp, Arlan Lewis, Luke Martin, Ed Everitt and Jonathan Cobb will present a seminar entitled "Fundamentals of Construction Contracts" on June 24, 2010 in Birmingham, AL.

David Taylor recently authored an article entitled "Road to Resolution – How ADR can Help Avoid Conflict Disputes" which was published in the March/April edition of Journal of Property Management

Arlan Lewis, Rhonda Caviedes, and **Ed Everitt** participated in the ABA Forum on the Construction Industry's mid-winter conference in San Francisco entitled "Government Construction Contracting."

For more information on any of these activities or speaking engagements, please contact Terri Lawson at 205-521-8210.

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BRADLEY ARANT BOULT CUMMINGS LLP **Third Quarter 2010**

CONSTRUCTION AND PROCUREMENT LAW NEWS

Recent federal, state, and local developments of interest, prepared by the firm's Construction and Procurement Group:

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Federal Circuit Raises the Stakes for Contract Disputes Act Claims

The federal appeals court that supervises all contract claims against the United States recently expanded the risk of failing to properly seek a formal extension of time under the Contract Disputes Act ("CDA"). In *M. Maropakis Carpentry, Inc. v. United States*, the Court of Appeals for the Federal Circuit held that a contractor's failure to submit a valid CDA claim for a time extension not only prevented the contractor from pursuing a contract modification but also barred the contractor from presenting factual defenses to the government's claim for liquidated damages.

In *Maropakis*, the contractor failed to complete the renovation of a U.S. Navy facility in accordance with the terms of the contract and argued that the government caused the bulk of the 467 day delay. Three months after completing the project, the contractor sent a letter to the contracting officer ("CO") requesting a contract modification for an extension of time due to the government's delays. The CO rejected the claim, asked for additional information, and specifically stated that the rejection was not a Final Decision. The contractor did not submit additional information. Ten months later the CO again wrote to the contractor, pointed out that the contractor never provided additional information in support of the extension request, and stated that due to the delay, the government was entitled to over $300,000 in liquidated damages. The parties exchanged letters again without the contractor providing any additional information to support its excusable delay claim. Subsequently, the CO issued his Final Decision on the liquidated damages assessment. The contractor then filed suit seeking a time extension due to government delays and seeking elimination of the liquidated damages assessment. The government counterclaimed for liquidated damages.

The court ruled for the government on all counts. First, the court held that the contractor never submitted a valid CDA claim seeking time extensions. While there is no specific format for a CDA claim, a valid claim requires

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notice of the basis for the claim, the amount of the claim, and a request for a final decision from the contracting officer. Because the contractor never provided this information to the CO in support of its claim for a time extension, it never submitted a valid CDA claim. Thus, the court held that it did not have the legal authority to consider the contractor's claim seeking a contract modification for an extension of time.

The scope of the court's rejection of Maropakis' CDA claim went far beyond rejecting its affirmative claim. The court also held that because it could not consider the contractor's claim for the time extension, the contractor could not present any factual evidence of the government's delays in defense of the government's counterclaim for liquidated damages.

The implications of this far-reaching opinion are significant. Now, in all contract disputes before the Court of Federal Claims or the Boards of Contract Appeals, a contractor can be deemed to have waived its ability to present certain factual defenses by failing to recast and properly submit these facts in a formal CDA claim. At a minimum, if a contractor believes that the government may pursue liquidated damages and it if believes it has valid grounds for a time extension (compensable or excusable), it must submit a proper CDA claim for a time extension to preserve the right to present evidence of government delays in any future court proceedings.

By Lewis Rhodes

Prime Contractors on Federal Projects Beware: Big Penalties for Providing False or Inaccurate Certified Payrolls to the Government

The federal government recently was awarded $1,661,423.13 in damages against a prime contractor who submitted false certified payrolls to the government on a federal project. In *United States of America v. Circle Construction, LLC*, the federal trial court held that because Circle Construction, LLC ("Circle"), the prime contractor, submitted false certified payrolls in violation of the Davis Bacon Wage Act and False Claims Act, the government was entitled to three (3) times the amount it would not have paid Circle had it known about the false certified payrolls.

The case arose from the construction of various buildings on the Fort Campbell military facility in Clarksville, Tennessee. Circle subcontracted with Phase Tech for the electrical work on the Project. After the Project was complete, an employee of Phase Tech filed an action alleging that Circle submitted false certified payrolls to the government throughout the Project.

Circle's prime contract with the government, and applicable federal law, obligated Circle to pay electricians according to the wage determinations in the contract, submit payroll certifications to the government as a condition for payment, and ensure that all subcontractors on the Project submit complete and accurate certified payrolls. After an extensive investigation by the government, it was discovered that Circle provided roughly 62 false or inaccurate certified payrolls throughout the Project, many of which failed to list any Phase Tech employees. Moreover, the government found that Phase Tech employees were paid significantly less than the wage determination Circle agreed to in the prime contract. The Court noted that the Davis-Bacon Wage Act certified payroll requirement is designed to give local laborers and contractors fair opportunity to participate in federal projects and protect local wage standards by preventing contractors from basing their bids on wages lower than the prevailing wage in that area. The Court concluded that Circle's conduct was a direct attempt to pay a lower wage to Phase Tech employees than the prevailing wage in that area. The Court ruled that the contractor's false statement only needed to be material to the government's payment decision. In this case the Court reasoned that the government would not have paid Circle had it known Circle was submitting false certified payrolls.

Prime contractors on federal projects must ensure that any subcontractors on the project are submitting accurate certified payrolls. As this case demonstrates, if a prime contractor fails to do so the penalties for submitting false or inaccurate certified payrolls could be significant.

By Nick Voelker

"No Damage for Delay" Clause Means No Problem for Government

In *Harper/Neilsen-Dillingham, Builders, Inc. v. United States*, the United States Court of Federal Claims recently held that "no damage for delay" clauses contained in contacts between subcontractors and prime contractors bar pass-through delay claims to the government (under the so-called 'Severin Doctrine'), provided the clause is enforceable against the subcontractor under applicable state law.

Harper was one of several prime contractors performing work to construct residential housing for the government. Harper was delayed in commencing its work, and had to perform its work out of sequence because other prime contractors were late in completing their work. This had the effect of forcing Harper's subcontractor, KCI, to perform its landscaping work during the winter and to encounter severe weather delays.

However, when KCI and Harper executed the subcontract, KCI was already aware that the work would have to be performed in the winter. Therefore, in the Court's words, "the delays complained of in this case occurred prior to the subcontract award and were therefore within the contemplation of the parties at the time they entered into the subcontract." Moreover, the subcontract contained a standard no damages for delay clause: "In the event of any delays, entailed as a result of fault of Contractor or Owner, then Contractor shall grant Subcontractor an extension of time equal to the delay and Subcontractor shall be entitled to no other or further damages against Contractor or Owner."

In eventually holding that the pass-through claim was barred, the Court first recited the rule that, to succeed on a pass-through claim against the government, the prime contractor must show that it is liable or potentially liable to the claiming subcontractor vendor. The Court further held that to defeat such a claim, the government must show "an *iron-bound release or contract provision immunizing the prime contractor completely from any liability to the sub.*" Under California law, the Court found that the no damages for delay clause was sufficient to defeat the subcontractor's delay claim. In addition, the Court held that even assuming that the "no damages for delay" clause did not bar the subcontractor's delay claim, the prime contractor still did not have any liability to the subcontractor because the delays were in the contemplation of the parties at the time of contracting.

In summary, while the holding of *Harper* may provide broad protection for the government against pass-through liability for claims barred under relevant subcontract provisions, it leaves some room for future pass-through claims seeking damages for delay, even where the subcontract includes a "no damages for delay clause." Specifically, any state law exceptions to the enforceability of such clauses, if properly supported by the requisite facts, would allow the prime contractor to pass through the subcontractor claim. Additionally, *Harper* did not rule out the possibility that a properly drafted liquidation agreement could solve the problem at issue in *Harper*. Finally, it remains to be seen if the breadth of the clause at issue, which is a bit unusual in that it included the "owner" in the protection of the "no damages for delay" clause, may prove to be a distinguishing factor.

By Tom Lynch

The Importance of Reviewing and Understanding Governmental Permitting Documents and Pursuing Administrative Remedies

The Supreme Court of Indiana recently issued a decision which highlights the importance of carefully reviewing – and fully grasping the implications of – governmental permitting documents. In *Carter v. Nugent Sand Company*, the court ruled that a lawsuit filed by a sand and gravel stockpiling and transporting company (Nugent Sand) was due to be dismissed because the company failed to exhaust certain administrative remedies as required under certificates of regulatory approval obtained from the Indiana Department of Natural Resources (IDNR). As a result, Nugent Sand was left with no way to challenge IDNR's stance that a man-made lake used for the company's operations and a channel excavated by the company to connect the lake with the Ohio River were open to full use by the general public.

As part of its commercial barge operation, Nugent Sand leased 156 acres of land adjoining the Ohio River in Utica, Indiana. This land included a fifty acre man-made lake which stood approximately 200 feet inland from the river. In 2000, Nugent Sand obtained the required governmental permits, including the certificates of regulatory approval from the IDNR. Nugent Sand then spent substantial sums of money excavating a channel so that the lake and channel could be navigated by tugboats and barges up to 195 feet long and 35 feet wide. The company also constructed a dock in the man-made lake for unloading the barges.

Recreational boaters began using the lake through the excavated channel, creating traffic problems and safety hazards for Nugent Sand's operations. Nugent Sand turned to IDNR for assistance, complaining that the recreational boating was interfering with its operations, driving up its costs, and jeopardizing the safety of its employees and the public-at large. IDNR took the position that the lake and the channel were public, refused to take action, and even provided statements that the waters were public in response to public inquiries.

Nugent Sand filed a lawsuit against IDNR, seeking a declaration that the channel and the lake were private property and an injunction to prevent IDNR from issuing statements that the waters were open to the public. The trial court entered a permanent injunction in Nugent Sand's favor.

The Indiana Supreme Court reversed the trial court because Nugent Sand had not properly exhausted its administrative remedies as set forth in the excavation permit. The Supreme Court noted that "the terms imposed by IDNR, 'requiring all additional waters created by this project be dedicated to the public as required under IC-14-29-4,' were explicitly set forth in the 'Special Conditions' section of the approval documents" issued by IDNR prior to the channel excavation. The Court also pointed out that the approval documents contained provisions notifying Nugent Sand about the administrative procedures under which it could appeal any condition on the excavation contained in the permits. Those procedures specifically gave Nugent Sand the right to request IDNR "to interpret a statute or rule administered by the [IDNR] as applicable to a specific factual circumstance" and, if aggrieved by the response, to file a petition for administrative review under provisions of the Indiana Code. Because Nugent Sand had not exhausted its administrative remedies under those provisions to challenge the public access condition in the excavation permits, it was not entitled later to seek judicial relief.

The obvious reminder: review and understand the conditions in governmental permitting documents. The failure to see and appreciate the traps that may exist in these permits can result in unanticipated costs, negative operational impacts, and (as this case demonstrates) even the inability to seek legal relief.

By Keith Covington

Modified Total Cost Recovery and Owner's Warranty of the Plans and Specifications

For construction of the Hyperion Wastewater Treatment Plant, the City of Los Angeles obtained millions of dollars worth of construction from Dillingham-Ray Wilson (DRW) and its subcontractor, CBI Services, that it did not want to pay for. When the city was sued for failure to pay for this work, the trial judge excluded from the jury's consideration $25 million of damages, and the jury awarded the contractor $12.4 million for the claims and damages it was allowed to consider, in addition to $23 million in interest, prompt payment penalties, and lawyers' fees ($6.6 million total in lawyers' fees). On March 18, 2010, an intermediate appellate court in California affirmed the jury's verdict, and reversed the trial court as to excluding the $25 million of damages from the jury's consideration. It made two important rulings of general interest to the construction industry.

First, the trial court excluded the $25 million because DRW and CBI were not prepared at trial to show the "actual costs" of the changes. DRW and CBI argued that the City ordered them to proceed on disputed change orders and made it impossible to keep up with the "actual costs" of the changes. Moreover, they pointed out that the City at times agreed to certain change orders based upon the City's "engineering estimates" of what work should have cost, as opposed to actual costs. Based upon this showing, the intermediate court concluded that the trial court was wrong to exclude DRW's and CBI's cost evidence. The case was remanded to allow them to prove the costs of the change orders through engineering estimates or through the "modified total cost" method of pricing, so long as those are the "best evidence of damages available." In memorable language that is often overlooked by parties opposing damage claims, the court stated: "When it is clear that a party suffered damages, the fact that the amount of damage may not be susceptible of exact proof or may be uncertain, contingent or difficult of ascertainment does not bar recovery."

Second, the trial court also refused to allow DRW and CBI to proceed using a breach by Los Angeles of the implied warranty of the correctness of the plans and specifications (a concept often referred to as the *Spearin* doctrine). Again, the appellate court reversed, concluding that California law recognized such claims.

While the DRW case may be appealed yet again, it nevertheless is a reminder that Contract damages may be proved in less than precise methods, if the fact of damage is clear. Moreover, where there are numerous changes during construction, the entity ordering the changes (owner, general contractor, or subcontractor) may be liable to the claiming tier below based upon not only the changes clause (what is sometimes called "under the contract") but also upon the theory that the ordering entity breached the implied warranty of the adequacy of the plans and specifications ("arising out of the contract"). Of course, regardless of the theory, the claiming entity is entitled to be paid only once for the same damages.

By Mabry Rogers

New "Transparency Act" Reporting Requirements under the FAR

On July 8, 2010, the FAR Council created a new rule implementing the requirements of the Transparency Act. The purpose of this rule is to disclose information regarding subcontracts and salaries of certain employees. These new regulations can be found in FAR 4.41 and FAR Clause 52.204-10. These are completely new rules. There was an existing pilot program established in 2008 that was limited to contracts over $500,000,000 and subcontracts greater than $1,000,000. The new requirements are much broader and eventually will attach to ALL contracts and subcontracts $25,000 or higher.

FAR clause 52.204-10 requires that by the end of the month following the month of the award, ALL first-tier subcontracts with a value of $25,000 be reported at www.fsrs.gov according to the procedures laid out in FAR Clause 52.204-10(c)(1). Furthermore, by the end of the month after the prime contract award – *and annually afterwards* – the contractor has to report the total compensation of each of the five most highly compensated executives for the contractor's most recently completed fiscal year, but only if:

1) The contractor received 80% or more of its annual gross revenues from Federal Contracts; AND

2) $25,000,000 or more gross revenue from Federal Contracts; AND

3) The contractor is not a publicly traded company publishing this info under the security acts.

The contractor must also report the five highest paid employees of its first-tier subcontractors if the subcontractor meets all of these same three requirements.

This rule making creates a new clause that will be inserted into NEW contracts; however, the rule requires existing ID/IQ contracts to be modified to include the new reporting clause. We have also seen at least one instance where the contracting officer modified an existing contract to include FAR Clause 52.204-10. This modification is a unilateral modification and does not need to be signed by the contractor. Thus, contractors need to be on the lookout for a modification adding this clause.

This rule is both an interim rule and a proposed rule making. Under the first phase, from now until September 30, 2010, only prime contracts $20,000,000 and higher are required to follow the reporting procedures in FAR Clause 52.204-10. Beginning October 1, 2010, all prime contracts of $550,000 or higher have to report the required sub-contract and salary information. Beginning March 1, 2011, absent a change in the rule, all contracts $25,000 and higher will be governed by the reporting rules.

The FAR Council is accepting comments on the rule until September 7, 2010. Information on how to comment on this rule is available at www.regulations.gov by entering "FAR Case 2008-039" as the keyword. For further information about this proposed rule or about commenting on this rule, feel free to contact one of the government contracts lawyers at Bradley Arant Boult Cummings.

By Lewis Rhodes

Bradley Arant Lawyer Activities:

Mabry Rogers has been named in the International Who's Who of Construction Lawyers 2010. This is published by the ABA Section of International Law.

Jim Archibald and **Wally Sears** recently updated the Alabama section of the *State-by-State Guide to Construction Contracts and Claims.*

Mabry Rogers and **David Bashford** recently presented contract and risk management seminars in Raton, NM, Boulder City, NV, Sarnia, Ontario and Tempe, AZ, among others.

David Taylor presented a seminar entitled "Tennessee Retainage Laws" on April 7 for the Tennessee AGC in Nashville, TN

Stanley Bynum attended the ABA International Law Spring Meeting April 14th - 17th in New York, NY.

David Taylor presented a seminar entitled "What to do When Your Commercial Contractor Stops Working" as part of Bradley Arant Boult Cumming's 9th Annual Commercial Real Estate Seminar on May 9 in Nashville, TN

Joel Brown presented a seminar in Huntsville, AL on May 13, 2010 for the Defense Acquisition University concerning government contracts and intellectual property rights.

David Taylor and **Bryan Thomas** presented a session entitled "The Great Debate: Do You Arbitrate" at the national CONSTRUCT 2010 meeting in Philadelphia, PA on May 14, 2010.

Jonathan Head co-presented a national webcast on June 3, 2010 for DRI regarding privilege and its effect on major litigation.

David Pugh, Michael Knapp, Arlan Lewis, Luke Martin, Ed Everitt and Jonathan Cobb presented a seminar entitled "Fundamentals of Construction Contracts" on June 24, 2010 in Birmingham, AL.

Jonathan Head participated in a panel discussion at the Alabama State Bar annual conference on July 16, 2010 about Alabama's new electronic discovery rules and responses to common problems in electronic discovery.

Michael Knapp taught a course entitled "International Construction Contracts and Law" at Misr University of Science and Technology in Cairo, Egypt from July 24 to July 28th to graduate level engineering students**.**

David Taylor presented at an annual project managers meeting regarding "Dispute Avoidance" on August 4, 2010

Bob Symon will be presenting seminars on the Federal Acquisition Regulation (FAR) in Rockville, MD and Huntsville, AL

David Taylor spoke regarding the Tennessee Retainage and Prompt Pay Act to the Tennessee Professional Estimators Association on August 6, 2010.

Bob Symon will be speaking at the Mid-Atlantic Build Expo in Washington, DC on August 18-19, 2010.

Jim Archibald, Sid Trant, and **Rhonda Caviedes** will be presenting on August 26, 2010 at the Green Building Focus Conference & Expo 2010 in Birmingham, AL concerning the emerging regulation and incentives in areas of construction, environmental and tax law.

Bob Symon and **Joel Brown** will present a Bid Protest discussion to Government Contractors in Huntsville, Alabama on August 26, 2010.

Michael Knapp will present a session entitled "Drafting Effective, Enforceable Consulting Agreement to Protect and Maintain Privileges at Various Stages of Project/Litigation" at the 2011 Annual Meeting for the ABA Construction Forum in Scottsdale, Arizona which is scheduled for April 14-16, 2011.

Arlan Lewis, Rhonda Caviedes, and **Michael Knapp** will be participating in the ABA Forum on the Construction Industry's conference entitled "We Won't Get Fooled Again: Lessons Learned in the Economic Downturn" on September 2-3, 2010.

John Bond recently accepted a position as President and Chief Operating Officer for a client of the firm. We thank John for his years of service and wish him well in this outstanding opportunity.

Bradley Arant attorneys have recently presented training sessions to a number of clients regarding Contract Administration and regarding Mandatory Written Ethics Compliance Programs for Federal Government Contracts. If you are interested in either of these seminars for your company, please contact one of the attorneys listed on page 8 of this newsletter.

For more information on any of these activities or speaking engagements, please contact Terri Lawson at 205-521-8210.

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NOTES

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If you did not participate on-line would you want to receive the seminar in another format? ☐ Video Tape ☐ CD ROM

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BRADLEY ARANT BOULT CUMMINGS LLP **Fourth Quarter 2010**

CONSTRUCTION AND PROCUREMENT LAW NEWS

Recent federal, state, and local developments of interest, prepared by the firm's Construction and Procurement Group:

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Owner May Be Liable to Contractor for Failure to Disclose Material Information

The industry uses bid/build delivery systems as a staple. An owner decides what its program is, and hires a designer to put the program into drawings and specifications from which bidders may establish a lump sum price for the work. Is an owner liable to the contractor where the owner knows of a condition but fails to disclose it to the bidders? In many jurisdictions, the answer is yes, if the information is material and if the owner willfully withholds the information. But what if the owner simply is negligent in withholding its superior knowledge? Is there an avenue for a contractor to seek financial redress?

The answer will vary from jurisdiction to jurisdiction. In California recently a public owner (the Los Angeles Unified School District) was held liable to a take-over contractor for negligent failure to disclose superior information. After defaulting its original contractor, the school district issued the original plans and specifications, along with a hundred plus page "pre-punchlist" of items which were incomplete or unsatisfactory from the defaulted contractor's work. On the "pre-punchlist" and in the request for completion bids, the school district stated that the take-over contractor would be liable for all defects in the defaulted contractor's work. As sometimes happens, the specific spot repairs to plaster noted on the "pre-punchlist" in fact required removal of all the plaster on the exterior of the building and repair of the substrate. Likewise, the spot repairs to tile required removal of all of the tile and its substrate in order to obtain a satisfactory tile product. Neither of these was evident from the take-over contractor's pre-bid walk; both were known, or knowable, to the school district at the time it sought the replacement contractor bids.

In a case of first impression, the Supreme Court of California held that a public owner in California is liable to a contractor for resulting cost overruns and damages and that the contractor need not prove an affirmative fraudulent intent to conceal. Rather – with the qualifications stated below – a public entity in California may be required to

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provide extra compensation if it knew, but failed to disclose, material facts that would affect the contractor's bid or performance. Because public entities do not insure contractors against their own negligence, relief for non-disclosure will be allowed in California only when (1) the contractor submitted its bid or undertook to perform without material information that affected performance costs; (2) the public entity was in possession of the information and was aware the contractor had no knowledge of, nor any reason to obtain, such information; (3) any contract specifications or other information furnished by the public entity to the contractor misled the contractor or did not put it on notice to inquire; and (4) the public entity failed to provide the relevant information.

The court itself cautioned that an owner is not liable for *any* failure to disclose. Instead, it explained that the circumstances affecting recovery may include (but are not limited to) positive warranties or disclaimers made by either party, the information provided by the plans and specifications and related documents, the difficulty of detecting the condition in question, any time constraints the public entity imposed on proposed bidders, and any unwarranted assumptions made by the contractor. The public entity likely will not be held liable for failing to disclose information a reasonable contractor in like circumstances would or should have discovered on its own, but may be found liable when the totality of the circumstances is such that the public entity knows, or has reason to know, that a responsible contractor acting diligently would be unlikely to discover the condition that materially increased the cost of performance.

While the case is couched as one involving a public owner, its teaching may be used by a subcontractor (or a takeover surety) against a general contractor in the appropriate context. Whether a given jurisdiction will in fact provide relief, notwithstanding the lack of willful suppression, is a matter that you should carefully consider with the aid of your lawyer.

By Mabry Rogers

Protecting Other Men's Wives: Controlling Employer Liability on the Jobsite

Occupational Safety and Health Administration ("OSHA") regulations long have stated that construction industry standards apply "to every place of employment of every employee engaged in construction work" and that every contractor "shall protect … places of employment of each of its employees." OSHA took the position for many years that a general contractor could be liable for safety violations under these provisions *even if* the general contractor did not cause the hazard and *even if* its own employees were not exposed to it. In other words, a general contractor could be liable for a subcontractor's violation which only affected the subcontractor's own employees. This was called the "controlling employer" doctrine.

Under the previous administration, the controlling employer doctrine was abrogated in an administrative proceeding. That case held that the language above meant that a contractor only had responsibility for protecting its own employees against jobsite hazards, noting that laws about husbands and wives apply only to one's own wife and not everyone else's. OSHA thus would not cite a general contractor for violations that it did not cause or which did not affect the general contractor's employees. That was in 2007.

Controlling employer liability is back. This past August, the original 2007 decision was overturned by the federal Occupational Safety and Health Review Commission. General contractors again face OSHA liability for any and all hazards on a jobsite so long as they have control of the jobsite and so long as they have at least one employee on the site. According to the new decision, the focus is on the language in the regulation, "places of employment." In the Commission's view, that language requires contractors to protect their employees in those places even if only one employee is there and even if the hazard is created by another entity: owner, subcontractor, or anyone else.

General contractors of course want to be vigilant in correcting workplace hazards; this decision may extend that vigilance to hazards that they might not otherwise even see. General contractors may be required to take steps to identify and to correct hazards even if those hazards were created by someone else.

The general contractor respondent in the case likely will appeal. There is a lengthy and well-reasoned dissenting opinion that provides a roadmap for such an appeal. If the decision is reversed, a split in the circuits will occur, as controlling employer liability already has been affirmed in some circuits.

By John W. Hargrove

Recent Revisions to AIA A312 Payment and Performance Bond Forms

The American Institute of Architects ("AIA") maintains over 100 contract document forms in use throughout the construction industry. These contract documents are utilized by owners, architects, contractors, subcontractors, sureties, and other industry participants to define the roles and responsibilities of the parties on design and construction projects.

Periodically, the AIA revises its forms in response to court decisions or to comments from industry participants. One such revision recently occurred with regard to the AIA A312 Payment and Performance Bond forms. The prior (1984) edition of the AIA A312 Payment Bond form provided that the surety had 45 days to respond to a Claim and to state the basis for challenging any amounts that were disputed. Several courts held that the surety's failure to state the basis for challenging disputed amounts within this 45-day period amounted to a waiver by the surety of any challenge to these amounts.

The 2010 revisions to the A312 Payment Bond form address this issue. First, the 2010 revision extends the Surety's response time to 60 days. It then adds an entirely new section which provides that a failure to dispute the Claim within the 60-day period does not constitute a waiver of defenses. This change is in direct response to the court cases which held that a surety's failure to respond within 45 days amounted to a waiver of all defenses.

The revised A312 form does include an impetus for the surety to respond. If the surety does not respond within 60 days, the surety becomes liable to the Claimant to reimburse it for attorney fees "the Claimant incurs thereafter to recover any sums found to be due and owing to the Claimant." These fees are recoverable from the surety even if, when coupled with the amount of the Claim, they exceed the penal sum of bond.

There are other significant changes to the A312 Payment Bond form. The 2010 revision of the Payment Bond form adds a requirement that a Claimant submit a "Claim" and provides that the surety's obligations do not arise until it has received that Claim. This "Claim" is different from the "Notice of Claim" required under previous versions of the A312 form. It is more detailed and includes eight categories of information that must be included. The specific requirements for a proper "Claim" are found at § 16.1 of the revised bond form.

The new requirement for submission of a "Claim" as opposed to a "Notice of Claim" also affects the time in which a Claimant must file suit. Under § 12, the Claimant must file suit within the earlier of one year after the date it submits its Claim or one year after it last performed work on the project. Thus, suit may be required earlier than one year after completion of the work *if* the Claim is filed while work is still ongoing.

Finally, the 2010 revision to the Payment Bond form expands the number of potential Claimants. Previous versions of the Payment Bond form restricted Claimants to first and second tier subcontractors. The revised form broadens the scope of potential Claimants to anyone who may assert a mechanic's lien.

The AIA has also issued important revisions to the A312 Performance Bond form. These revisions deal mainly with the process for making a Claim on the basis of Contractor Default, and with the process for defaulting a non-performing Surety. The process under the new form is less administrative and thus far more streamlined.

Owners, contractors and subcontractors should be on the lookout for these revised forms. Always consider carefully any contract document before signing. After work has begun on a project, be sure to abide by whatever requirements are set forth in the applicable surety bond when making claim under these bonds.

By Luke Martin

No Home-Office Overhead Recovery for Government Contractor Absent Government-Imposed Standby

In a recent case, the Florida Court of Appeals reexamined and left unchanged the law in Florida regarding a government contractor's ability to recover "home-office overhead" as part of its delay damages. In *Martin County v. Polivka Paving, Inc.*, the Florida Court of Appeals held that, although the government contractor was entitled to extended "field-office overhead" and other damages arising out of a delay caused by differing site conditions, the contractor could not recover home-office overhead because it was not the case that the "government imposed delay required [it] to indefinitely standby to the point that [it] was effectively suspended and unable to take on additional work."

The parties to the case, Martin County, Florida ("Martin County"), and Polivka Paving ("Polivka"),

entered into a contract under which Polivka constructed soccer fields and related improvements at a Martin County park. Early in the project, Polivka discovered inaccuracies in the county-provided elevation information on which it based its bid. Predictably, this necessitated the placement of significantly more fill material than Polivka had accounted for in its bid, increasing the project cost and lengthening the project schedule. Although the parties agreed to change orders to account for these discrepancies, Martin County eventually refused to pay for the additional work.

At trial, Polivka argued that it was entitled to home-office overhead costs because, in its view, home-office overhead costs are simply those "costs associated with the home office that are funded by the projects which the company is performing." The trial court allowed the jury to consider these damages, and the jury awarded Polivka, among other damages, $275,251.00 for home office overhead.

Martin County appealed and the Court of Appeals reversed the home office overhead portion of the damages, relying upon a series of previous Florida cases which examined and adopted the law developed in various federal appellate courts. Specifically, entitlement to home office overhead damages requires proof of three elements: (1) a government-imposed delay occurred; (2) the government required the contractor to "standby" during the delay; and (3) while "standing by," the contractor was unable to take on additional work.

The Court of Appeals extensively examined the "standby" requirement and held that, because Polivka had other ongoing jobs which contributed to paying the contractor's home office overhead, it would have incurred the individual cost components of the home office overhead whether or not it ever undertook the Martin County park project.

Contractors who are experiencing government-caused delay on a project should be cognizant of this "standby" gloss as a potential hurdle to recovery of home office overhead costs. As evidenced by this case, when the delay does not stifle the contractor's ability to maintain ongoing work or obtain new work, it may be difficult in some jurisdictions to recover for home-office overhead. On the other hand, if the government requires the contractor to stand by on the project such that it is difficult for the contractor to use its resources elsewhere, or the delay is so uncertain in duration as to make bidding on other work impractical, the contractor may have an eventual claim for extended home-office overhead, and should thoroughly document both the causes of these extended costs and the costs themselves.

By Nick Voelker and James Warmoth

Make Sure You Protect Your Rights

In a recent case, the Armed Services Board of Contract Appeals (the "ASBCA") granted summary judgment – that is, it found that there was no real factual dispute – over 90% of a Contract Disputes Act claim brought by the contractor. The basis for the ASBCA's holding was that the contractor (Whiting-Turner) released all of its rights to claims related to almost all of its contract modifications.

In July 2008, Whiting-Turner entered into a contract to perform new construction and renovation of the U.S. Military resort at Walt Disney World. Over the next 18 months, the parties agreed to 46 bilateral contract modifications. At the end of the project, Whiting-Turner submitted a Request for Equitable Adjustment ("REA") of nearly $4 million on behalf of itself and some of its subcontractors. The contracting officer denied the claims. Litigation followed.

The ASBCA held that in 18 of the 21 disputed modifications Whiting-Turner gave up all of its rights to any additional claims. Each of these 18 modifications stated that the adjusted contract price "constituted a complete and equitable adjustment" and that the modification "resolved any and all costs, impact effect, and … delays and disruptions." Additionally, and to the ASBCA "significantly," not one of these modifications contained any reservation of rights language. Therefore the ASBCA granted summary judgment for the government on all of Whiting-Turner's claims relating to these 18 modifications on the basis that all of these claims were resolved by accord and satisfaction, meaning that because Whiting-Turner accepted the payment amount in the modification, it accepted the terms of the modification. Conversely, the three modifications that the ASBCA allowed to continue to trial had reservation of rights language and reflected that they only addressed a partial recovery.

The lesson here is that modifications need to be read and analyzed carefully. If possible, proposed modifications should be reviewed by in-house or outside counsel. As this case demonstrates, a small, overlooked sentence or phrase in a modification can have significant long term repercussions.

By Lewis Rhodes

"Inconvenience and Discomfort" Damages Available for Mold Infestation

In *Mayer v. Chicago Mechanical Services, Inc.*, an Illinois Appellate Court established that, in Illinois, damages for inconvenience and discomfort are available to an occupant of a home that has been damaged by defective construction, even when the occupant subsequently moves out of the home.

Chicago Mechanical, a contractor, improperly installed the HVAC system in plaintiffs' condominiums which led to a mold infestation. When plaintiffs were forced to move to substitute housing, they sued for inconvenience and discomfort damages. Plaintiffs argued that being displaced caused feelings of homelessness and dissatisfaction – they could not sleep in their own bed, bathe in their own bathroom, or cook in their own kitchen.

The court held that even though inconvenience and discomfort damages typically would be available in this fact scenario, these particular plaintiffs were not entitled to any money because their grievances were vague and subjective, focusing principally on the abstract sense of satisfaction from the comfort of their home. The home owners would have prevailed had they argued tangible damages such as inadequate amenities in the substitute housing, longer travel times to work or school, and any particular nuisances associated with the substitute housing (like having to live in tighter quarters or being exposed to road noise).

The majority of state courts hold, like *Chicago Mechanical*, that inconvenience and discomfort damages are available to plaintiffs whose homes have been negligently damaged. *Chicago Mechanical* provides an argument against such damages for construction industry participants that become involved in such litigation. If a plaintiff argues his theory of damages in a sentimental, abstract manner ("a feeling of homelessness and dissatisfaction") without the support of concrete, factual statements ("driving an additional 6 miles to work each day"), a builder or contractor may have a defense based on the generality of the allegations.

By Vesco Petrov

Bradley Arant Lawyer Activities:

Bradley Arant Boult Cummings' construction practice group was recognized as a Tier 1 national practice group by *U.S. News and World Report* in its first ever ranking of law firm practice groups. This ranking was based on the comments of clients and industry participants, and was performed in conjunction with Best Lawyers, a company which performs a highly-regarded semi-annual ranking of law firms. This recognition is client-driven, and we hope to continue in the future to deliver the services that win this respect.

Mabry Rogers was named "Lawyer of the Year" in the area of Construction Law for Birmingham, AL.

Jonathan Head co-presented a national webcast on June 3, 2010 for Defense Research Institute regarding privilege and its effect on major litigation.

David Pugh, Michael Knapp, Arlan Lewis, Luke Martin, Ed Everitt and Jonathan Cobb presented a seminar entitled "Fundamentals of Construction Contracts" on June 24, 2010 in Birmingham, AL.

Jonathan Head participated in a panel discussion at the Alabama State Bar annual conference on July 16, 2010 about Alabama's new electronic discovery rules and responses to common problems in electronic discovery.

Michael Knapp taught a course entitled "International Construction Contracts and Law" at Misr University of Science and Technology in Cairo, Egypt from July 24 to July 28th to graduate level engineering students**.**

David Taylor presented at an annual project managers meeting regarding "Dispute Avoidance" on August 4, 2010.

David Taylor spoke regarding the Tennessee Retainage and Prompt Pay Act to the Tennessee Professional Estimators Association on August 6, 2010.

Bob Symon spoke at the Mid-Atlantic Build Expo in Washington, DC on August 18-19, 2010.

David Taylor spoke regarding the Tennessee Prompt Pay Act and Retainage to the Tennessee Association for Professional Engineers on August 23, 2010.

Bob Symon and **Joel Brown** presented a Bid Protest discussion to Government Contractors in Huntsville, Alabama on August 26, 2010.

Jim Archibald, Sid Trant, Joe Gibbs, Nick Landau and **Rhonda Caviedes** spoke regarding emerging

regulation and incentives in areas of construction, environmental and tax law at the Green Building Focus Conference & Expo in Birmingham, AL on August 26, 2010. Bradley Arant was a sponsor of this event.

Bob Symon presented a FAR seminar to a government contractor in Huntsville, Alabama on August 27, 2010.

Rhonda Caviedes was appointed to serve on the ABA Forum on the Construction Industry Marketing Committee and thereafter attended this committee meeting on September 1, 2010, Miami Beach, FL.

Arlan Lewis, Rhonda Caviedes, and **Michael Knapp** attended the ABA Forum on the Construction Industry's conference entitled "We Won't Get Fooled Again: Lessons Learned in the Economic Downturn" on September 2-3, 2010.

Arlan Lewis was a featured speaker at the American Bar Association Forum on Construction Industry 2010 Fall Meeting in Miami Beach, FL on the topic of "*Dangers and Dilemmas Associated with Waiving Subrogation Rights in the Construction Contract*."

David Taylor and **Chuck Mataya** led a "2010 Legal Update for Subcontractors" workshop at the September 23, 2010 meeting of the American Subcontractors Association of Tennessee.

Keith Covington wrote an article entitled "Military Leave Under ESERRA: Know Your Obligations" for the October/November 2010 edition of the Alabama Construction News.

David Taylor presented a seminar entitled "Legal Aspects of Construction Claims" to the Tennessee Association of CPAs on September 27, 2010.

Bob Symon provided a client seminar regarding Certified Payrolls and the Davis-Bacon Act in Rockville, Maryland on October 20, 2010.

Keith Covington attended the Defense Research Institute's Annual Meeting in San Diego, California from October 20-22.

David Pugh will serve as emcee at the November 4, 2010 ABC Excellence in Construction Awards Banquet in Birmingham, AL.

Rhonda Caviedes will be attending the 30th IRMI Construction Risk Management Conference on November 14-18 in Orlando, FL.

Jonathan Head and **David Deusner** will be speaking regarding e-discovery at a seminar in our Birmingham, AL offices on November 16, 2010.

Michael Knapp will present a session entitled "Drafting Effective, Enforceable Consulting Agreements to Protect and Maintain Privileges at Various Stages of Project/Litigation" at the 2011 Annual Meeting for the ABA Construction Forum in Scottsdale, Arizona, which is scheduled for April 14-16, 2011.

David Taylor has been named to the Legal Advisory Panel for the Tennessee Association of General Contractors.

Bradley Arant attorneys have recently presented training sessions to a number of clients regarding various topics, including Contract Administration, Risk Analysis and Management, and Mandatory Written Ethics Compliance Programs for Federal Government Contracts. If you are interested in these or similar seminars for your company, please contact one of the attorneys listed on page 8 of this newsletter.

For more information on any of these activities or speaking engagements, please contact Terri Lawson at 205-521-8210.

NOTE: YOU CAN FIND THIS NEWSLETTER AND PAST NEWSLETTERS ON OUR WEBSITE. IF YOU ACCESS THIS NEWSLETTER ON OUR WEBSITE, CASE-LINKS WILL BE AVAILABLE UNTIL THE NEXT NEWSLETTER IS PUBLISHED. WE DO NOT VIEW THIS NEWSLETTER AS WRITTEN FOR ATTORNEYS BUT RATHER FOR PRACTICING MEMBERS OF THE CONSTRUCTION INDUSTRY. IF YOU OR YOUR LAWYER WOULD LIKE TO KNOW MORE INFORMATION ABOUT A PARTICULAR ARTICLE OR WOULD LIKE THE CASE CITES, YOU MAY GO TO WWW.BABC.COM/PG_CONSTRUCT.CFM OR CONTACT ANY ATTORNEY LISTED ON PAGE 8 OF THIS NEWSLETTER.

NOTES

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The lawyers at Bradley Arant Boult Cummings LLP, including those who practice in the construction and procurement fields of law, monitor the law and regulations and note new developments as part of their practice. This newsletter is part of their attempt to inform their readers about significant current events, recent developments in the law and their implications. *Receipt of this newsletter is not intended to, and does not, create an attorney-client, or any other, relationship, duty or obligation.*

This newsletter is a periodic publication of Bradley Arant Boult Cummings LLP and should not be construed as legal advice or legal opinion on any specific facts or circumstances. The contents are intended for general information purposes only, and you are urged to consult your own lawyer concerning your own situation and any specific legal questions you may have. For further information about these contents, please contact your lawyer or any of the lawyers in our group whose names, telephone numbers and E-mail addresses are listed below; or visit our web site at www.babc.com.

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READER RESPONSES

If you have any comments or suggestions, please complete the appropriate part of this section of the *Construction & Procurement Law News* and return it to us by folding and stapling this page which is preaddressed.

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We are in the process of developing new seminar topics and would like to get input from you. What seminar topics would you be interested in?

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If the seminars were available on-line, would you be interested in participating? ☐ Yes ☐ No

If you did not participate on-line would you want to receive the seminar in another format? ☐ Video Tape ☐ CD ROM

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