

**American Bar Association
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Law Committee**

**GETTING TO THE BOTTOM OF
CONSTRUCTION CLAIMS**

**ADMINISTERING THE CONTRACT TO PRESERVE AND PURSUE CLAIMS:
CURRENT TRENDS AND STRATEGIES IN CONSTRUCTION LITIGATION**

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Contractors need to properly administer the “project record” in order to protect and preserve their rights. This does not mean that every problem with the owner or a subcontractor needs to be “papered to death.” It does require, however, that project managers and administrators know how, when, and why notice and other contractual provisions are to be administered and followed. It is also important to understand the role and obligations of the designer as it affects the ability to pursue claims. We have highlighted below some the recent decisions regarding these important points. We also suggest some strategies that can be employed during the project to better ensure that contracts are properly administered.

I. Documenting and Protecting the Record: Important Concepts and Strategies

A. The Need To Comply With The Owner’s Request For Assurances—The Law Of Anticipatory Repudiation In Construction Litigation

The court in Danzig v. AEC Corporation,¹ highlighted the importance of the general contractor’s duty to provide the owner with timely assurances following issuance of a cure notice. In Danzig, the Navy issued a notice to cure when the contractor fell behind schedule to construct the Naval and Marine Corps Reserve Training Center in Florida. The Navy agreed not to terminate for default if the contractor continued to progress toward the new completion date of April 26, 1991 proposed by the contractor.

Despite the extension, the contractor again fell behind, causing the Navy to issue a letter demanding that the contractor “show cause” why it should not be terminated. This notice stated that unless adequate assurances were made within 10 days the Navy would terminate for default. When adequate assurances were not made, the Navy terminated for default on April 22, 1991.

The Board of Contract Appeals held the termination invalid, agreeing with the contractor that modifications and delays attributable to the government warranted an extension of the completion date beyond April of 1999. Because the Navy could not reasonably have concluded

that the contractor would fail to complete the contract by that date, the termination was deemed invalid.

On appeal, the court reversed the Board's decision, finding that when the government issues a demand for adequate assurances based upon reasonable grounds that the contractor may not be able to perform on timely basis, the contractor had an obligation to take steps to demonstrate or give assurances to the owner that progress was being made toward timely completion, or to explain that the reasons for any prospective delay in completion were not the responsibility of the contractor. While the law applicable to a contractor's failure to provide assurances of timely completion is a branch of the law of anticipatory repudiation, anticipatory repudiation in the construction context is not limited to cases of express and unequivocal statements of repudiation. It also applies where the obligee's belief that the obligor will breach the contract is supported by "reasonable grounds." In that setting, the owner may demand adequate assurance of due performance, and if the assurance is not given, the owner can interpret the failure to do so as a repudiation of the contract.

The court further explained that the contractor's assertion of government-caused delay did not respond adequately to the Navy's request for assurances. Any such allegations must be supported by specifics as to what changes caused the delay, how much delay was caused by the Navy, and contain a representation that the contractor could complete the contract within the additional time it believed it was entitled.

B. The Importance Of Strict Compliance With Notice Provisions Regarding Claims

Almost all construction contracts contain notice provisions that require the contractor to provide the owner with notice of a delay or other impact to the work, and precludes recovery of a time or cost adjustment if such notice is not provided. In general, courts have required a party to

strictly comply with clear and unambiguous contract provisions regarding notice of claims. The rationale is that the notice allows the owner to timely investigate and consider alternative methods to address the impact. Contractors typically attempt to raise defenses and excuses for non-compliance with notice provisions by alleging “substantial compliance” with the terms, or that the owner waived the requirement, orally directed the work, or that the owner otherwise knew of the conditions. As the cases below illustrate, courts are becoming even more reluctant to excuse failure to comply, especially in the context of government contracts.

ILM Systems, Inc. v. Suffolk Constr. Co.² is a recent decision underscoring the need to provide timely, definitive notice of claims, as well as the importance and impact of signing typical releases for payment requests during the course of the project. The contract between the subcontractor and contractor required that the subcontractor give notice of all “claims (including disputes over the scope of work) . . . in writing within ten (10) business days (unless a shorter period is specified in the Contract Documents) after the occurrence of the event giving rise to such claim, or the claim shall be considered abandoned by the Subcontractor.” Delays plagued the project, and the subcontractor sent letters and notices of claims to the contractor starting in April 1998 through August 1999. Only one letter in November 1998, however, had sufficient detail to obtain additional payments from the owner so that the contractor could compensate the subcontractor. Except for that one letter, the court found that the letters provided insufficient detail under the contract. The subcontractor cleverly presented evidence that the contractor was late in responding to change order requests and that the contractor impeded the subcontractor’s ability to comply with the notice provisions. Finding a potential factual dispute, the court denied the motion for summary judgment on this point, but required the subcontractor to prove that the

subcontractor prove that the contractor impeded the subcontractor's ability to comply with the notice provisions by failing to fully and timely respond to the change order requests.

With respect to the form releases signed as part of the progress payment procedure, the court found that the broad language of the form release barred the subcontractor's claim of over \$544,000 in delay damages. The court rejected the subcontractor's claims that the form releases were never intended to bar delay damages that were the subject of the "notice" letters, finding that the broad release language was unambiguous with "respect to all claims based on labor, materials and/or equipment furnished through the date [of the release]."

Garofalo Electric Co., Inc. v. New York University,³ also illustrates the importance of strictly complying with contractual notice provisions to preserve a claim. The contract required the general contractor to send notice and documentation of any changes to the owner, architect, and construction manager. The contractor performed additional work, claiming that the construction manager's failure to properly coordinate work caused delays. The general contractor disregarded the strict contractually-required notice provisions, on the basis that the construction manager directed it to deal exclusively with it, and not to correspond with the owner or the architect.

When it wasn't paid for the extra work, the contractor sued. The court barred its claim, ruling that the contract's notice and documentation requirements were conditions precedent to recovery, and therefore the contractor's noncompliance barred its claims. The court rejected the plaintiff's argument that its failure to comply was excused because the construction manager had orally abandoned, waived, or modified the notice requirement. The court found that because the construction manager's authority was clearly and unambiguously limited by the express terms of

both the contract and the construction manager's agreement, it lacked authority to waive or modify the notice and documentation requirements.

As the court in Heckler Electric Company, Inc. v. City of New York,⁴ illustrated, the failure to strictly comply with the notice provisions can be fatal even when the owner has actual notice of the contractor's intent to seek delay damages. In this case, an electrical contractor sued the City of New York and its transit authority for delay damages. Under the contract, when the City allegedly caused damages, the contractor had a limited number of days to give the City a written statement of the nature, details, and amount of the claim. While the contractor did not comply with this provision, it did comply with another contract provision that required contemporaneous notice of delays. The contractor argued that its claim should be allowed because by sending letters to the owners that informed them of its intent to seek delay damages and of some items of damage, it had substantially complied with the notice provision.

The court rejected that argument. In granting the City's motion for summary judgment, the Court noted that "it is well settled that strict compliance is required with contract provisions requiring notice and itemization of damages" and that "it has been expressly held that compliance with a [provision requiring contemporaneous notice of fact of damages but not amount] is not a substitute for compliance with the separate requirements of a provision ... regarding notice of the amount of the damages."

The North Dakota Supreme Court in Dan Nelson Construction, Inc. v. Nodland & Dickson,⁵ went even further than the Court in Heckler Electric Company. The contract there required the contractor to give written notice to the State before any changes could be made to the contract. The notice had to identify both the unforeseen physical conditions and the increase

in the contract price. Notice had to be given in writing to both the owner and the engineer within 15 days of the occurrence of the event giving rise to these claims.

In January, the contractor encountered an unforeseen amount of rock in the subsurface. Four months later it sent a letter to the State asking for additional money based upon unforeseen and changed conditions at the site. After mediation failed to resolve the dispute, the contractor filed suit. The State claimed that the contractor's noncompliance with the notice provision barred suit. The contractor claimed that the State waived those provisions or was estopped from raising them because the State had actual knowledge of the problems in January and even helped the contractor prepare a draft claim form for the changed conditions.

The court agreed with the State, ruling that actual knowledge of changed conditions did not estop the government from raising the untimely filing of the claim as a defense, absent a showing that the delay in filing was induced by the State or that the State had misled the contractor as to the need to file a claim. Even the State's alleged assistance in drafting a claim form was not sufficient to warrant the application of estoppel.

Similarly, in A.H.A. General Construction, Inc. v. New York City Housing Authority,⁶ the court rejected a contractor's allegations that the project owner's misconduct and past practice between the parties could operate to waive the notice requirements. The contract there required written notice within 5 days of the event and daily written statements from the contractor detailing any extra work. The contract explicitly stated that no claim for breach of contract or compensation for extra work could be brought unless the notice and information provisions were complied with strictly.

The contractor attempted to excuse its failure comply with these provisions on the basis of the housing authority's misconduct. The court noted that the notice provisions were

conditions precedent, but that they would not bar a claim if the owner had frustrated or prevented compliance. In this case, however, because none of the owner's alleged misconduct prevented the contractor from complying with the provisions, the contractor's claims were barred.

The court was similarly unpersuaded by the contractor's claim that the past practice between the parties waived the requirements, noting that an alleged past practice with respect to other agreements cannot override specific legal obligations undertaken by parties in later contracts.

In the context of contractor/subcontractor claims, in Wild-Fire, Inc. v. Laughlin, et. al.,⁷ the Court of Appeals of Ohio denied a subcontractor's claim that oral approval of changes in the field waives a requirement that changes in the scope of work be in writing. The subcontractor routinely performed additional work without a signed change order. At the end of the project, the subcontractor submitted 23 written change order requests. It claimed that the contractor approved the extras orally in the field, and that this oral approval constituted a waiver of the contractual requirement of written change orders. The contractor's testimony was that it orally requested work on only two occasions and that it had no idea that the subcontractor was performing change orders throughout the project. This was sufficient evidence, the Court ruled, that the contractor did not waive the written change order requirement. The lesson: a subcontractor who performs additional work without a contractually required written change order proceeds at its own risk.

In addition to requiring strict compliance with notice requirements, courts have ruled that a contractor who fails to comply with such requirements cannot recover in quantum meruit. In Precision Mechanical Contractors, et. al. v. Metropolitan Development & Housing Agency,⁸ for example, the Court of Appeals of Tennessee ruled that a contractor's failure to comply with

notice provisions barred a suit against the owner for additional cost claims and declined to award quantum meruit recovery for the value of these claims. The contractor renovated two housing projects under a contract that required it to assert its rights to an adjustment to a change order within 30 days by submitting a written statement describing the nature and amount of the proposal.

After final payment, the contractor filed suit against the owner for additional costs and delays, despite the fact that it did not comply with the contract's requirements to preserve its claim after receipt of a change order. The court held that this failure to comply with the notice provision barred recovery. Moreover, the court declined to award damages on a quantum meruit theory noting that, as a general rule, implied-contract or quasi contract remedies will not be imposed where an express contract exists.

Strict compliance with notice requirements goes both ways, and applies equally to all project participants. For example, in Tenting v. McPheters,⁹ the court ruled that an owner cannot rely upon undisclosed defects in a contractor's work to avoid a contractual obligation to pay for work that had been substantially completed. The owner withheld final payment, claiming that some work was not performed in a workmanlike manner. The owner had never given notice to the contractor of the defects, and therefore, the contractor claimed that the owner had given up its right to withhold payment by failing to provide a punchlist of items to correct. The court agreed, and ruled that the contractor was entitled to payment because the contractor had not been provided the opportunity to correct any defects.

Similarly, in Envirocorp Well Services, Inc. v. Camp, Dresser & McKee, Inc.,¹⁰ the court required a contractor who failed to timely object to a subcontractor's payment request to pay the full amount of the request. The subcontractor provided services for a deep well injection system

as part of an environmental remediation project. The general contractor was required to state any objections to the subcontractor's application for progress payment within 14 days of receipt. If no objection were made within this time period, the subcontractor's application would be deemed "acceptable."

While general contractor did not object to the subcontractor's application within 14 days, it argued that there was a genuine issue of fact as to the meaning of "acceptable" and that "acceptable" meant something less than liable for payment. The court found that reasonable people could not differ as to the meaning of the term "acceptable"; moreover, because an ambiguous contract will be construed against the party who drafted it, the term "acceptable" would be construed in favor of the subcontractor even if it were ambiguous. Because the general contractor did not object to the subcontractor's request, it was liable to pay this request.

The general contractor next argued that it was relieved of its obligation to pay the subcontractor because it was not paid by the owner. The contract provided that the engineer would bill the owner monthly for subcontractor's services and would pay the subcontractor within 15 days of receiving payment from the owner. While the subcontractor argued that this provision merely governed the timing of payments, the general contractor argued that it created a condition precedent to the payment of subcontractors, thus permanently relieving it of its obligation to pay subcontractors should the owner refuse to pay. The court rejected the general contractor's position, noting that other parts of the contract used the phrase "conditions precedent" and that an absence of such language here indicated that this provision was meant to govern timing of payment and not to create a condition precedent. The court granted summary judgment in favor of the subcontractor, requiring the general contractor to pay the entire amount of its request.

Similarly, in Scherer Construction, LLC v. Hedquist Construction, Inc.,¹¹ the court ruled that apprising the subcontractor of problems did not constitute a demand for repairs. The subcontractor expended significant funds purchasing special equipment and materials called for under the contract. After the general contractor suggested that the owner issue a change order that rendered these materials unnecessary, the subcontractor sued the general contractor for breach of implied covenant of good faith and fair dealing, alleging that the value of the contract was seriously diminished by the change order.

The court barred the general contractor from charging the subcontractor after it took over the subcontractor's work and completed it at its own expense. The court ruled that the general contractor had to give the subcontractor reasonable notice to make repairs, and that the fact that the subcontractor was allegedly aware of the problem did not equate with a demand to make these repairs.

C. Light On The Horizon: The Failure To Comply With Notice Provisions Is Not Always Fatal.

While the foregoing cases illustrate the tremendous importance of complying with notice provisions, some courts have held that failure to comply with these provisions may not be fatal to a claim in several situations: (1) where the claim stems from the owner's affirmative breach of contract that affects the contractor's ability to comply; (2) where the owner has actual notice of the condition to which the notice requirement relates; (3) when "clear and unmistakable evidence" shows that the owner waived the notice provision; and (4) where the conditions triggering the notice requirement have not fully occurred. Some recent cases on these points include the following.

In ILM Systems, Inc. v. Suffolk Constr. Co., discussed above, the subcontractor was narrowly able to avoid summary judgement against it for failure to comply with notice

provisions by claiming that the contractor affirmatively impeded its ability to comply with the notice provisions in the contract.¹² Similarly, in Amelco Electric v. City of Thousand Oaks,¹³ the court ruled that failure to comply with a notice provision did not bar a contractor's claim where that claim was based on the owner's own breach and abandonment of the contract. In this case, an electrical contractor sued the owner for damages caused by the owner's abandonment and breach of contract based upon the owner's issuance of a series of sketches that changed virtually every part of the work at least once.

The Supreme Court of Mississippi in Ronald Adams Contractor, Inc. v. Mississippi Transportation Commission,¹⁴ held that a contractor's failure to comply with a notice provision did not bar suit where the owner had actual knowledge of the condition to which the claim related. The contractor encountered areas along a proposed roadway where the soil conditions at the designated grade were unacceptable. The contract required the party discovering differing site conditions to notify the other party in writing before the conditions were disturbed and before the affected work was performed. The contractor sued to recover additional compensation for extra work.

The owner claimed that the contractor's failure to comply with the notice provision barred its suit. The court disagreed, noting that both the owner's engineer and the contractor knew of the alleged differing site condition. Because Mississippi law recognizes that a person is never required to perform a useless act, and because the owner already had actual knowledge of the alleged differing site condition, giving notice would have been a useless act. Therefore, the contractor was not obligated to give formal written notice and its failure to comply with the notification provision did not bar suit.

In Koren-DiResta Construction Co., Inc. v. New York City School Construction Authority,¹⁵ the court ruled that a failure to comply with a notice provision did not bar a claim because the notice provision had not yet come into play. The contractor filed a claim against the owner for breach of contract, seeking the contract balance, acceleration and impact costs, and compensation for extra work. The owner argued that the claim was barred because notice of the claim was not timely filed.

Both parties agreed that the running of the three-month period for filing notice of a claim began with the date of substantial completion. They disagreed, however, on when the project was substantially complete. The contract defined the date of substantial completion as the date on which the owner certifies completion. Because the owner *never certified completion*, the three month period never began to run and the claim was not barred.

In Associated Mechanical Contractors, Inc. v. Martin K. Eby Construction Co., Inc.,¹⁶ the Court of Appeals for the Eleventh Circuit offered more hope for contractors by ruling that the timeliness of claims must be evaluated separately for discrete events. The subcontractor contracted to perform work on a prison construction project. The contract required notice for delay damages to be given in writing within 10 days of the commencement of the alleged damage. While the subcontractor was scheduled to start work in May of 1990, it was unable to start the job until June 18, 1990.

While the prime contractor acknowledged the delays, it announced that it would make up the lost time by revising the construction schedule. By letters beginning on August 1990 and continuing through February 1991, the subcontractor complained to the general contractor about the delays. In November 1992, the subcontractor presented a claim for equitable adjustment, seeking additional compensation and a 462 day time extension on its contract completion date.

When the prime contractor denied the claim, the subcontractor brought suit for breach of contract, equitable adjustment, and quantum meruit. The prime contractor filed a summary judgment motion, alleging that the subcontractor had failed to give timely notice of its intent to seek delay damages. The trial court granted its motion.

On appeal, while the subcontractor admitted it knew of delays as early as May of 1990 and did not give notice until August of that year, it argued that the delays did not constitute damages at that point because both parties hoped that the early schedule slippage would be recouped. The contractor responded that damages were incurred once equipment sat idle and overhead began to accrue, and thus notice should have been given promptly. The court noted that the damages from the pre-notification period were a small part of the total damages claimed for delay. Timeliness of claims must be evaluated separately for each discrete event, and events occurring after July of 1990 were not related to those in the earlier period. Because the district court failed to take into account damages caused by events after July, the judgment was remanded for determination of which claims were barred by failure to give timely notice and which were preserved.

D. Strategies For Effectively Dealing With Notice Provisions

Project managers and foremen need to be informed of the importance for strictly following contractual notice provisions. The project or contract administrator should read the contract terms and conditions, including any provisions that “flow-down” from the prime contract. A “checklist” should be prepared and distributed to the staff and field superintendents to clearly define and inform them of the time frames, procedure, parties and conditions under which notice is to be provided. Information as to the event, the actual or potential time and cost impact should be noted, as well as a request for an equitable adjustment to the schedule. The

level of detail provided will depend upon the facts, but the key to keep in mind is to preclude an argument that the party receiving the notice is prejudiced by the late or insufficient notice.

Many states have also adopted statutes requiring time periods under which payment requisitions must be reviewed. Strict notice provisions of any disputed work must be issued, with prompt payment of any undisputed work. The “checklist” noted above should contain a distillation of these important statutory requirements.

Photographs and videotapes can also be used to define and depict changed conditions. Careful tracking of costs through cost coding can also be a tremendous asset in costing claims.

II. Design Issues: Dealing with the Architect/Engineer

Several noteworthy cases have recently addressed the importance of documenting issues with the designer. Other interesting decisions on the importance of timely and properly documenting conversations with a project’s architect or engineer are also discussed below.

A. The Spearin Doctrine Continues To Provide Protection To Contractors, With Exceptions.

In the landmark case of U.S. v. Spearin,¹⁷ the United States Supreme Court held that an owner who provides plans and specifications to a contractor impliedly warrants the adequacy of the plans and specifications. Therefore, the contractor must usually bear the burden of unanticipated costs that arise during construction, unless these costs arise from deficiencies in the plans and specifications. The Court further limited the ability of an owner to contractually shift the burden of unanticipated costs imposed by inadequate plans and specifications, stating that “the implied warranty is not overcome by the general clauses requiring the contractor to examine the site, to check on the plans, and to assume responsibility for the work until completion and acceptance. The obligation to examine the site did not impose upon [the contractor] the duty of making a diligent inquiry into the history of the locality.”¹⁸

The end result is that the owner must ensure that the plans and specifications are adequate.

The Spearin Court did not indicate that it is impossible for the owner to shift to the contractor the burden of due diligence. Therefore, owners continually attempt to shift the burden of the adequacy of plans and specifications for the work to contractors via contract clause. In T.L. James & Co., Inc. v. Traylor Bros., Inc.,¹⁹ for example, the plans and specifications provided to the contractor did not include a series of concrete slabs below grade. However, the contract notified the contractors of these below grade structures and referred them to an archive of maps detailing the area. The contractor was eventually delayed during construction due to the presence of the underground concrete slab.

The Court held that the contract clause notifying the contractor of the presence of the possible structures and referring them to maps detailing the area was insufficient as a matter of law to shift the risk of incomplete plans and specifications to the contractor. The Court ruled that an owner may not shift the burden by merely indicating that additional information is available elsewhere.

However, in Franklin Pavkov Construction Co. v. James G. Roche, Secretary of the Air Force,²⁰ the owner inadvertently provided the contractor with plans from a previous year rather than the correct updated plans. The outdated plans had less detailed descriptions of the materials required to complete the project, and did not indicate that the owner would provide particular materials which the owner did, in fact, intend to provide. Normally, this could be a sufficient basis for a claim. Looking at the totality of the circumstances, however, the Court held that the plans and specifications were not defective. The Court held that the contractor took the risk of submitting a bid on the information before it, even though it did not have the updated

specifications. The Court noted that the contractor had other opportunities to gather information during the bid process, including visiting the job site and investigating whether the plans are sufficient to perform the construction project.

The Appellate Court of Connecticut has recognized that compliance with an architect's written plans does not insulate a contractor from a suit for negligence where the contractor knew or should have known of deficiencies in the plans. In Greene v. Perry,²¹ the owner sued the contractor after the floor in his home began to buckle. A civil engineer's examination of the home's structural system revealed that the support system was overstressed and that remedial measures needed to be taken to prevent further damage.

The architect allegedly orally "suggested" to the contractor during construction that one of the columns called for in the written plans could be removed, but "recommended" the steel beam be installed instead of a wooden one and that the contractor consult with the owner. Contrary to this, the contractor removed the column and proceeded with installation of the wooden beam without informing the owner. When the floor began to buckle, the owner filed suit, alleging the contractor's negligence.

The contractor argued that because he built the home in accordance with architectural plans that did not specify a steel carrying beam, his workmanship could not be found faulty and he could not be held responsible for the damage caused by the inadequate support system. The court disagreed, finding that the builder held himself out as a skilled builder and knew or should have known that the wooden beam was inadequate to handle the increased load based upon his consultation with the architect.

B. Subcontractor Could Not Recover From Project Inspector For Tortious Interference With Business And Contractual Relations In The Absence Of A Malicious Motive.

In PAR Painting, Inc. v. Greenhorne & O'Mara, Inc.,²² a subcontractor contracted to sandblast and repaint three bridges for the Department of Transportation, which retained an inspector for the project. The subcontractor and the inspector repeatedly clashed over the subcontractor's alleged noncompliance with contract specifications. Eventually, the subcontractor voluntarily left the job. The subcontractor brought suit against the inspector claiming that it had performed inspections too slowly and in bad faith, resulting in monetary and reputational damages. The jury found for the subcontractor on its tortious interference with business and contractual relations claims.

The inspector moved to set aside the verdict. The court granted its motion, finding that the verdict was contrary to law and unsupported by the evidence. The subcontractor appealed. The court denied its appeal, finding that the subcontractor failed to show that the inspector's conduct was in fact tortious. Because it is in the very nature of an inspector's function to interfere with the work being inspected, evidence of some malicious motive was especially crucial. Because the subcontractor failed to establish such motive, the jury's verdict was improper.

C. Project Owner Liable to Contractor For Delay Damages When The Designer Concealed Circumstances That Would Impact Timely Performance.

In Triple R. Paving, Inc. v. Broward County,²³ the court allowed the contractor to recover delay damages from the owner where the project designer had knowledge of conditions likely to cause delay, yet did not apprise the contractor of these conditions. The contract at issue barred claims for delay damages unless the delay was due solely to fraud, bad faith or active interference on the part of the owner or its agents. The general contractor's engineer submitted

designs that did not meet certain standards. The project designer realized this fact, yet said nothing. The court held that the designer's knowledge of the design flaw and its subsequent failure to apprise the general contractor of the flaw was sufficient to constitute willful concealment of foreseeable circumstances which would impact timely performance, such that the "no delay damages" clause may be overcome. Because the project designer was the owner's agent, the owner was liable for delay damages.

D. The Statute Of Limitations On Professional Negligence Claim Begins To Run When Owner Is On Inquiry Notice Of Potential Claim.

In Gering-Fort Laramie Irrigation District v. Baker,²⁴ the court held that the two year statute of limitations for a professional negligence claim began to run on an owner's claim against an engineer when it discovered one aspect of the defect in the work such that it should have been on inquiry notice that all of the work was defective.

The engineer contracted to relocate irrigation structures along a highway. The district's discovery that one of the joints was improperly constructed put it on inquiry notice of possible negligence such that it had a duty to investigate whether all the joints were improperly constructed and whether the engineer had approved such improper construction. Because the district had knowledge of the facts forming the basis for its complaint, the statute of limitations began to run when it first discovered a defect in the work. Its claim, filed more than two years later, was barred.

E. Strategies For Administering The Project With The Architect: Use Logs To Track Submittals And Avoid Delays.

Most contracts require that work not proceed until materials and the work have been reviewed and authorized by the architect through the submittal process. Contractors should monitor the process and avoid delays by creating comprehensive submittal logs.

The logs should keep track of all submittals that must be made for the project, and include the following important information:

- the dates submitted;
- the subcontractor or supplier involved;
- the architect's response and any revisions thereto.

Each submittal should be tracked by the date required to be submitted to the architect, the supplier or subcontractor, the date actually submitted, the return date and any response or supplemental submittals. Any variance to the strict contract terms should be noted and a prompt notice sent to all parties pursuant to the contractual notice requirement.

IV. The Importance of Maintaining/Updating the Progress Schedule

There have been many recent decisions regarding delay claims and how progress schedules can be used to prove or disprove claims.

Most contract documents for complex projects require that contractors submit construction progress schedules using CPM methodology and incorporating the milestones required in the contract. Scheduling requires judgment calls used in establishing logic, ties and sequences. Therefore, it can be difficult to justify termination of a contractor for defective or inappropriate schedule. Yet, in In re Stone & Webster, Inc.,²⁵ the court upheld the owner's termination of a contractor for defective and inadequate scheduling.

The contractor was required to develop a schedule necessary to complete the project on time and budget. The project was to decommission Maine Yankee Atomic Power's Wiscasset nuclear power plant. The schedules submitted by the contractor were not resource loaded, contained logic problems that masked that the project was nine months late, and lacked a number of work activities.

The owner terminated the contractor, took over the schedule, but in order to use it the owner had to add an immense amount of detail and logic. In defense, the contractor claimed that the owner unreasonably rejected many schedules making it impossible to comply with its obligations.

The bankruptcy court disagreed with the contractor, finding that the owner was entitled to demand great attention to detail in the schedule. Since the contractor never provided that schedule, the owner was entitled to terminate the contractor.

In Alcan Electrical & Engineering Co., Inc. v. Samaritan Hospital,²⁶ the court rejected a claim by a general contractor that two subcontractors who caused a concurrent delay should be held jointly and severally liable for the entire delay. The project was delayed by 201 days. One subcontractor was found responsible for 31 days of this delay, and its award was offset for its own delay. The other was found responsible for 170 days of delay. The general contractor appealed, claiming that they both should have been held jointly and severally liable for the entire amount of the delay. The court declined to hold the subcontractors jointly and severally liable, noting that it had been pointed to no schedule, or authority from Washington or any other jurisdiction standing for that proposition. Moreover, the court found that the amount of delay attributable to each party was a question of fact and the trier of fact found that the project record and schedule was adequate to split the delay periods.

A time impact analysis is the preferable method to analyze and measure delays. In Morganti National, Inc. v. United States,²⁷ for example, the court rejected an as-built delay analysis that did not include the project schedule's regular update as a tool to measure delays. In this case, a contractor was required to prepare a schedule using critical path method scheduling and to submit a time impact analyses in support of any extension requests. The contract did not

allow the contractor to add time to the contract schedule unless it was approved by a bilateral modification.

The contractor brought suit seeking to convert its termination for default into termination for the convenience of the government on grounds that the government excusably delayed its performance and breached the contract. The contractor abandoned an impact analysis, and instead proffered another expert relying on an as-built schedule analysis. The court rejected this analysis, stating that the contractor had to offer an impact analysis to measure delay. The court found that the total time analysis based merely upon an as-built schedule was wholly lacking in the face of contemporaneous schedule updates.

Similarly, in Sauer, Inc. v. Danzig,²⁸ the Federal Circuit rejected a contractor's claims for government-caused delay and disruption and remission of liquidated damages. When crane construction work being performed by others fell behind schedule, the contractor at issue was forced to complete its interim finish work concurrently with crane-rail installation. This activity disrupted its performance and caused inefficiency.

The Board of Contract Appeals found that crane work during the contractor's performance caused only two days of delay, which were concurrent with other contractor-caused delays, and denied the remainder of its delay claims.

The contractor appealed. The court noted that to establish entitlement to an extension based upon an excusable delay, a contractor has to show that the delay resulted from unforeseeable causes beyond its control, without its fault or negligence, and that it delayed the overall contract completion, i.e., affected the critical path of performance. The court found that substantial evidence supported the Board's finding that the contractor failed to demonstrate an excusable delay. Specifically, the court noted that there was no persuasive schedule impact

analysis performed, that much of the testimony related to conditions after the completion date, and that contemporaneous complaints made no mention of difficulties specific to the presence of cranes.

In contrast, in Metropolitan Transit Authority,²⁹ the Court of Appeals of Texas declined to require a contractor to prove the exact length of an alleged delay. The owner hired a contractor to build a concrete parking lot and transit lane bridge over a pedestrian walkway. The contractor eventually filed suit for breach of contract, seeking damages for a delay allegedly attributable to the owner's indecision in selecting a detour route. The jury found for the contractor and awarded damages on its differing site conditions, breach of contract, and delay damages claims.

On appeal, the owner claimed that the evidence supporting the delay damages award was legally and factually insufficient. At trial, the contractor testified that the project was initially delayed three and a half to four months by the owner's indecision on choosing a detour. This initial indecision caused further delays because it pushed the project into the rainy season, causing further delay of "a couple of more months." The owner argued that this evidence was vague, and that the contractor had to prove the exact number of days of delay with a critical path schedule to recover delay damages.

While the appellate court agreed that the contractor had the burden to prove the extent of delay with reasonable certainty, it disagreed that the contractor had to prove precisely the number of days of delay. Because there was no evidence that the overall delay in question was caused by anything other than the owner's indecision in choosing the detour location, the court found that the evidence presented a trial was legally and factually sufficient to support the jury's award of delay damages..

V. Litigating or Arbitrating Claims Before Project Completion

There have been several recent interesting decisions related to dispute review boards and the timing and consideration of arbitrations of disputes.

A. *Courts Have Embraced The Use Of Dispute Review Boards.*

It is the well-established policy of federal courts and virtually every state court to encourage enforcement of alternative dispute resolution procedures. Normally, if a party is disputing enforcement of a dispute resolution procedure, the courts will look at three issues: whether the parties entered into a valid agreement to submit their dispute to ADR; whether the particular dispute comes within the scope of that agreement; and whether there has been compliance with any condition precedents to access to the ADR.

In BAE Automated Systems, Inc. v. Moorse-Diesel International, Inc.,³⁰ the Court addressed whether a dispute review board should provide an initial interpretation of a contract claim based upon the automatic bag handling system for the new terminal facility at John F. Kennedy International Airport. The claim was asserted by a subcontractor against the general contractor, which then brought a third-party action against the project owner for any damages sustained on the claim.

Section 7 of the prime contract set up a dispute review board to assist and facilitate the timely and equitable resolution of all project-related disputes, claims or other controversies. The board consisted of three members: one member chosen by the owner, the contractor and the architect.

The subcontract specifically incorporated by reference the dispute resolution procedure in the prime contract, including use of the dispute review board.

After substantial completion of the project, the subcontractor brought the claim against the general contractor for alleged mismanagement, seeking damages and extension of time to complete its work.

The subcontractor argued that the dispute resolution procedure applied only to claims attributable to the owner's conduct, and not to claims related to the general contractor's mismanagement. The subcontractor also relied upon a provision of the dispute review board procedure that required the general contractor to "pass on" to the owner all proper claims submitted by the Subcontractor under the dispute's procedure of the Prime Contract on behalf of and to the extent required by the Subcontractor [and Subcontractor] agrees that Construction Manager's liability herein is strictly limited to the amount(s) Construction Manager receives from the Owner." The subcontractor argued that this provision prevented the subcontractor from initiating the review process, forced the general contractor to "pass on" to the owner claims against itself, and prohibited the subcontractor from recovering any damages caused by the general contractor's breaches.

The Court ruled that the subcontractor's position was without merit because the subcontract unambiguously incorporated the dispute resolution procedure of the prime contract and required the subcontractor to pursue and exhaust that procedure prior to commencing any other action. Nothing, the Court found, limited the dispute resolution procedure to those claims attributable to the owner's conduct. Although the dispute resolution procedure required that the construction manager pass on the subcontractor's claims, that provision merely provided the mechanism for invoking the dispute resolution procedure and to not define its ultimate scope.

The Court also rejected the subcontractor's claim that the dispute resolution board did not have jurisdiction for claims that arose after substantial completion of the work. Again, the Court

found that claim to be without merit as the claims obviously arose from work on the project, which fell within the broad scope of the dispute review board's jurisdiction.

B. Courts Generally Decline To Order Consolidation Of Arbitrations If The Agreement Is Silent On The Question.

Everyone knows that a major problem with arbitration of disputes is the customary contract clause that precludes consolidation of disputes. In Rolls-Royce Industrial Power, Inc. v. Zurn EPC Services, Inc., et. al.,³¹ the court denied a petition to consolidate two pending arbitrations because the court did not find that it was more likely than not that all the parties involved intended for their disputes to be consolidated. In this case, the owner entered into a purchase order contract with the general contractor. The main contract contained an arbitration provision that required the parties to arbitrate all disputes with the AAA in Chicago. This provision was incorporated by reference into the contractor's subcontracts.

The general contractor terminated a subcontractor after the owner terminated the main contract. The general contractor filed a demand for arbitration against the owner, requesting it to take place in Atlanta rather than in Chicago as the contract required. Subsequently, the subcontractor sued the general contractor in California state court. After removing the action to federal court, the general contractor filed a motion to stay the litigation pending arbitration. The parties agreed to arbitrate, and the subcontractor filed a demand with the AAA in Chicago. The general contractor then sought consolidation of the two pending arbitrations. The other two parties opposed consolidation, arguing that they never agreed to consolidate arbitrations with third parties who were not signatories to their respective arbitration agreements.

The court noted that the Fifth, Sixth, Eighth, Ninth and Eleventh Circuits have all held that a court may not order consolidated arbitration if the parties' agreement is silent on the question. However, the court noted that the Seventh Circuit has pulled back slightly from this

clear-cut rule, requiring the court to determine if it is more likely than not that all the parties involved “intended” for their disputes to be consolidated. Under the facts of the case, especially in light of the fact that two separate arbitration agreements signed by different parties were involved, the court determined that the parties did not intend for their disputes to be consolidated. The petition to consolidate the arbitrations was denied.

C. Arbitration Agreements Can Apply To Claims Between Persons Not Party To The Agreement If The Issues Involved Are Related To Or Intertwined With The Main Agreement.

In Choctaw Generation Limited Partnership v. American Home Assurance Company,³² the Second Circuit ruled that a signatory to a contract containing a mandatory arbitration provision was estopped to avoid arbitration with a nonsignatory, where the issues raised by the nonsignatory were intimately intertwined with the performance under the other agreement requiring arbitration. There, the general contractor and the owner entered into a contract to build a power generation facility under which the general contractor was to provide engineering, procurement, and construction services. The contract between the general contractor and the owner contained a mandatory arbitration provision. The general contractor’s performance was also guaranteed by a bond. Provisional acceptance of the facility was delayed for reasons that were in dispute. While the general contractor claimed that the delay was due to force majeure, the owner disagreed and claimed liquidated damages in an ongoing arbitration. The owner drew down a \$33 million letter of credit posted by the general contractor and demanded that the surety replenish the letter of credit as necessary. The bonding company refused.

The bonding company argued that the owner, as signatory to the construction contract, had to arbitrate its dispute with the bonding company because the bonding company had a close relationship with the contractor, and because the dispute was closely linked to an owner’s dispute

with the contractor that was subject to arbitration in the underlying contract. The court agreed, noting that “the circuits have been willing to estop a signatory from avoiding arbitration with a nonsignatory when the issues the nonsignatory is seeking to resolve in arbitration are intertwined with the agreement that the estopped party has signed.”

Similarly, in Cunningham Hamilton Quiter, P.A. v. B.L. of Miami, Inc.,³³ the court ruled that an owner had to arbitrate its claims against the architect hired by the design builder, even though there was no signed contract between the Architect and owner for the construction of an entertainment complex in Florida. A dispute arose between the owner and the design builder. The owner instituted a contractually required arbitration proceeding against the design builder. In addition, the owner filed a lawsuit against the design-builder’s architect for architectural and engineering services malpractice. The court agreed with the architect that the lawsuit should be dismissed because the owner had to arbitrate all of its disputes with the architect, notwithstanding that the architect and the owner had not signed any contract. The court ruled that the owner’s lawsuit against the architect was intertwined with the design build contract, and that therefore the architect is a necessary party to the arbitration.

D. Arbitration Clause Could Not Be Assigned In A Liquidating Agreement.

The Supreme Court on Rhode Island ruled that a contractor could not assign to a subcontractor the contractor’s arbitration agreement with the owner. In Bd. of Governors v. Infinity Construction Services, Inc.,³⁴ a subcontractor claimed that architect’s design documents misrepresented the quantity of necessary excavation. The subcontractor settled its claims against the contractor under a liquidating agreement, under which the contractor agreed to permit the subcontractor to pursue the claim against the owner in the name of the contractor. In exchange,

the subcontractor agreed to pay all costs to pursue the claim and to release the contractor from any liability.

The contractor and owner had agreed to binding arbitration. The subcontractor then filed an arbitration demand against the owner. The owner moved in court to enjoin the arbitration on the grounds that it never agreed to arbitrate against the subcontractor. The Supreme Court agreed that the owner could be compelled to arbitrate because the right to arbitrate is not an assignable right. The court also noted that a prime contractor could not pursue a “pass-through” claim under a liquidating agreement on behalf of a subcontractor unless the prime had incurred liability toward the subcontractor.

E. Alternatives To Litigation During The Project

Many contracts require that the parties proceed through various steps as part of the dispute resolution procedure. This process, called “step negotiations,” can resolve disagreements at lower levels of management before proceeding to higher levels of negotiations.

Parties should consider establishing a series of contractually required dispute resolution steps, with each “step” taking the dispute to the next level of management. For example, the parties could contractually agree that they will attempt to resolve their differences through direct negotiations between defined project site representatives who have authority to settle. Time limits should be set for each phase of the step negotiation after which personnel at the next higher level take over the resolution of the disagreement. The procedure could establish, for example, that the project managers have an obligation to meet, present their claims and then within a certain time frame (such as 14 to 21 days) either reach an agreement or state that they have reached a stalemate.

The project executives may then take over the analysis. Again, if not resolved within a certain time period of exchanging information and position papers, they may wish to refer the dispute to senior management.

It is important that site representatives and project managers know of the procedure and follow it. Lines of authority and levels of settlement authority need to be established. Practical business decisions also come into play before positions become polarized and the dispute turns into a prolonged legal battle.

Dispute review boards are also an approved form of alternative dispute resolution. They typically consist of three to five neutral members who have an experience with the type of construction involved. All members are usually approved by both the owner, the contractor and the engineer, with the fees and expenses to be shared equally. The procedure is usually part of an express “flow down” contract term to subcontractors.

The board members are generally kept advised of job progress and meet with the project team members during construction at critical events.

When disputes arise, the board may conduct a hearing with ample opportunity given to all interested parties to present evidence, documentation and testimony.

The board typically deliberates in private and prepares written recommendations.

If the recommendations do not resolve the dispute, the written recommendation may, or may not, depending upon what the parties agree, be admissible as evidence in subsequent dispute resolution proceedings.

The existence of dispute review boards tends to reduce the overall number of disputes and generally leads toward an early settlement of disputes.

Dispute review board specifications should be noted in the instructions to the bidders and referenced in the general or supplemental conditions. A typical provision may state as follows:

Dispute Review Board. Dispute Review Board (“DRB”) shall be established after contract award and shall be active throughout the duration of the project. The DRB shall assist in a timely and equitable resolution of disputes and other controversies between the owner and contractor. The purpose, procedure and function and key features of the DRB are set forth in more detail in the specifications included herein.

Forms of dispute board resolution specifications are available, including from the American Society of Civil Engineers. Key terms that should be covered include the following:

payment for services and expenses;
disputes that are governed by the DRB specifications;
procedures for submittal of disputes, claims, hearings;
timing for the board’s recommendations;
confidentiality and other provisions related to appeal or rejection of any recommendation.

If DRB’s are to be used, the appropriate dispute resolution procedures in the specifications should be changed to note that the DRB is the first step in the resolution process.

VI. Conclusion

Courts continue to strictly construe and enforce notice, scheduling and dispute resolution provisions outlined in contracts. Contractors need to be especially vigilant in following the “letter of the contract” in public works projects. Otherwise, the chance to preserve and pursue claims is greatly diminished, despite the fact that the actual job conditions and events may justify an equitable adjustment.

¹ 224 F.3d 1333 (Fed. Cir. 2000)
² 2002 U.S. Dist. LEXIS 15095 (August 2, 2002)
³ 705 N.Y.S.2d 327 (2000)
⁴ 715 N.Y.S.2d 619 (2000)
⁵ 608 N.W.2d 267 (N.D. 2000)
⁶ 92 N.Y.S.2d 20 (Ct. App. N.Y. 1998)

7 2001 Ohio App.LEXIS 976 (March 9, 2001)
8 2001 Tenn. App. LEXIS 794 (October 25, 2001)
9 977 P.2d 234 (Id. Ct. App. 1999)
10 2000 U.S. Dist. LEXIS 16088 (S.D. Ind. Oct. 25, 2000)
11 18 P.3d 645 (Wyo. 2001)
12 2002 U.S. Dist. LEXIS 15095 (August 2, 2002)
13 82 Cal. App. 4th 373 (2000)
14 777 So.2d 649 (Miss. 2000)
15 740 N.Y.S.2d 56 (2002)
16 271 F.3d 1309 (11th Cir. 2001)
17 248 US 132, 63 L.Ed 166, 39 S. Ct. 59 (1918)
18 248 U.S. at 136.
19 No. 97-0342, 2000 U.S. Dist. LEXIS 4378 at *3 (E.D. La. March 28, 2000)
20 279 F.3d 989 (Fed. Cir. 2002)
21 771 A.2d 196 (Conn. App. 2001)
22 763 A.2d 1078 (Conn. Ct. App. 2001)
23 774 So.2d 50 (Fla. App. 4 Dist. 2001)
24 612 N.W.2d 897 (Neb. 2000)
25 279 B.R. 748, 2002 Bankr. LEXIS 606 (D. Del.)
26 2002 Wash. App. LEXIS 33 (January 10, 2002)
27 2001 U.S. Claims LEXIS 57 (Fed. Cl. April 4, 2001)
28 224 F.3d 1340 (Fed. Cir. 2000)
29 788 A.2d 192 (Md. Ct. App. 2002)
30 2001 WL 547133 (S.D.N.Y., May 22, 2001)
31 2001 U.S. Dist. LEXIS 18278 (N.D. Ill. 2001)
32 271 F.3d 403 (2d Cir. 2001)
33 776 So.2d 940 (Fl. Dist. Ct. App. 3d Dist. 2001)
34 795 A. 2d 1127 (R.I. 2002)