Construction Tool Box: Construction Laws, Cases, Notes and Alerts

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INTRODUCTION

This Second Edition of 2015 contains an interesting assortment of cases and opinions from Rhode Island to Washington on topics such as pay-if-paid provisions, delay damages, roof warranty, and what is a "final" release. There are also interesting decisions on the recurring subjects of CGL coverage for construction defects (Pennsylvania), and establishing additional insurance coverage (Maryland). Harmonie attorneys are well-versed in these issues, and know the law in their particular jurisdiction.

- The Editor

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CONCRETE SPECIFICATIONS

U.S.f/b/o San Benito Supply v. KISAQ-RQ 8A 2 JV, 2015 U.S. Dist. LEXIS 9921 (N.D. Cal. January 28, 2015).

Frazier Masonry was the concrete sub-contractor on a project to build an equipment facility in California. San Benito Supply (SBS) delivered concrete to the project that failed to meet specifications. Frazier withheld $300,000.00 from SBS to recover the remediation costs, and a District Court found Frazier was justified in removing and replacing non-conforming concrete, and holding the retainage constituted a justifiable damages recovery.

Because this was a heavy duty maintenance facility, the specifications required floor slabs to be 6000 psi concrete. No specific concrete mix was specified, but there were limitations such as suggested percentages of fly ash, recommendations to add steel fibers, etc. After the concrete was poured, a thin top layer of the concrete peeled and flaked, and compression tests also showed the concrete did not reach required strength and had to be replaced. Frazier argued that the design and qualifying of the concrete mix is the supplier's job. In addition, SBS apparently admitted its role as the primary mix designer. It also turned out that SBS had no real field or contract experience with heavy duty concrete, which was concealed during the bid process.

NATIONAL FOCUS

CONTRACT DISPUTES ACT -- CONTENTS OF CLAIMS

Construction Group LLC v. Dep't Homeland Sec., 2015 CIVBCA LEXIS 71 (March 4, 2015).

Construction Group LLC ("Construction Group") was the prime contractor on a pier restoration project for the U.S. Coast Guard. Construction Group completed the project, and the Coast Guard accepted its work. Several months later, Construction Group gave the Coast Guard notification that it intended to submit a claim to "modify, reform, and renegotiate" the contract. The Coast Guard contracting officer wrote to Construction Group that "the terms and conditions of the [contract] [had] been received and accepted," the "contract [was] hereby considered complete," and the remaining balance on the contract was $6,028.55. Construction Group characterized this letter as a final decision which constituted "a money claim . . . against the contractor" and appealed the letter to the Civilian Board of Contract Appeals. The Board held that there was no underlying claim as required by the Contract Disputes Act (CDA) and dismissed the appeal for "lack of jurisdiction."

Construction Group's complaint alleged that it asked the Coast Guard to pay for rework it performed following unsatisfactory performance by a subcontractor. The complaint also alleged that the same contractor stole copper from the work site, but the Coast Guard had prevented security from making an arrest. However, the record did not reflect that Construction Group submitted written claims to this effect, a requirement of the CDA. Additionally, the complaint asserted that Construction Group had suffered damages of an amount between $40,000 and $120,000. The CDA requires that claims contain damages described in a "sum certain." The "wide range of dollars" here asserted as damages did not satisfy this requirement. Finally, the Coast Guard letter did not truly make a "claim" against Construction

Group, but "merely [sought] the contractor's acquiescence to being paid $6,028.55 and having the contract closed out."

NATIONAL FOCUS

CONSTRUCTIVE CHANGE OF CONTRACTS

Appeal of: AMEC Environment & Infrastructure, Inc., 2015 ASBCA LEXIS 104 (March 16, 2015).

AMEC Environment & Infrastructure, Inc. ("AMEC") was awarded a contract for a construction project at an Air Force Base in Maryland. The Maryland Department of the Environment ("MDE") requires all construction projects of one acre or more of earth disturbance to obtain an "Individual or General Permit for Stormwater Associated with Construction Activity." When AMEC prepared its bid, and when the contract was awarded, a general permit was in place. However, this permit lapsed a few months after AMEC began work. Due to an unrelated legal challenge, AMEC was unable to obtain a general permit and was forced to apply for an individual permit.

AMEC submitted a request for equitable adjustment to the contract seeking costs related to the additional expense of obtaining an individual permit. The claim was denied by the contracting officer, and AMEC appealed to the Armed Services Board of Contract Appeals. The government moved for summary judgment on this issue and the Board granted the motion.

AMEC's legal basis for their claim was a constructive change theory. "[T]o demonstrate a constructive change, the contractor must show: (1) that it performed work beyond the contract requirements; and (2) that the additional work was ordered, expressly or impliedly, by the government." The Board held that AMEC had not established either prong of this test. AMEC was not required to perform extra work beyond what the contract required. While AMEC was forced to apply for an individual permit, "'[t]he physical requirements to implement erosion controls in accordance with MDE standards . . . did not change' and AMEC did not request costs for any such work." Additionally, the extra expenses incurred by AMEC were the result of a change in state permitting requirements, that the Federal government had no role in. While it was not clear whether AMEC also asserted a claim for breach of contract, the Board dismissed any such claim as well. The contract explicitly required AMEC to obtain the permits at its own expense.

NATIONAL FOCUS

"FINAL" RELEASE

H.J. Lyness Construction Inc. v. United States, 2015 Ct. Fed. Cl. No. 11-129C LEXIS 16 (January 21, 2015).

The GSA terminated a contract for convenience and the contractor sought over $500,000.00 in settlement costs. The government claimed the contractor waived its right to seek those costs by executing a release of claims. The government claimed that a third release, was a "final release" that closed out the project and precluded any settlement sum. The contractor argued that the release was not a final release, but was limited to the third payment application and included change order work only. It was not a final contract release, or meant to waive or release any settlement amount. The contractor also argued that its

settlement proposal was timely under the FAR regulations which allow a contractor to submit a final termination settlement proposal to a contracting officer within one year from the effective termination.

In addition, the release language was required by the GSA with respect to all three payment applications submitted on the project, and all three applications could not be final payment applications. Thus, the government should not have considered the third payment application and its accompanying release as different or more extensive than the previous ones. The net result was that summary judgment was denied and the government was not able to dismiss the contractor's claim, but a trial and further proceedings would follow presumably focusing on the meaning, intent, and language of the alleged release form and its delivery.

NATIONAL FOCUS

ROOF WARRANTY

Appeal of: Alliance Roofing & Sheet Metal, Inc., 2015 ASBCA No. 59663 LEXIS 182 (May 4, 2015).

The U.S. Navy contracted with Alliance Roofing for roof repair and replacement at various locations in Washington. The contract was inconsistent regarding the extent to which Alliance had to provide roof warranties. Alliance purchased manufacturer limited warranties for repair of roof leaks which excluded damage caused by wind gusts in excess of 55 miles per hour. The Navy argued that Alliance had to comply with other standards which mandated a 115 mile per hour warranty for the EPDM membrane roofs. Alliance alleged breach of contract for the Navy's demand of warranty to cover wind speeds up to 115 miles per hour.

The Board of Contract Appeals noted that neither the Contract Specifications, nor any other criteria cited by the government, required a warranty covering damage from 115 mile per hour winds.

It held that the directive that Alliance provide 115 mile per hour wind warranties was beyond its contractual obligations. The government, therefore, received the provided 20 year warranty for damage caused by winds of less than 55 miles per hour on a few of the buildings. It was held there was nothing in the contract to support the government's requirement of a 115 mph warranty.

CONNECTICUT

NOTICE OF CLAIM

Electrical Contractors, Inc. v. Pike Co., 2015 U.S. Dist. LEXIS 70092 (D. Conn. May 29, 2015).

Electrical Contractors was the electrical subcontractor on a school renovation project claiming extensive cost overruns incurred when it had to "rush" to complete work on time during the school holidays. Electrical Contractors alleged that the general contractor, Pike, mismanaged the project, delayed, accelerated, and compressed Electrical Contractors' work, etc. The District Court ruled that these claims were invalid and barred by two primary contract provisions.

The first contract provision was the notice of claim provision. The project admittedly involved a tight schedule with multiple trades working concurrently working during the Summer 2010 recess. On July 21, 2010, the parties met to discuss project scheduling, and Pike denied Electrical Contractors' requests for more time and told Pike to increase its manpower to "get the job done". Electrical Contractors did not issue a written notice of claim until October 2010 which was beyond the subcontract provision that required notice of a claim within three days of the event giving rise to it. Although there was some correspondence and job minutes indicating Electrical Contractors' complaints about the scheduling, the Court ruled that these reports did not satisfy the requirement that Electrical Contractors notify Pike of a claim against it, or furnish Pike with actual knowledge of a claim.

The Court also ruled that Electrical Contractors' claim in October 2010 was barred by an unconditional lien waiver signed on September 21 executed as part of a payment application covering work performed through August 31, 2010.

KANSAS

PAY-IF-PAID PROVISIONS

APAC-Kansas, Inc. v. BSC Steel Inc., 2015 U.S. Dist. LEXIS 24589 (D. Kan. March 2, 2015).

The general contractor for a hospital construction project subcontracted with W&W Steel, LLC ("W&W") to perform a portion of that work. Liberty Mutual issued a Payment Bond in connection with that subcontract. W & W further subcontracted its portion of the work. One of W & W's subcontractors, BSC Steel, Inc. ("BSC"), subcontracted with APAC-Kansas, Inc. ("APAC") and American Riggers Supply, Inc. ("American Riggers"). APAC and American Riggers both completed the obligations under their subcontracts but received no payment and brought suit against W & W and Liberty Mutual seeking reimbursement under the Payment Bond. APAC and American Rigger both moved for summary judgment. Applying Kansas law, the District Court granted the motion.

Opposing the motion, W&W and Liberty argued that APAC's and American Rigger's construction contracts included "pay-if-paid" provisions that made payment conditional on payment to the upper-tier contractors. According to W&W and Liberty, since APAC and American Rigger had not shown that such payments occurred, they were not entitled to summary judgment. The court rejected this argument, holding that the provision in question was actually only a "pay-when-paid" provision. Pay-if-paid clauses make payment of the general contractor a condition precedent to payment of the subcontractor, shifting the risk of owner's nonpayment from the general contractor to the subcontractor. On the other hand, pay-when-paid provisions are merely timing mechanisms for payment schedules.

Under Kansas law, pay-if-paid provisions are enforced only if the language of the provision "clear[ly] and unequivocal[ly]" creates a condition precedent. Here, the relevant language provided that the "Contractor shall be obligated to pay Subcontractor only when Contractor receives payment." This was not the "clear and unequivocal" language the court was looking for.

LOUISIANA

DELAY DAMAGES

Gilchrist Construction Co., LLC v. State of Louisiana, 2015 La. App. LEXIS 483 (March 9, 2015).

Gilchrist Construction completed a highway construction contract some 130 days early for the State of Louisiana. Gilchrist received an early completion bonus but still sought additional $4 Million in delay costs allegedly due to extra quantities of embankment material used on the project. The State paid Gilchrist the cubic yard price for the material but Gilchrist argued it incurred additional damages due to the delay such as the cost of idle equipment and stock piled materials. Gilchrist claimed that placement of the extra embankment delayed the project by 180 days. The trial court ruled in Gilchrist's favor and on appeal the issue was whether Gilchrist properly proved it incurred any delay damages.

Neither Gilchrist nor the State provided an alternative delay analysis using an updated "as built" schedule. Despite discrepancies in the schedules offered by the various parties, the appellate court ruled it was proper to accept the impact schedules as evidence of delay. It found no error in the Trial Court's ruling and Gilchrist was entitled to recover costs incurred as a result of the delay it proved. Gilchrist essentially argued that, although it had accelerated its work due to other factors, without the excess embankment and fill quantities it still would have shaved 180 days off the completion date. Although the facts indicated that Gilchrist performed the embankment and fill work faster than shown on the approved schedules, the contractor still proved that by completing the job despite the extra quantities it still incurred 180 days of construction delay.

MARYLAND

CONTRACTOR AS ADDITIONAL INSURED

Capital City Real Estate LLC v. Certain Underwriters at Lloyd's London, 2015 WL 3606861 (Fourth Circuit June 10, 2015).

The Fourth Circuit in this case ruled that a general contractor was entitled to a defense as an additional insured on a subcontractor's insurance policy even though the subcontractor was not a party to the underlying lawsuit. The cause of the litigation was a wall shared by buildings in Washington, D.C. Capital City was the general contractor on the project, and it subcontracted foundation work to Marquez Brick Work. The subcontractor agreed to obtain general liability insurance listing Capital City as an additional insured, and the Lloyd's policy was obtained with an endorsement naming Capital City as an additional insured. The wall collapsed in June 2009 during the work. Capital City notified Lloyd's of the loss, and tendered all claims brought because of the wall collapse.

The insurance company for the property owner, Standard Fire Insurance, paid for the repairs and then brought a subrogation action against Capital City seeking to recover the $600,000.00 cost. This complaint did not name Marquez as a party. In response, Capital City filed a Third Party Complaint against Marquez for defense and indemnity. Lloyd's notified Capital City that it was denying coverage for the Third Party Action against Marquez. Capital City then sued Lloyd's in United States District Court, for a declaration that Lloyd's had a duty to defend the Standard Fire Insurance action under the Lloyd's-Marquez policy.

The trial court granted summary judgment to Lloyd's on the basis that the Standard Fire underlying complaint did not allege that Capital City was vicariously liable for Marquez's negligence. On appeal, the Fourth Circuit reversed and granted judgment in favor of Capital City.

The Appellate Court held that the Lloyd's policy provided coverage to Capital City as an additional insured for property damage caused in whole or in part by the named insured Marquez. The issue next turned to the question of whether the allegations in the underlying Standard Fire action created the "potential for coverage" and a duty of defense on the part of Lloyd's.

The Federal Court noted that, while Maryland does not allow an insurer to rely on extrinsic evidence to contest coverage, insureds may do so to show that underlying complaint allegations create the potential for coverage. In this case, Capital City's evidence that the subcontractor's work caused the wall collapse created the necessary linkage and potential for coverage for the loss event. The Fourth Circuit reversed the judgment in favor of Lloyd's and sent the case back to the District Court with instructions to enter judgment for Capital City.

The first lesson of this case is that all sides took the procedurally correct steps to place the case on a platform for the ultimate issues to be decided. The contractor Capital City brought a third party complaint against the subcontractor Marquez, triggering the possibility of coverage by Lloyd's. The contractor then brought an appropriate declaratory judgment action against Lloyd's to assert the additional insured coverage.

The second lesson of this case is that, while the pleadings remain important and perhaps determinative in reviewing coverage issues, some states allow "extrinsic evidence" to expand upon the factual allegations in a complaint which might lead to coverage. Such extrinsic evidence might include expert reports, appraisals, repair invoices, etc. providing further and perhaps more detailed information concerning a loss, potential causes of the loss, and the types of damages incurred. In this case, while the Standard Fire complaint contained no allegations against the subcontractor, Capital City was able to establish that the nature and cause of the loss nonetheless potentially arose from the subcontractor's work thereby triggering potential coverage. It was undoubtedly assisted in this case due to the fact that the wall collapse most certainly implicated work of the foundation subcontractor.

The third lesson of this case is that federal district courts generally are tasked with applying state law to the best of their ability, and whether there is controlling state law on a subject and how to apply it can often be difficult to determine. Federal trial courts may be reluctant to overly extend state substantive law, preferring to defer to the state courts and refrain from establishing what might become controlling authority on a certain issue. In this case, the Fourth Circuit determined that Maryland law would allow the contractor to present "extrinsic evidence" indicating possible coverage even if the underlying pleadings were silent or did not clearly trend in that direction.

MICHIGAN

NO DAMAGES FOR DELAY CLAUSE

Macomb Mechanical, Inc. v. LaSalle Group, Inc., 2015 Mich. App. LEXIS 833 (April 23, 2015).

Macomb Mechanical a sub-contractor sought compensation under a surety bond for costs due to project changes and delays. The trial court dismissed the claims because of "no damages for delay" and "pay if paid" clauses in its contract. These decisions were reversed on appeal.

Macomb's plumbing and mechanical work was scheduled for six months, but delays and interruptions extended the time to more than 15 months. The sub-contractor defended the claim siting a no damages for delay clause in its contract with Macomb. However, Macomb claimed that the delays in this case were not contemplated by the parties, and that no one anticipated a nearly 10 month delay in the bid and contract. The appellate court held there was a valid question of fact whether the parties contemplated such an extensive delay to the work.

The appellate court did interpret the clause as a pay if paid clause, but Macomb successfully made out an argument that much of its claim was for work done outside the original agreement, and if the work was "extra-contractual" pay if paid provisions would not bar recovery.

PENNSYLVANIA

CGL COVERAGE FOR CONSTRUCTION DEFECTS

Pennsylvania National Mutual Casualty Insurance Co. v. St. Catherine of Siena Parish, 2015 WL 3609353 (11th Circuit June 10, 2015).

The Eleventh Circuit Court of Appeals reversed a trial court ruling and held that Penn National had to indemnify its insured under a CGL policy for a construction defect claim. The Parish hired Kiker Corp to repair its roof and replace shingles. In the course of that work, Kiker learned that the roof deck was made of gypsum panels. Kiker attached the new shingles directly to the gypsum deck using a special fastener. The Parish again hired Kiker two years later to repair leaks on another roof. A few months later, water began to leak through the ceiling. The Parish alleged that Kiker's use of the special fasteners to the gypsum deck caused the leak, and that problems with the second roof were also allegedly caused by Kiker's work. The Parish sued Kiker in Alabama State Court, and the company put Penn National on notice of the claim. The insurer provided a defense under a reservation of rights.

A jury awarded the Parish $350,000.00 in damages. Penn National filed suit in the Southern District of Alabama seeking a declaration it did not have a duty to indemnify Kiker for the verdict. The District Court granted Penn National's Motion for Summary Judgment finding that the policy's "contractual liability" exclusion precluded coverage. This typical exclusion stated that coverage was not available for damages the insured might become obligated to pay by reason of the assumption of liability by contract or agreement.

On appeal, however, the Eleventh Circuit reversed the judgment, and ruled that the policy provided coverage for property damage caused by an "accident". The Court held that an "accident" does not necessarily occur when a contractor performs faulty work, but may occur under Alabama law if the faulty work/defect creates a condition that causes property damage.

The damages in the underlying litigation were for the cost of repairing water damage to the ceilings, fixing improper installation of shingles, and destruction of the gypsum decking. Since Kiker did not work on the ceilings, they were not part of the alleged faulty work/defect, and the water damage thus arose from an "accident". The Court also found that damage to the decking resulted from an accident because Kiker did not really perform work on the decking either. The cost of removing and replacing the shingles was covered because those tasks necessarily had to be undertaken to repair the underlying damaged roof deck.

Consequently, the Appellate Court reversed Penn National's Summary Judgment and directed the case back to the District Court with instructions to enter judgment in favor of the Parish.

This case represents a recent and continuing dialogue on whether and when construction defects are covered by a contractor's CGL liability policy. This case gives the issue a fairly thorough treatment focused on Alabama state law.

One of the common issues is whether a construction defect is truly an "accident", with many cases and courts holding that a construction defect may be accomplished with intent and purposefully, and therefore is not an "accidental occurrence" that triggers coverage. The analysis in this case is somewhat unusual since whether or not the defect was an accident, according to this Court, seems to depend on the outcome and not on the act itself. This Court seems to say that, if there is damage to property which is not strictly speaking part of the construction work or defect, that may constitute an "accident" which appears to be an odd analysis. Most cases discussing this issue have focused on whether the construction defect was intended, a surprise, or not to be expected and therefore an accident.

This case also discusses the common contractual exclusion argument. Many construction defect claims and related breach of warranty claims are barred by various contractual liability exclusion clauses in CGL policies. The Court argued that the breach of warranty claim, while requiring a contractor to use reasonable skill, did not constitute "assumption of liability" under a contract, whereas other courts and cases have held that such claims are indeed contractual in nature and subject to the policy exclusion.

Some states have fairly universally denied coverage under CGL policies for construction defects, whereas Alabama apparently draws a common distinction where a construction defect might be covered if it damages personal property other than the construction work itself. However, this case is fairly unique in extending that analysis to determine whether an "accident" had occurred in addition to covered property damage.

This issue has become very contested, convoluted, and contradictory on a national basis, and even within states. State courts have issued conflicting rulings that are often overturned or modified on appeal, and the federal courts have consequently struggle to interpret and apply perceived state law. Many states have had to address this issue by statute or insurance regulations to clarify the extent of construction defect coverage.

RHODE ISLAND

ARBITRATION AWARDS -- JUDICIAL REVIEW

Atwood Health Properties, LLC v. Carlson Construction Co., 2015 Sup. Ct. R.I. LEXIS 36 (March 16, 2015).

Atwood Health Properties, LLC ("Atwood") contracted with Carlson Construction Co. ("Carlson") to build an office building. Carlson subcontracted with Gem Plumbing & Heating Co., Inc. ("Gem") to design and install an HVAC system. After experiencing compressor failures for several years, Atwood replaced the HVAC system and initiated arbitration proceedings to recover those costs. The arbitrator concluded that Carlson breached its contract with Atwood and instructed Carlson to pay Atwood $358,223.42. Relying largely on an indemnification clause in Gem's contract with Carlson, the arbitrator concluded that Gem breached its contract with Carlson and instructed Gem to pay Carlson the amount

Carlson had to pay Atwood. A trial court confirmed the award. Gem appealed and the Rhode Island Supreme Court affirmed confirmation of the award.

Gem argued that the arbitration award should be overturned because the arbitrator erroneously interpreted the indemnity clause in Gem's contract with Carlson. The Supreme Court agreed with Gem that the arbitrator's construction of that clause—which indemnified Carlson for Gem's negligent acts but not negligent performance of the subcontract—was error but held that this legal error was not sufficient grounds for overturning the award: "An arbitrator's award will not be overturned for mere errors of law." When an arbitrator's award is based on an erroneous construction of a contract, the award will be upheld as long as the interpretation is "plausible and rational and did not manifestly disregard the law." While the arbitrator got the indemnity clause wrong, the contract, taken as a whole, clearly contemplated Gem designing and installing a sound HVAC system and taking economic responsibility for failure to do so. In that light, the arbitrator's award was sufficiently "grounded in the contract" and within the scope of his authority.

WASHINGTON

LIMITATION OF LIABILITY CLAUSE

URS Corp. v. Transpo Group Inc., 2014 U.S. Dist. LEXIS 11340 (W.D. Wash. January 30, 2015).

URS was the lead designer on a highway project for the state of Washington, and Transpo provided design services for the design of road sign panels. Some of these sign structures failed to meet contract requirements, URS withheld payments from Transpo, and litigation ensued. One of the issues was whether URS waived its right to damages under a limitation of liability contract clause. Transpo argued that a Teaming Agreement applied which contained a limitation of liability clause barring lost profits, consequential damages, etc. URS claimed that a later Master Subcontract Agreement governed the dispute which provided that it superseded all prior agreements with respect to its subject matter. The Court ruled that the subject matter of the two documents was different. The Teaming Agreement involved pursuing the contract and the Master Subcontract Agreement addressed post-award work. The Court concluded that the Master Subcontract Agreement could not supersede and therefore negate the limitation of liability clause. This was based on a line of cases generally holding that a subsequent contract not pertaining to precisely the same subject matter will not supersede an earlier contract unless the later contract contains express language canceling the prior agreement.

Transpo also cited "flow down" provisions in the Teaming Agreement that incorporated terms of the prime contract URS had with the design-builder which also included a limitation of liability clause.

While upholding the effectiveness of the limitation of liability, the Court did not determine what specific damages might be included or excluded from recovery, as for example what damages might be considered lost profits or consequential damages and excluded, and those that might be direct damages resulting from the alleged breach of the design contract.