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

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This last edition of the Tool Box for 2015 includes some cases on new and unusual topics such as the inter-relationship of construction law and cases with the "Buy American Act," expert witness testimony, the "parol evidence" rule and even governmental-sovereign immunity.

Happy Holidays, good reading, and see you next year.

- The Editor

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NATIONAL FOCUS
BUY AMERICAN ACT

U.S. ex rel Michael Kress v. Masonry Solutions International, Inc., 2015 U.S. Dist. LEXIS 73907 (E.D. La. June 8, 2015.)

A False Claims Act plaintiff claimed that his employer submitted false claims because materials did not comply with the Buy American Act. The BAA covers materials or supplies that are "mined, produced, or manufactured in the United States." Manufactured in the United States is satisfied if the cost of the U.S.-origin components exceeds 50%. Compliance may also be achieved if operations performed on foreign items in the United States create a basically new material, or result in a substantial change in physical characteristics.

The employer argued that items complied with the BAA because more than 50% of the product's end value was the result of domestic manufacturing operations, and that other items were manufactured through a cold-forging process which changed the molecular properties of the material, thus resulting in a new item "manufactured" in the United States.

The Court agreed with the employer and accepted these arguments, as well as an additional argument that one of the countries of origin - England- was exempted from BAA restrictions under various trade agreements.

NATIONAL FOCUS
CONSTRUCTIVE CONTRACT CHANGE

Appeal of: MarCon Engineering, Inc., 2015 ASBCA No. 57471 LEXIS 167 (May 1, 2015).
MarCon was the general contractor on a design/build project for border fencing in Arizona. The project specs required all construction activities to be contained within a corridor limited to a 60 foot strip adjacent to the border. The government alleged that MarCon's work did not strictly conform, MarCon alleged that the government relaxed these restrictions by accepting the contractor's design, and the Armed Services Board of Contract Appeals (ASBCA) accepted the contractor's position.

MarCon's work plan was to follow the natural contours of the land which required some limited work outside the restricted area. This design was accepted and MarCon relied on the government's acceptance of its design. The contractor stated that the contractual drainage plan submitted by MarCon modified the contract provisions, and upon the government's acceptance the specifications were deemed changed and "relaxed". The Board held that MarCon was entitled to an equitable adjustment for its claim. The incorporation of MarCon's design/build proposal served to modify the contract.

NATIONAL FOCUS
CONTINUATION OF WORK

JJK Group, Inc. f/k/a John J. Kirlin, Inc. v. VW International, Inc., 2015 U.S. Dist. (M.D. March 27, 2015).

In this case the government demanded that the contractor repair a nurse call system during a one year warranty period following its installation. The government ultimately revoked acceptance of the system

based on "latent defects", and directed the contractor to replace it at no additional cost. The issue was whether the F.A.R. Disputes Clause required the contractor to perform immediate corrective work.

The contractor argued that the government accepted the original call system two years before, and that the Disputes Clause is inapplicable post-contract acceptance. The contractor argued that, after contractual acceptance, the burden shifted to the government to prove a defect before the contractor was required to act. However, the contractor lost this contest.

The Court ruled that decisions support the notion that a government contractor must proceed with work the government demands even if it believes the government's directions are wrong. The contractor was required to perform the work and then seek an equitable adjustment later. This was so even though the call system was installed many months earlier, and the work had been accepted by the government.

NATIONAL FOCUS
DIFFERING SITE CONDITIONS

Meridian Engineering Co. v. United States, 2015 U.S. Ct. Fed. Cl. LEXIS 905 (July 22, 2015).

Meridian contracted with the Corps of Engineers to complete a flood control project in Arizona which became plagued with flooding and water problems. Meridian said the delays were caused by ground water on the job and soft subsurface soil conditions, and essentially argued to the Corps that there were differing site conditions. The government argued that the contract gave notice of saturated soils, flowing water, and that the worksite may become inundated because of runoff. The government also argued that a site visit would have revealed various areas of saturated soil upon inspection. The government further argued that the site was on a known flood plain, and that the very purpose of the project was to control flash floods and drainage. The Court held that Meridian had proved neither a Type I or Type II differing site condition.

Meridian also argued that its contract performance was hindered by working in the winter and periods of inclement weather, but this claim was also rejected since there already had been an adjustment to contract time and price for weather delays, and the contract schedule had always planned some work during periods of bad weather.

NATIONAL FOCUS
DIFFERING SITE CONDITIONS

Old Veteran Construction, Inc. v. United States, 2015 U.S. Ct. Fed. Cl. LEXIS 615 (May 19, 2015).

The contractor here sought a price adjustment because it allegedly bid with summer work in mind and wanted to recoup extra money to contend with winter weather conditions. The contractor claimed it bid the job anticipating favorable weather conditions since a specific award date was apparently never identified. The initial bid date, however, was in May 2011, and the contractor believed work would take place shortly thereafter. Unfortunately, notice to proceed was given in October 2011, the contractor began excavation in 2012, and ran into wet clay and frozen ground conditions.

The government called the contractor's assumption that work began in the Summer of 2011 unfounded. The solicitation apparently contained language that a Winter start date was possible, and the contractor had made changes to its proposal once it became clear that Summer work was unlikely. If this was a Type

I differing site condition, the government argued that the site conditions encountered were what the geotechnical report had specified. The report explicitly stated that the soil and clay would not be suitable for use as engineered fill during colder and wetter months. The Court agreed with the government and granted a motion for summary judgment dismissing the claim.

NATIONAL FOCUS
EXPERT TESTIMONY

Waste Management of Louisiana, LLC v. Jefferson Parish, 2015 U.S. Dist. LEXIS 135529 (E.D. La. October 5, 2015).

Waste Management maintained a landfill for the Parish. Waste Management terminated its contract, and in the following dispute, the Parish designated an expert witness. Waste Management filed a motion to exclude the expert report and potential testimony.

The first argument was that the expert demonstrated no expertise in landfill engineering. Waste Management also argued that much of the expert report revolved around interpreting sections of the contract with the Parish and amounted to legal interpretation of the contract as opposed to expert testimony. Waste Management argued that this essentially would take over the Court's role by providing contract "interpretations" and conclusions of law.

The Court did allow the expert to testify since he demonstrated more than 30 years of engineering experience in a field of sewage systems, site engineering, land surveying, and structural engineering. The Court found no basis to exclude the witness' testimony in its entirety. The Court did agree that a large part of the report spoke to alleged duties and interpretations of the contract, and to whether the parties had acted "reasonably". Some of the experts' opinions, therefore constituted legal conclusions and should be stricken. However, the expert could still potentially offer testimony on the subject under the guise of industry norms and practices as to what understandings and practices in the industry would be with respect to a certain subject or duty. In short, the expert was not wholly barred from testifying, but he was not allowed to testify on matters of strict contractual interpretation or legal conclusions.

CALIFORNIA
CONSTRUCTION DEFECT

American Home Assurance Co. v. SMG Stone Co. Inc., 2015 WL 3638363 (N.D. Cal. June 11, 2015).

In many respects, California is heavily involved in construction defect litigation, and a recent ruling in California relieved two insurance companies of any obligation to defend and indemnify with respect to claims of alleged faulty tile installation in a condominium development in Los Angeles. The District Court granted summary judgment to American Home Insurance Co. and Insurance Company of the State of Pennsylvania.

A developer hired Webcor Construction to build a 54 story hotel and luxury condominium in downtown Los Angeles. Webcor subcontracted installation of stone floor tiles to SMG Stone Co. Eventually, fractures in the floor tiles were discovered, and many had to be removed and replaced, with the remediation also requiring removal and replacement of drywall and the concrete sub floor. The developer initiated an arbitration proceeding against Webcor, the general contractor, and SMG Stone Co. Webcor paid $8 Million to settle the dispute, including $7 Million paid by its insurer. SMG and another contractor

subsequently sued Webcor for non-payment of services. In a cross claim, Webcor sought recovery of sums expended to repair, replace, and remediate SMG's allegedly defective work. These claims were tendered for defense to the insurance companies who denied coverage and filed a declaratory judgment action.

On competing cross-motions for summary judgment, the District Court did conclude that fracturing of the stone tiles caused by allegedly defective installation was the result of an insured "occurrence". However, the Court ruled there was no obligation to defend or indemnify because the fracturing of the floor tiles did not constitute "property damage", which the policies defined as physical injury to tangible property, including resulting loss of use of that property, or loss of use of tangible property that is not physically injured. The Court applied the rule from California cases that coverage does not exist where the only "property damage" is to the defective construction itself, and damage to other adjoining or existing property has not occurred.

The Court rejected an argument that the damage to the concrete subfloors and interior walls during removal and reinstallation constituted requisite "physical injury" and "property damage". The damage to the subflooring and drywall did not result from the defective floor tile installation itself. Rather, the damage was the result of remediation of the defective floor tile, and under California law remediation work does not constitute "property damage".

CALIFORNIA
CONSTRUCTION DEFECTS: MISREPRESENTATION

Monier Inc. v American Home Insurance Co., 2015 WL 3814493 (Cal. Ct. App. June 18, 2015).

California homeowners brought a class action against Monier, a manufacturer of roof tiles, and the state court action claimed that roof tiles deteriorated well before expiration of a 50 year warranty. American Home and several other companies denied coverage due to the lack of a defined accidental occurence. Monier then sued a number of insurers seeking a declaration that they had an obligation to provide defense and indemnification in the class action.

After a bifurcated bench trial, the trial court concluded that the insurance companies did not have a duty to defend because the class action did not allege a covered "occurrence". On appeal, this decision was affirmed. The essential basis for the ruling was that the claims alleged arose from claimed misrepresentations regarding the roof tiles were intentional, non-accidental actions outside the scope of potential coverage.

Monier argued that the complaint included a claim under the California Consumers Legal Remedies Act which could be based on unintentional conduct. However, this theory was rejected by the appellate court because the class action was essentially based upon misrepresentations, which are intentional acts whether made knowingly or negligently.

Monier also raised the argument that, while "misrepresentation" may have been a stated legal theory, the class action claims really arose from an unintentional product defect in the roofing tiles. The appellate court also rejected this analysis holding that the factual allegations in the complaint were that class members were damaged by misrepresentations concerning the tiles, not by some defect in manufacturing or application.

DELAWARE
BOND CLAIMS AND CHOICE OF LAW

VSI Sales, LLC v. International Fidelity Insurance Co., 2015 U.S. Dist. LEXIS 126392 (D. Del. September 22, 2015)

VSI Sales supplied construction materials to a subcontractor on a highway project and sued under the payment bond for improperly handling its claim. The question was whether the Delaware choice of law provision in the subcontract applied to the surety bond dispute. VSI argued that Delaware law applied because its claims arose from the bond, and the bond referred to the subcontract and its choice of law provision. The surety argued that the bond did not incorporate the subcontract choice of law provision, that Pennsylvania law applied, and did not recognize a claim of bad faith against a surety, or a separate claim for breach of an implied covenant of "good faith and fair dealing". The Court agreed with the surety company holding that incorporation by reference of a contract into a bond is not intended to bring the substantive provisions of the contract into the bond. Rather, the incorporation establishes the limits of the surety's obligation, and provides a basis for measuring any performance that may be required. Furthermore, the choice of law provision in the subcontract stated that "this subcontract" shall be governed by Delaware law and this language itself restricted its application to disputes arising out of the contract itself. Therefore, Pennsylvania law applied, and therefore several of the claims were subject to dismissal as not actionable under Pennsylvania law.

ILLINOIS
INSURANCE COVERAGE – DUTY TO DEFEND
MEASURING THE DUTY TO DEFEND

Pekin Insurance Co. v. Martin Cement Co., Inc., 2015 WL 5139356 (Ill. App. Ct., September 2, 2015).

In this case, an Appeals Court in Illinois held that an insurance company owed coverage to a contractor as an additional insured under a policy issued to its subcontractor. The plaintiff, Jake Swartz, was injured in July 2010 when rebar broke from a building causing him to fall. His employer was Platinum Steel, a subcontractor to Martin Cement. The subcontract agreement required Platinum to maintain insurance naming Martin as an additional insured. Swartz sued Martin and one other party for his injuries, and the defense was tendered to Pekin which insured Platinum under a CGL policy. Pekin Insurance rejected the tender arguing that the policy only covered Martin for vicarious liability imputed through Platinum to Martin, but did not apply to claims arising from Martin's own alleged negligence. A declaratory judgment action was eventually filed with Pekin and Martin filing competing summary judgment motions with respect to the tender of coverage.

Pekin argued that the Platinum policy did not cover Martin because Swartz alleged direct negligence against Martin, and the Platinum policy only applied to vicarious or imputed claims against Martin. Martin alleged that the claims against it were potentially the responsibility of Platinum, and that Platinum was actively at fault. The trial court granted summary judgment to Pekin Insurance, declining to consider the content or allegations of a third party complaint. The Appellate Court reversed. The Appellate Court held that the trial court should be able to consider all of the relevant facts contained in the pleadings, including third party complaints and counterclaims, to determine whether there may be a

duty to defend. The third party complaint made sufficient allegations that actions or omissions of Platinum may have caused the injuries, making summary judgment in favor of Pekin Insurance on the duty to defend in error. The summary judgment for Pekin Insurance was reversed, and the case was remanded to the trial court to enter summary judgment for Martin Cement in the declaratory judgment action.

The existence or non-existence of coverage is largely determined by the allegations within the four corners of the pleadings. This case stands for the proposition that courts may consider all of the relevant pleadings including answers, cross claims, counterclaims, and third party complaints, to review the factual allegations and legal theories of recovery and liability to determine whether a coverage threshold triggering the duty to defend has been crossed.

MASSACHUSETTS
CONSTRUCTION MANAGER AT RISK

Coghlin Electrical Contractors, Inc. v. Gilbane Building Company, 2015 Mass. LEXIS 621 (September 2, 2015).

An electrical subcontractor incurred costs due to defects in the building design and sued the construction manager for breach of subcontract. The issue was whether the owner of a CMAR project warrants the project design. The subcontractor discovered that the design allowed for just two feet of space between ceilings and the bottom of structural steel while also anticipating approximately five feet of mechanical and electrical work to be placed in the area. The construction manager initially argued that the project owner was responsible for damages caused by errors unrelated to any wrongdoing on the part of the construction manager. The trial court disagreed and held that the owner's implied warranty applies only where the construction project uses traditional design-bid-build-construction methods. However this ruling was reversed on appeal.

The CMAR delivery method is a hybrid between the traditional method and design-build approach. Typically, an implied warranty attaches when a project owner has complete control over the design process and the contractor has none. However, that is not the case in an at-risk contract where the CMAR may consult and have input on the design. However, even in an at-risk contract the owner ultimately controls the design. The Court ruled that the owner's implied warranty would be limited and reduced by the contractor's own design responsibilities. The more the CMAR has to do with design, the higher its burden would be to show the owner's liability under an implied warranty with respect to the design.

Here, the prime contract delegated to the contractor or construction manager extensive design responsibilities. The CMAR was required to consult on an instruction plan, study all design-related documents, verify field conditions, etc. On the other hand, the prime contract clearly placed the CMAR in a subordinate position regarding the project design. In short, the Court ruled that if the construction manager was found liable to the electrical subcontractor, it may be able to recover from the owner to the extent that additional costs were caused by reasonable and good faith reliance on the owner's defective design and the owner's control over the design.

This design in essence adopted a "sliding scale" analysis for design liability. The more the construction manager is involved in design development and review, the less able it is to argue that it reasonably relied on what is later discovered to be a defective design. Because the case had been

dismissed without factual inquiry as to the nature and extent of the construction manager's design involvement, the dismissal was reversed.

MISSOURI
ARBITRATION CLAUSES

Winco Window Co. Inc. v. G&S Glass & Supply, Inc. 2015 WL 3604072 (E.D. Mo. June 5, 2015).

The Court compelled arbitration even though a window supplier did not accept a purchase order submitted by the general contractor containing an arbitration provision. This was because the supplier's own terms and conditions contained an arbitration provision as well. Both provisions incorporated AAA arbitration rules which, inter alia, empower an arbitrator to determine his/her own jurisdiction. Since the supplier in fact did provide the windows, the general contractor accepted them, and the supplier's own documentation contained in the arbitration provision, the terms of the parties' agreement contained provisions which from the records of both parties included the arbitration provisions. Therefore, this matter which involved a dispute concerning procurement of windows for a construction project was referred to arbitration for resolution.

NEW MEXICO
LIMITATION OF LIABILITY FLOWDOWN CLAUSES

Centex/Worthgroup, LLC v. Worthgroup Architects, LP, 2015 N.M. App. LEXIS 101 (September 10, 2015).

The prime construction contract was between a resort and Centex/Worthgroup and the subcontract entered into with the architects. When a stabilized earth wall failed, Centex sued the architects for nearly $7 Million in damages for redesign and repair costs. The prime contract included a limited liability clause which stated that the owner agrees it will limit design/builder's liability to the amount of insurance coverage. This provision was alleged incorporated into the architects' subcontract by a flowdown clause stating that the architects have all the rights toward Centex which Centex has under the prime contract towards the owner, and the architects assume all the obligations, risks and responsibilities towards Centex which Centex assumed towards the owner with respect to the design work. The architects argued that their monetary obligations to Centex were satisfied by the payment of the insurance coverage that it was contractually obligated to procure and maintain.

Centex countered pointing to the general liability clause in the subcontract which held the architects responsible, without limit, for redesign costs and reconstruction costs required to correct the architects' errors or omissions. The language in the flowdown clause limited the clause's scope because the flowdown clause did not incorporate the limitation of liability clause from the prime contract because the subcontract already covered the liability between Centex and the architects. The New Mexico appellate court agreed. It limited the flowdown clause so that it only applied to rights, obligations, risks and responsibilities in the prime contract, and that the subcontract did not otherwise allocate. The specific section in the architect's agreement providing for a greater liability and responsibility imposed a "higher standard" of liability and therefore took precedence over the flowdown clause.

NEW YORK
PAROL EVIDENCE

Science Applications International Corp. v. Environmental Risk Solutions, LLC, 2015 N.Y. App. LEXIS 7928 (October 29, 2015).

Several gas station sites were contaminated by petroleum, and Environmental Risk Solutions was hired as the environmental remediation contractor. ERS hired Science Applications to perform on site remediation work. Science Applications eventually filed a mechanics' lien and sued ERS for breach of contract upon non-payment. The primary issue was how the subcontract defined the scope of Science Applications' work.

ERS and Science Applications had a Professional Services Master Agreement, but also entered into 3 separate but basically identical subcontracts designated as Project Specific Scopes of Work. In part, the subcontracts required Science Applications to meet a contractually defined "cleanup standard", but the subcontracts also permitted remediation to the extent of receiving a "no further action" letter from the DEC. The New York courts ruled that parol evidence was necessary to determine the parties' intent with respect to the required level of performance/completion.

Science Applications definitely complied with the less stringent DEC standard. It obtained closure of DEC files at each of the 18 sites, where it completed its work. However, it was argued that residual petroleum contamination still remained at the 18 sites and that the contractually defined and stricter "cleanup standard" had not been met. The courts looked at the course of performance which showed that there had been no objections made to Science Applications' remedial actions, and Science Applications was never requested to perform additional remediation to satisfy the more stringent cleanup standard. The courts ruled that Science Applications had sufficiently performed its remedial obligations under the subcontracts.

There was also a fraud allegation in the case which was dismissed for two reasons. First, the parties had full opportunity to comment on Science Applications' action plans for each site, so there could not be any real misrepresentation or detrimental reliance. Second, these claims were largely duplicative of the breach of contract causes of action and defenses and subsumed within that analysis and outcome.

NEW YORK
PRIVITY OF CONTRACT

Greg Beeche Logistics, LLC v. Skanska USA Building, Inc., 2015 U.S. Dist. LEXIS 116980 (D. Mass. September 2, 2015).

Beeche, a scaffolding subcontractor, alleged extra expenses on a renovation project at the UN Building in New York City. The project contractor denied much of the extra work requests, so Beeche then sought the remainder from Skanska, the project's Construction Manager. Beeche alleged that Skanska had approved payments for the extra work in two separate e-mail messages. However, the Court granted Skanska's motion for summary judgment.

The first ground was the lack of privity between Beeche and Skanska. The parties did not contract directly, and their separate agreements specifically provided that they did not create contractual relationships with third parties. New York law prohibits a sub from bringing a breach of contract claim

against an owner or general contractor absent privity of contract. Beeche's subcontract in fact stipulated that requests for payment had to be made directly to the contractor.

The terms of the project contract also denied Beeche's unjust enrichment claim because in New York an express agreement on the subject at issue bars an unjust enrichment claim. Here, the Court said that the subcontract governed disputes over extra work and, even though Skanska was not a party to the subcontract, that contract barred Beeche's claims.

NORTH CAROLINA
CONTRACTUAL DELAYS

Flatiron-Lane v. Case Atlantic Company, 2015 U.S. Dist. LEXIS 102539 (August 4, 2015).

Case Atlantic was hired to construct support shafts for highway bridges. Case's method of installation was appropriate and approved and had an estimate of 16 weeks for completion. The work actually took 44 weeks and required a re-design since the plan could not accommodate construction methods. Eventually Flatiron sought delay damages for 22 weeks of work. The court ruled that Flatiron knew or should have known that the design was inconsistent with proposed construction methods. The general contractor's failure to coordinate between Case and the designers led to re-designs that delayed the work. However, the subcontract put the burden on Case to use means and methods consistent with the plans and specifications. It did not give Case the right to insist on the work being designed to suit its construction preferences.

The Court also ruled that Case shared some responsibility. The Court eventually agreed that Flatiron's delays breached the subcontract, but it ruled that Flatiron failed to prove any measure of damages. North Carolina law bars a party from recovering damages where both parties contribute to the delay unless there was proof of clear apportion of the delay and expense attributable to each party. In this case, the parties simply blamed one another for the delays, but did not offer any proof or apportion of the delays and costs.

TEXAS
SOVERIGN IMMUNITY

City of Galveston v. CDM Smith, Inc., 2015 Tex. App. LEXIS 3249 (April 2, 2015).

Several years ago, Texas loosened the rules of Sovereign Immunity for local government entities and held that governmental entities that entered into contracts for goods or services were not immune to breach of contract suits. In this case, the parties argued whether there was in fact of contract for services. The Texas Court of Appeals construed the term "services" broadly and held that the unpaid contractor could sue the City of Galveston. Galveston entered into a contract with CDM Smith as its "program administrator" to allocate federal hurricane relief funds. CDM would invoice the City, the City would review the invoices for regulatory compliance, and then forward the invoices to the appropriate state agency for payment. When the city fell behind in submitting and paying invoices, CDM initiated its lawsuit.

The City argued that it was still entitled to governmental immunity because the contract was missing an essential term, specifically regarding payment. The City argued that there was no blanket agreement to pay CDM, and that in fact any "payments" came from other sources such as state agencies or the federal

government. The Court disagreed and held that the contract did state sufficient essential terms such as the names of the parties, the property at issue, and basic obligations. The Court ruled that the contract set forth the City's basic obligations with regard to payment.

The City also argued that the immunity statute did not apply because the contract was not for services to the City but rather to identify and direct funds to citizens whose homes were in need of repair due to hurricane damage. The Court disagreed with this argument also because it found that the services benefitted not only individual citizens but also the City itself by providing program management, project development and creation of master plans and housing studies. The Court of Appeals gave the word "services" a broad definition to include generally any act performed for the benefit of another under some arrangement or agreement whereby such act was to have been performed. Therefore, there was a contract for services between CDM and the City, and the City was not immune from the breach of contract claim.

WASHINGTON
TERMINATION FOR CONVENIENCE

SAK & Associates, Inc. v. Ferguson Construction, Inc., 2015 Wash. App. LEXIS 1871 (August 10, 2015).

SAK was a subcontractor who sued the General Contractor, Ferguson Construction, after an airport hangar construction project was "terminated for convenience". SAK alleged that Ferguson breached the subcontract by unilaterally terminating without cause. The trial court dismissed these claims, and on appeal the argument was that the termination for convenience clause made the contract illusory and therefore unenforceable. The appellate court ruled that the right to cancel an agreement was illusory only if there was no limit on the power of cancelation. Indeed, for some courts, a written notice requirement may even be deemed sufficient. This contract provided that upon termination for convenience, the subcontractor would be compensated for work actually performed in an amount proportional to the total subcontract price. SAK had performed approximately 25% of the work at the time of cancelation and it was paid out proportionately for that work. Thus, the court reasoned, partial performance was adequate consideration to make the clause enforceable. The termination for convenience clause was not vague, illusory, or without consideration.