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

A Service of The Harmonie Group Construction Law Committee

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Introduction

This is the Third Edition of Harmonie's Construction Tool Box.

Items of interest include Design-Build Contracts, some interesting insurance coverage construction cases, and statutes of repose and statutes of limitation.

Please accept Harmonie best wishes for a successful 2012 Calendar Year, an even better 2013, and a happy holiday season.

- The Editor

Index of Topics Covered

National Focus

Contractual Duty to Obtain Permits

Bell/Heery JV v. United States, 2012 U.S. Claims LEXIS 929 (Fed. Ct. Cl. July 31, 2012).

The claimant in designing and building a New Hampshire prison for the Federal Bureau of Prisons ("FBP") agreed to comply with State laws, regulations, and permitting requirements. The New Hampshire Department of Environmental Services made multiple changes to the construction plans costing the contractor an extra $8 Million to phase and build the prison. The FBP refused to reimburse the contractor for the additional costs on grounds that the contractor assumed the risk of the State actions and the obligation for obtaining State's permits. The Federal Court of Claims agreed with the FBP.

The contract contained a fairly standard FAR clause entitled "Permits and Responsibilities" which makes the contractor responsible, without additional expense to the government, for obtaining necessary licenses and permits, and for complying with any federal or state laws applicable to performance of the work. Despite the contractor's arguments to the contrary, the Court ruled that the contract did not impose any liability on the FBP or impose on the FBP a duty to deal with the state agencies on behalf of the contractor. The FAR clause and other contract documents dealing with construction permits and regulations assigned responsibility for permits to the contractor and not the government.

National Focus

Government Contracts - Compliance With Solicitation

Matter of Carothers Construction Inc., 2012 U.S. Comp. Gen. B-405241.1 (July 26, 2012).

The Corps of Engineers RFP to build an elementary school in Georgia required not less than 30% of the hot water demand for the school to be met through installation of solar hot water heaters unless demonstrated not to be life cycle cost-effective. The Corps awarded the contract to a higher-priced bidder and another contractor, Carothers, appealed. The Corps said that Carothers failed to meet the solar heat requirement, but Carothers disagreed and charged the Corps with using an unstated or imprecise bid evaluation factor.

Carothers' proposal called for using a high-efficiency gas-fired hot water heater. Carothers claimed that a solar domestic hot water system would not be cost effective. The Comptroller General rejected the protestor's arguments. The solicitation clearly required the 30% solar heat benchmark or demonstration that it would not be cost effective, and Carothers clearly did not meet that criteria. Furthermore, Carothers' "cost effectiveness" analysis was only based on the school kitchen which comprised only 60% of the overall school hot water usage. The Corps therefore had reasonable basis to find the cost-effectiveness rebuttal analysis inadequate since it did not pertain to the entire facility's hot water consumption. In addition, the cost-effectiveness argument was not contained in Carothers' proposal, but was only presented in "discussions" with the Corps.

National Focus

Government Contracts - Differing Site Conditions

Appeal of Strand Hunt Construction Inc., 2012 ASBCA No. 55904 Lexis 48 (June 21, 2012).

Strand Hunt contracted to design and build emission reduction facilities at a power plant in Fairbanks, Alaska. Strand needed to upgrade a draft fan drive motor because temperatures at the plant exceeded those indicated in the contract specs. Strand also filed a claim for time and costs related to working in excessive heat and related inefficiencies at the power plant. The Corp of Engineers denied the claim, contending that the contract had given notice of the high temperatures the contractor encountered.

The government cited sections of the contract specs that described temperatures as high as 160 degrees, and the government further cited a pre-proposal meeting and walk through indicating that it was very hot inside the building and that contractors would have to take precautions for personnel working in the heat.

The Board of Contract Appeals found that contract documents indicated that the plant would have high temperatures ranging from 90-140 degrees and that the contractor encountered neither a constructive change nor a differing site condition. There was no Type I DSC since the contract specs indicated high heat conditions, and there was no Type II DSC because encountering high heat conditions in a power plant is an expected and normal work environment.

- Contributor
Earl K. Cantwell
Hurwitz & Fine, P.C.
Buffalo, New York

National Focus

Design - Build Contractor Liable

Fluor Intercontinental, Inc. v. Department of State, 2012 CIVBCA Lexis 89 (March 28, 2012)

A contractor was hired to construct an embassy in Kazakhstan. Fluor claimed it suffered delays when an alleged government promise that pre-cast concrete foundation piles could be obtained "locally" did not come to fruition. The government countered that it made no promises that foundation materials would be made available locally.

This was an ambitious design-build contract which stated that the contractor was solely responsible and liable for the design sufficiency and should not depend on any reports provided by the government as part

of the contract documents. The contract also made Fluor responsible for adapting the design to the unique conditions of the site and other "local factors".

The Civilian Board of Contract Appeals (CIVBCA) rejected the claim ruling that, in this design-build contract, the risk of developing a design and the consequences of miscalculating resources available for constructing the design fell upon the contractor. In short, the contractor assumed the risk that its design for the construction would work. If it had to change the construction plan due to site problems and conditions, that was the contractor's problem.

Florida

Chinese Drywall Not Covered Due to "Pollution Exclusion"

First Specialty Insurance Corp. v. Milton Construction Co., 2012 W.L. 2912713 (S.D. Florida, July 16, 2012).

A Federal Court in Florida held that sulfur compounds emitted by Chinese drywall fell within the insurance policy definition of "pollutants" excluding coverage, rejecting a claim that the exclusion should be applied only to "traditional" forms of environmental and industrial pollution. The plaintiffs had sued Milton, a Miami builder, as part of a class action lawsuit in a Louisiana Federal Court. First Specialty, the insurance company, sued Milton in Florida Federal Court seeking a declaratory judgment that it owed no duty to defend or indemnify Milton in the Louisiana class action. The plaintiffs alleged that the sulfur compounds emitted from the drywall caused property damage and personal injuries such as eye, throat, and neurological problems.

The court granted First Specialty summary judgment stating that the drywall's alleged release of sulfur compounds contaminated and irritated people and things and, therefore, constituted "pollutants" within the definition in the policy. The court held that Florida courts have consistently applied the "pollution exclusion" in a broad manner to bar claims for a variety of forms and types of environmental pollution and toxic tort claims.

Illinois

Insurance Coverage Determined By Complaint Allegations

Lagestee-Mulder Inc. v. Consolidated Insurance Co., 2012 U.S. App. Lexis 13004 (7th Circuit, June 26, 2012).

The General Contractor claiming to be an additional insured on a CGL policy sought coverage for construction defect claims relating to water infiltration during the late stages of construction of a multi-story office building. The insurance company denied coverage, and that denial was upheld by the District Court and on appeal.

Generally, if a claim alleges damage to the construction work/ project itself due to a construction defect, there may be no CGL coverage. Where the complaint alleges that the construction defect damaged something other than the work itself, coverage may exist. Here, the complaint did not specify the

damages sustained, or whether anything other than the building/project itself was damaged. The general contractor claimed that the vagueness of the complaint should have dictated a duty to defend if the facts in the complaint were not specific enough to exclude coverage. However, the courts ruled that the underlying complaint here did not plead enough sufficient facts to trigger coverage, demonstrating or alleging anything other than damage to the building structure itself. Although the complaint included a claim of water infiltration, it did not identify the damage or location of the damage caused by the water. Due to this vagueness, the "mere possibility" that a covered event occurred, did not trigger a duty to defend under Illinois law. The court ruled that it is the actual complaint and its allegations that must be considered in determining whether an insurer's duty to defend is triggered, not a hypothetical or one of many interpretations.

This case represents a fairly clear line of cases that CGL coverage does not apply to damage from defective construction to the work itself, with the courts concluding that to hold otherwise would make a CGL policy a substitute for "a performance bond".

Kentucky

Contract Payments as Evidence of Compliance

U.S. f/u/b/o CKF Excavating, LLC v. ACC Construction, Inc., 2012 U.S. Dist. LEXIS 109070 (W.D. Kentucky, August 3, 2012).

ACC Construction was the prime contractor on a project to construct a facility at Ft. Campbell, Kentucky. CKF Excavating performed grading and excavating subcontract work until it was terminated for breach of contract. CKF sued for breach of contract under the Miller Act, referencing Prompt Payment Certifications for work performed in the amount of $262,000.00. The contractor argued that these certifications were irrelevant to calculating proper damages or establishing contract breach, and were inadmissible. The Federal District Court disagreed.

The Court ruled that the amounts CKF was entitled to be paid for work performed, and the amounts CKF were actually paid, were relevant at least to a damages determination. The subcontractor argued that the Prompt Payment Certifications established that its work was compliant with the contract. Each certification attested that the amounts requested were for performance in accordance with the contract specifications and conditions, and that the request for payment did not include amounts which were intended to be withheld or retained from the subcontractor. In addition, the Court noted that there was little or no case law to support the proposition that the payment requisitions were not admissible or of relevance to the breach of contract action, either on the issue of contract breach or damages or both.

Mississippi

Contract Terminable at Will

Denbury OnShore, LLC v. Precision Welding, Inc., 2012 Miss. Sup. Ct. LEXIS 369 (August 2, 2012).

Operating under an oral agreement, Precision Welding worked on a project to recover oil at a site in central Mississippi for Denbury. Denbury terminated the contract after four years, and a jury awarded Precision Welding $1.5 Million in damages. The Mississippi Supreme Court reversed.

The oral agreement set forth the hourly rate at which Denbury was to pay Precision, but the parties disputed whether the contract defined a particular duration or scope of work. The element of time was crucial because contracts for an indefinite period of time are terminable at will by either party upon giving reasonable notice to the other party. Although this was a major project which had been ongoing for over four years, the oral contract stipulated no specific end date, no particular number of hours, and no defined scope of work for the subcontractor. Since the contract contained no limit as to duration, it would not be construed as a "perpetual" contract, but rather as a contract terminable upon notice by the request of either party.

Mississippi

Limitation of Liability Clause Enforceable

Thrash Commercial Contractors Inc. v. Terracon Consultants, Inc., 2012 U.S. Dist. LEXIS 87338 (S.D. Miss. June 25, 2012).

Thrash Commercial Contractors hired Terracon Consultants to perform lab tests on film material. The allegation in the case was that Terracon did not test the soil in accordance with specifications and Thrash's fill did not meet required soil density levels. Thrash filed a breach of contract action against Terracon seeking some $300,000 in damages. Terracon argued that a limitation of liability provision in its subcontract capped Thrash's recovery at $50,000. Thrash argued the clause was unenforceable under Mississippi law.

Thrash claimed that the limitation of liability clause violated a Mississippi statute voiding agreements to indemnify or hold harmless another person for that person's own negligence in public and private construction contracts.

The Court however distinguished between and indemnity/hold harmless provision and a negotiated limitation of liability clause and held that a limitation of liability clause is different. In addition, Thrash's claim against Terracon was not for negligence, but for breach of contract. Therefore, the anti-indemnity statute did not apply and the Court upheld the limitation of liability clause.

New Hampshire

Statute of Repose

Phaneuf Funeral Home v Little Giant Pump Company, 2012 N.H. LEXIS 88 (N.H. June 29, 2012).

A decorative fountain was installed in a funeral home in 1999 which included the fountain and a power cord. The installation of the water fountain was done in January 1999, and on March 17, 2007 a fire broke out at the funeral home allegedly because the pump and power cord were defective. Claim was made against the installer of the pump, its manufacturer, the retailer, and also the manufacturer of the power cord. The trial court granted all defendants summary judgment based upon an eight year statute of repose found in New Hampshire Revised Statute Section 508: 4-b.

The appellate court upheld the application of the statute of repose to the benefit of the interior design firm that installed the fountain because that defendant could be said to have worked on and installed the fountain in a way that transformed it into an improvement to the real estate, the operative statutory language. The appellate court reversed summary judgment as to the other defendants, who were essentially product manufacturers and retailers, on the ostensible reason that they did not act in this instance in any way in the process of improving the value or use of the real estate.

The appellate court essentially narrowly interpreted the statute of repose to those defendants actively involved in improving and working on the real property. To the contrary, the court did not apply the statute to product manufacturers and retailers who operate in a general business environment and had no particular connection to working on the real property improvement at issue.

New York

Insurance Coverage – Construction Residential or Commercial?

Admiral Insurance Co. v. Joy Contractors, Inc., 2012 W.L. 2092863 (Court of Appeals, June 1, 2012).

A serious crane accident in New York City which killed seven people resulted in notice to Admiral Insurance, the excess carrier, which reserved rights and sought to deny coverage citing a policy exclusion that there was no coverage if the accident took place during "residential construction activities". The trial court denied Admiral's Motion for Summary Judgment due to "conflicting evidence" whether the building was strictly residential or would contain other retail and commercial "mixed uses". The Appellate Division, First Department, ruled that the exclusion did not apply as a matter of law. However, it then took the unusual move of certifying its own ruling to the Court of Appeals, essentially invoking a "self-appeal" to determine if the Appellate Division Order was correct.

The Court of Appeals ruled that the Appellate Division was in error because there were material issues of fact whether the building was in fact to be strictly residential or of mixed use, and the intermediate court was in error to rule out the possibility of the exclusion applying as a matter of law. The initial ruling of the trial court was essentially reinstated refusing to grant the insurance company's Motion for Summary Judgment due to differing facts and interpretations of to what use or purpose the building under construction would be put.

This is one of those cases where the application of insurance policy language (an exclusion) is not one of law or policy language interpretation, but becomes an issue of fact based upon the nature of the underlying activity and loss.

-Contributor
Earl K. Cantwell, Esq.
HURWITZ & FINE, P.C.
Buffalo, New York

Oklahoma

Bad Faith Claim Rejected

Hammer v. State Farm Fire & Casualty Co., 2012 WL 4023839 (W.D. Oklahoma September 12, 2012).

A house was damaged by wind and hail in 2010. State Farm made a partial payment for actual cash value of the loss. State Farm refused to pay an additional amount for a "general contractor" to coordinate the repairs. The insured claimed an extra 20% for the general contractor expense, while State Farm claimed the repairs were not extensive or complex enough to warrant hiring a general contractor. State Farm also paid the policyholders an additional sum for recoverable depreciation under the policy.

The insured sued for breach of contract and bad faith for the general contractor component. The trial court ruled that the insureds could proceed with their claim for breach of contract as to whether it was reasonable to retain a general contractor, but the court dismissed the bad faith claim noting that there was a genuine and bona fide dispute as to whether the services of a general contractor were warranted. The court also ruled that there was no evidence that State Farm conducted an inadequate investigation.

Rhode Island

Change Order Requires Written Extra Work Order

Process Engineers and Construction Inc. v. DiGregorio, Inc., 2012, R.I. Super. Lexis 112 (July 13, 2012).

DiGregorio was the excavation contractor on a Brown University project to replace underground hot, high pressure water lines for the University heating plant. DiGregorio hired Process Engineers to install the new pipe. There was some damage to the pipe and insulation, and work had to be done to replace pieces of deteriorated pipe at a substantial cost and there was a dispute as to who was responsible for the wet insulation. Process sued DiGregorio for extra work and for replacing the damaged pipe.

The subcontract contained standard language that extra work required written change orders. It also contained language that all work had to be done subject to final approval of the architect. However, there was no written approval for the alleged change orders/ extra work.

DiGregorio's failure to pay on the alleged change orders was upheld because there was no evidence of written approval of the "change order". The court did rule that Process was entitled to recover in

quantum meruit for the cost of replacing wet insulation piping since that fell under the category of replacing or repairing damaged work and not a change or extra work.

This case emphasizes the importance of complying with conditions precedent to making an extra work claim such as making written change orders and approvals from general contractors, the architect, the owner, and perhaps other parties as well.

Tennessee

Statute of Limitations

City of Chattanooga, Tennessee v. Hargraves Associates, Inc., 2010 Tenn. App. Lexis 405 (June 21, 2012).

The architect designed a downtown waterfront area along the Tennessee River. The Certificate of Substantial Completion was issued in 2005. In 2009, the City sued the architect for alleged design and construction defects. The architect asserted a Tennessee statute of limitations requiring that actions for injury to real property be commenced within three years from accrual of the cause of action.

The city claimed it had no knowledge of the design and construction defects until sometime in 2007 when another architect identified areas of concern such as wall defects, defective installation of concrete pavers, electrical defects and settling. The first architect contended that it had pointed out the very same defects much earlier, throughout 2004 and 2005, when it submitted periodic reports on the project.

The city contended this information concerned only "minor corrective work" and was not notice of defects that could not be corrected prior to project completion. The first architect refuted these contentions by comparing its 2004-2005 reports with those made by the later evaluation, and the majority of the items covered were essentially the same.

The trial court and the Tennessee Court of Appeals ruled that the city had constructive and actual knowledge of the construction defects at least three years before filing its complaint, and the action was barred and dismissed on the basis of the three year statute of limitations.

Texas

CGL Policy Does Not Cover Defective Work

Ewing Construcion Co., Inc. v. Amerisure Insurance Company, 2012 U.S. App. LEXIS 12154 (5th Circuit, June 15, 2012).

Ewing Construction built tennis courts for a school, but the courts cracked, flaked and became unfit for use. The school district sued Ewing under a number of theories including breach of contract, negligence, etc. The Federal District Court and the Fifth Circuit Court of Appeals held that the insurance company owed no duty to defend or indemnify Ewing because of the policy's contractual liability exclusion. The exclusion barred coverage for property damage which the insured became obligated to pay "by reason of

the assumption of liability in a contract or agreement." The courts distinguished other Texas cases and essentially held that a contractual liability exclusion excludes coverage for property damage when the insured assumed liability for the property damage by a contract. Essentially, the courts ruled that the CGL policy was not intended to be protection for an insured's poor contract performance.

The insured also argued that the contractual liability exclusion did not apply because of the negligence claim, but the courts disagreed looking to the "source of liability" and the nature of the damages. The courts ruled that the insurance company had no duty to defend the contractor, but vacated the ruling that the insurance company had no duty to indemnify the contractor on the narrow and limited ground that the underlying lawsuit was not yet resolved.

Texas

Delay Damages – Notice Requirements

Balfour Beatty Rail Inc. v. The Kansas City Southern Railway Co., 2012 U.S. Dist.. Lexis 106574 (N.D. Texas July 31, 2012).

A contractor submitted a substantial delay damage claim and the railway company asserted that the contractor failed to comply with contract notice requirements. The contractor alleged notice of the delays to the railroad by emails, letters, and verbal conversations at the job site. The railroad argued that contract "notice" required written notice by certified mail, hand delivery, etc.

The court agreed that the "notice" section of the contract provided for particular forms of notice, but it did not expressly condition recovery of delay damages on such notice. The court ruled that the contractor substantially complied with the required notice requirements, and strict compliance with all the contract terms was not a condition precedent to asserting a delay damage claim.

Texas

Design/Build Contracts - One Responsible Entity

City of San Antonio v. Casey Industrial Inc., 2012 Tex. App. LEXIS 6293 (August 1, 2012).

The City of San Antonio executed a contract with Casey for installation of air pollution control equipment at a power plant. Casey proposed using another company, Wheelabrator, as its subcontractor. Casey eventually initiated a lawsuit for breach of contract and the primary issue was whether the contract was invalid because it was not a proper design-build of contract. Since the contract was deemed void, Casey was entitled to prove liability and damages under a doctrine of quantum meruit. However, this ruling was reversed on appeal.

A Texas statute dictates how local agencies can procure design/build projects. Casey alleged that there was no design-build contract in this case because it did not involve one single, "offeror" that had exclusive

responsibility for the project. Rather, the argument was the contracts were with more than one entity, some of whom did not respond to any of the solicitation requests during the bidding.

The Court rejected this claim holding that the piecemeal interpretations of the contract failed to represent the meaning of the contract arrangement as a whole. The Court concluded that, when read in its entirety, the contract established Casey as a single responsible entity for purposes of satisfying the design/build statute and contract.

Texas

No Damages for Delay Clause Upheld

The Port of Houston Authority of Harris County, Texas v. Zachry Construction Corp., 2012 Tex. App. LEXIS 6591 (August 9, 2012).

Contractor sought delay damages based upon common law exception to "no-damages for delay" clauses finding such clauses invalid where delay results from fraud, misrepresentation, or other bad faith on the part of the party seeking to enforce the provision. The trial court agreed, found the provision unenforceable, and awarded the contractor $20 Million in damages. However, this award was reversed.

The "no damages for delay" provision on its face applied even if such delay or hindrance resulted from negligence, breach of contract or other fault of the project owner. The appellate court pointed out that the parties agreed to the clause regardless of the source of the delay. In any event, this clause specifically applied even if the owner's conduct caused the delay. The provision also applied even if the delay was due to three separate types of "owner conduct": negligence, breach of contract or other fault. The appellate court held that the provision applied even in the event of a project owner's breach.

The appellate court concluded that the clause precluded the contractor's claim. The contractor may be seeking review by the Texas Supreme Court, but acceptance of any appeal is discretionary.