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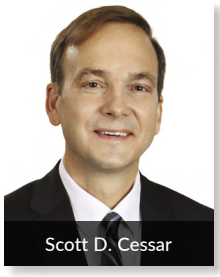
CONSTRUCTION LAW

In This Issue...

Practice pointer: Vouching in the surety


Scott D. Cessar

A not uncommon situation is where the construction contract between the contractor and the subcontractor contains an arbitration clause; however, the contractor's payment bond does not contain an arbitration provision. The subcontractor is then faced with having to sue the surety in court in order to comply with the limitation of actions in the bond, usually one year, and/or the statute of limitations on bonds in the state where the project is located, and then move the court to stay the court action pending the completion of the arbitration.

Even then, if the contractor turns out to be insolvent after the arbitration is over and unable to pay the award, the subcontractor may be faced with relitigating the underlying arbitration against the surety, as the surety may take the position that the award of the arbitration panel is not binding on it.

This same scenario arises in the context of owner and contractor disputes where the construction contract calls for arbitration and the contractor's performance bond does not.

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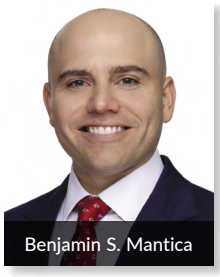
Brown v. City of Oil City: The potential expansion of contractor liability to third parties for defective work


Benjamin S. Mantica

Prior to the Pennsylvania Supreme Court's decision in *Brown v. City of Oil City*, a split existed between the Superior Court and the Commonwealth Court as to whether an out-of-possession contractor could be held liable to a third party for a dangerous condition that it created on a property if the condition was patent or obvious. The disagreement between the courts stemmed from conflicting interpretations of comment c to Section 385 of the Restatement (Second) of Torts.

In *Gilbert v. Consolidated Rail Corp.*, a wrongful death suit was brought against Consolidated Rail Corporation, alleging that an individual was killed as a result of a dangerous condition created by the defective design of a track crossing Conrail erected for the Southeastern Pennsylvania Transit Authority. [*Gilbert v. Consolidated Rail Corp.*, 623 A.2d 873, 874 (Pa. Cmwlth. Ct. 1993).] Relying

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Practice pointer: Vouching in the surety

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What then should counsel for the subcontractor, and/or the owner depending on the context, do to avoid having to repeat the arbitration?

At the outset, counsel should be sure to take steps to comply with the bond's limitation of actions and the statute of limitations of the state where the project is located. The filing of an action and moving to stay the action is the most prudent course, as tolling agreements with sureties may not be enforceable on public projects in all states.

Once having filed the action and moving to stay it, what steps should counsel take to address the surety claiming later that the award of the arbitration panel is not outcome determinative based on the doctrine of collateral estoppel?

The recent Pennsylvania appellate court case of *Eastern Steel Construction, Inc. v. International Fidelity Insurance Company* provides useful guidance.

In *Eastern Steel*, a payment bond surety contested that the underlying arbitration award in favor of the subcontractor—by default—should be given collateral estoppel effect in the bond action in court. The Pennsylvania appellate court rejected that argument, holding that, because the surety was given every opportunity to defend itself in the arbitration, "the arbitration award was conclusive and binding" on the surety.

Reading into the lessons of *Eastern Steel*, attorneys whose clients are counting on a surety for financial protection if the principal becomes insolvent after the arbitration should consistently and consciously keep the surety apprised throughout the arbitration proceedings by papering the record. This starts with inviting the surety to participate in the arbitration process, sending to the surety on a consistent basis all arbitration filings, including expert reports and interim panel orders. Also, the owner should inform the surety of the dates of the hearings and invite it to attend and participate and/or observe. The owner should also ask the surety if it wants to have the arbitration proceedings transcribed. All post-hearing submissions should be shared with the surety and, of course, also the award of the panel.

In effect, counsel is "vouching" the surety into the arbitration in order to handcuff the surety from later claiming that the arbitration award is not binding and attempting to relitigate the case.

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Brown v. City of Oil City: The potential expansion of contractor liability to third parties for defective work

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on comment c to Section 385, the trial court dismissed the complaint and held that a contractor who is out of possession of property cannot be held liable for a dangerous condition that it created on the property unless the condition is undiscoverable or latent. [*Id*.]

On appeal however, the Commonwealth Court disagreed with the trial court's interpretation of comment c and permitted the wrongful death action to proceed. The Court held that Section 385 read in conjunction with comment c expanded a contractor's potential liability for a dangerous condition that it created on the property. [*Id*. at 875.]

Disagreeing with the Commonwealth Court's decision in *Gilbert*, the Superior Court came to the opposite conclusion in *Gresik v. Pa. Partners, L.P*. In *Gresik*, a negligence action was brought against the prior owner of a steel plant for modifications they made while they owned the plant. The prior owner had removed a drawbridge that was designed to allow employees to escape in the event molten steel breached the sides of the furnace. The subsequent owner was aware of the modification prior to the sale. After the sale, one employee was injured and one was killed after they were unable to escape via the drawbridge following an explosive rupture. [*Gresik v. Pa. Partners, L.P.*, 989 A.2d 344, 347 (Pa. Super. Ct. 2009).] Based on their interpretation of comment c to Section 385, the Superior Court sustained the trial court's entry of summary judgment. The Superior Court determined that as a precondition for establishing liability under Section 385, a plaintiff must show that the danger was one unlikely to be discovered by the possessor or those who come upon the land with the possessor's consent. [*Id*. at 351.] Therefore, because the new owner of the steel plant knew about the removal of the drawbridge, the Superior Court concluded that the trial court did not err in dismissing the complaint. [*Id*.]

The split between the Commonwealth Court and the Superior Court was recently resolved by the Pennsylvania Supreme Court in *Brown v. City of Oil City*. In *Brown*, the City of Oil City hired multiple contractors to design and build new concrete stairs leading to the entrance of the Oil City Library. The stairs were completed in 2011 and almost immediately began to deteriorate.

> *"[I]t is critical that contractors be aware that they may be susceptible to claims well after a possessor of land has accepted their work and regardless of whether a defect is obvious."*

[*Brown v. City of Oil City*, 294 A.3d 413, 419 (Pa. 2023).] Despite several complaints about the deteriorating condition of the concrete stairs between 2012 and 2015, neither the city nor the contractors made any effort to repair the stairs, or to warn the public about their dangerous condition. [*Id*.] On November 23, 2015, Kathryn Brown tripped and fell on the stairs and later died from a traumatic head injury suffered as a result of the fall. [*Id*.]

Consequently, David Brown on behalf of himself and his wife's estate brought a wrongful death action against the City of Oil City and the contractors responsible for erecting the stairs. [*Id*.] Following discovery, however, the contractors filed for summary judgment, asserting that they owed no duty to third persons as they were not in possession of the property when Brown was injured. [*Id*. at 420.] Citing the Superior Court's decision in *Gresik*, the trial court determined that the contractor's liability was limited to only those situations where the contractor created a dangerous defect that the possessor was unlikely to discover. [*Id*.] Accordingly, the trial court entered summary judgment on behalf of the contractors.

After Brown reached a settlement with Oil City for the maximum amount authorized by the Political Subdivision Tort Claims Act, he appealed the trial court's decision to the Commonwealth Court. [*Id*. at 421.] Citing their previous decision in *Gilbert*, the Commonwealth Court reversed the trial court's decision and concluded that although Oil City had knowledge of the defective nature of the stairs, it did not relieve the contractors of liability under Section 385. [*Id*. at 422.]

The contractors appealed, and the Pennsylvania Supreme Court considered whether an out-of-possession contractor can be subject to liability under Section 385 of the Restatement of Torts for injuries to third parties where the dangerous condition of the structure is well known to the possessors of land. [*Id*. at 422-23.]

Ultimately the Pennsylvania Supreme Court decided that a contractor's liability under Section 385 does not hinge on whether the defective condition it caused is latent or patent; rather, comment c imposes liability on contractors to third persons for all defective structures on land that they are responsible for creating through their work. [*Id*. at 433-34.]

In sum, after the Court's decision in *Brown v. Oil City*, it is critical that contractors be aware that they may be susceptible to claims well after a possessor of land has accepted their work, regardless of whether a defect is obvious. Consequently, it is critical that a contractor communicate with the property owner and be proactive about coordinating a plan to correct any deficiencies related to their work.

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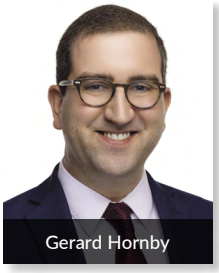
A practical guide to drafting construction contracts: Essential tips and key clauses


Gerard Hornby


David Meredith

Highlights from the Construction group's presentation at the Eckert Seamans' August 2023 Joel Lennen Legal Primer by David Meredith and Gerard Hornby

Earlier this year, the Construction group's David Meredith and Gerard Hornby presented at the firm's annual Continuing Legal Education event. The focus of their presentation was on essential tips and key clauses to look out for in drafting construction contracts, the highlights of which are below.

Contract drafting and agreement is a push-and-pull process. Everyone wants to pass down risk, limit risk, or blame someone else. A major part of the negotiated contract is risk control. The following six clauses should always be negotiated as required to control risk:

Pay If Paid/Pay When Paid Clauses shift the risk of non-payment to subcontractors or suppliers even though they may not have control over the circumstances that lead to non-payment. These are helpful for owners and general contractors while limiting the rights of subcontractors and suppliers.

Subcontractors and suppliers should do their best to avoid pay if paid and pay when paid clauses. At a minimum, subcontractors and suppliers should attempt to negotiate language that allows the contractor to withhold payment only if the owner's withholding of payment from the contractor is related to the performance of the subcontractor or supplier.

Indemnity Clauses provide that one party (the indemnifying party) will compensate the other party (the indemnified party) for any losses or damages that may arise from a particular event or circumstance. Many times, these clauses will provide that a contractor or subcontractor will indemnify the owner and design professionals from everything and anything that could go wrong on the project, from personal injury to property damage to environmental issues to economic damages.

As a general contractor, subcontractor, or supplier, you should only agree to indemnify parties when you caused or participated in the cause of the

loss. This means only indemnify to the percentile extent your conduct was the proximate cause of the loss and limit your indemnification obligations to property damage and/or personal injury. As an owner, do not agree to language providing that an indemnifying party is only liable in the event of "sole" negligence.

Liquidated Damages provisions specify a predetermined amount of money that must be paid as damages if one party fails to meet certain contractual requirements. These clauses can provide for damages for late completion at the end of the job, or on milestones, or even for the failure of the completed project to meet specified performance criteria.

A well-drafted clause eliminates the optional nature of the clause, specifies the rationale for liquidating damages, identifies the types of losses to be liquidated (and not to be liquidated), and clarifies the events that will (and will not) trigger the clause. This can significantly reduce the types of litigation that commonly attend liquidated damages clauses. As an owner seeking to include a liquidated damages provision, have the engineer or architect generate a memorandum indicating how the liquidated damages were calculated. Consider also including language indicating that damages will be difficult to ascertain and that the liquidated damages are a fair and reasonable estimate of likely damages. As a contractor negotiating a liquidated damages provision, provide that liquidated damages are the exclusive damages recoverable in the event of a delay or performance issue. Another option is to negotiate a cap on all damages based on a percentage of the contract value.

No Damages for Delay Clauses essentially provide that, if there is a delay not caused by you, you get more time, but not more money. A contractor negotiating a no damages for delay provision should seek to limit application of the provision to specifically contemplated events of delay, and also negotiate to provide for some objective means to calculate damages based on a reasonable per diem or percentage that ties into the original bid estimated costs for field and home office overhead. Negotiate to limit your right to recover to direct, provable costs, such as project supervision, jobsite equipment, and other project-specific costs rather than no damages at all. As an owner, consider avoiding overly broad clauses, as they could lead to inflated initial pricing, excess contingency, claims for additional costs outside of delay, or a contractor default. If the owner actively interferes with the contractor's ability to perform its contractual duties, these clauses can be challenged as unenforceable.

> *"As a general contractor, subcontractor, or supplier, you should only agree to indemnify parties when you caused or participated in the cause of the loss."*

Incorporation by Reference/Flow Down Clauses in a subcontract incorporate the general contract by reference and bind the subcontractor to the general contractor to the same extent the general contractor is bound to the owner. Subcontractors often take pains to negotiate changes to the subcontract, but then ignore the fact that all of those contractual "gains" may well be trumped by the fact that the terms of the prime contract—equally as onerous and one-sided—still govern because of this quiet, silent rogue.

As a contractor or subcontractor, at a minimum, make sure you have everything you are agreeing to by reference. Do you have all of the documents incorporated by reference? What do the documents say? How do they affect the risk? If possible, negotiate that the terms of your contract take precedence over whatever is being referenced OR negotiate a reciprocal flow down provision where the general contractor assumes to the subcontractor the obligations that the owner owes to the general contractor. From the perspective of the owner, collaborate and ensure that all required documents are easily accessible to downstream entities.

Material Escalation Clauses are typically used where there is a lump sum/fixed fee or guaranteed maximum price contract, especially where the duration of a construction project is long and complex, so that there can be an adjustment to the price to be paid by the owner if there are sharp increases in the price of materials or labor.

There are several key factors to consider when negotiating a material escalation clause. The provisions generally require that the parties must identify the materials that are anticipated to have price fluctuations during the course of construction. After identification, parties will agree to the "baseline price" for the materials. Material escalation clauses can be "cost-based" or "index-based." Index-based clauses are linked to published material cost indexes such as the U.S. Bureau of Labor Statistics. There may also be limits as to the maximum adjustment amount, such as a 10% increase limit. Contractors may include language intended to limit their liability for delays in the delivery of materials.

The bottom line is that typical risk avoidance techniques and unfavorable contract terms are here to stay. However, if recognized and dealt with during the negotiation of the contract, these terms—and any potential risk exposure—can and should be managed.

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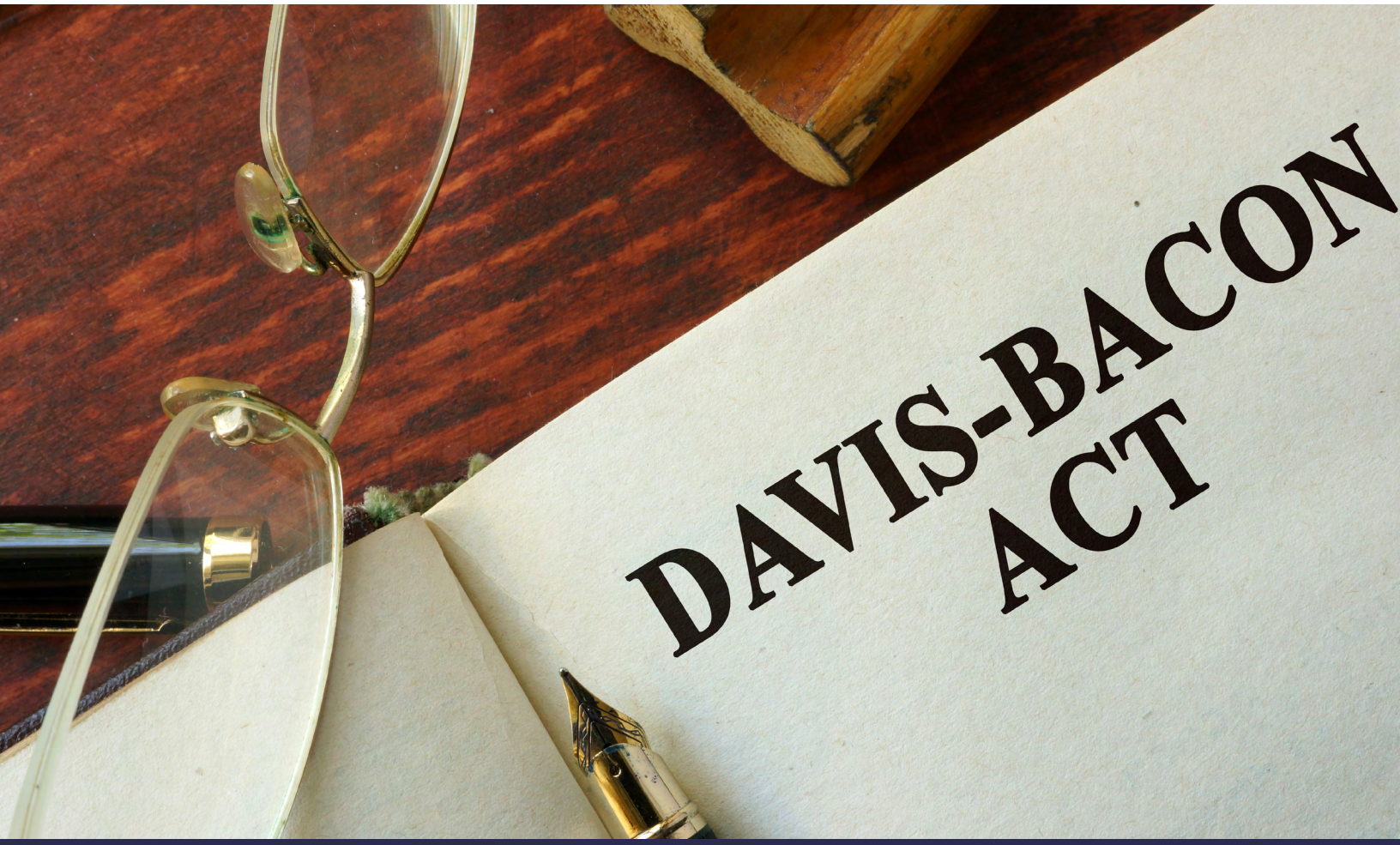
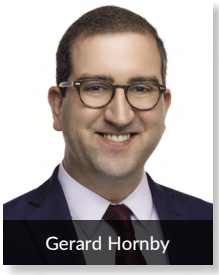


The first major revision to the Davis-Bacon Act in 40 years—what it means for the construction industry


Gerard Hornby

The Davis-Bacon Act (DBA) and all Davis-Bacon Related Acts (DBRAs) apply to contractors and subcontractors performing on federally funded projects for the construction, alteration, or repair of public buildings or public works. More specifically, the DBA and the DBRAs require employers working on these projects to pay their employees no less than the locally prevailing wages for corresponding work on similar projects in the area.

While the DBA was passed in 1931, examples of DBRAs include the 2022 Inflation Reduction Act, the 2021 Infrastructure Investment and Jobs Act (most commonly known as the Bipartisan Infrastructure Law), the 1974 Housing and Community Development Act, the 1956 Federal-Aid Highway Acts, and the 1948 Federal Water Pollution Control Act. In other words, if you're awarded a federal construction contract funded by one of these laws, then you'll have to abide by the DBA's prevailing wage laws. These laws cover a lot of ground, meaning the prospect of compliance challenges for contractors has only increased over the years.

The promulgation of rules and regulations surrounding the DBA and DBRAs is governed by the Department of Labor (DOL). The last major revision of the federal regulations under the DBA was in 1983, and these rules subsequently remained essentially unchanged for four decades.

But now, the DOL, for the first time since the Reagan Administration, has published a major comprehensive regulatory review of how the DBA is administered. On August 8, 2023, the DOL published its Final Rule Updating the Davis-Bacon and Related Acts Regulations. At over 800 pages, the Final Rule is lengthy. It took effect on October 23, 2023, and a summary of the key changes and codifications of current guidance as they apply to contractors is outlined below:

- "Building or work" now includes solar panels, wind turbines, broadband installation, and installation of electric car chargers on the non-exhaustive list of construction activities.
- "Construction, prosecution, completion, or repair" received additional language identifying the five types of activities that qualify as "covered transportation" under Davis-Bacon.
- The Final Rule states that where a significant portion of the building or work is constructed at a secondary construction site specifically for

the DBA project, then that work will be covered by the DBA (contrast this with secondary sites that manufacture or construct materials for sale to the general public). The prior version of the regulation only applied DBA rules to secondary sites that were established specifically for a DBA project.

- The Rule adopts a three-pronged criteria in order to define what a "material supplier" is and is therefore not subject to the DBA: (1) the material supplier's work on the contract must be limited to the supply of materials or equipment, which may include pickup and delivery; (2) the material supplier's facilities being used for the contract either must have been established before opening of bids or, if it was established after bid opening, may not be dedicated exclusively to the performance of a covered contract; and (3) the material supplier's facility manufacturing the materials or equipment may not be located on the primary or secondary construction site.
- The Rule defines the term "prime contractor" to include controlling shareholders, joint venture members, and anyone who has been delegated responsibility for overseeing all or substantially all of the construction under the prime contract.
- The Final Rule clarifies that upper-tier contractors can be held responsible for a lower-tiered subcontractor's DBA violations.
- The Rule authorizes the DOL to require contractors to pay back wages to workers on DBA contracts even when the contracting agency failed to include a DBA contract clause or wage determination in the contract.

On the surface, these changes may appear minor and years away from directly affecting any particular project. But in reality, under the Final Rule, compliance has grown more complicated; wages and costs will likely rise, and more risk has shifted onto contractors. Landmark Congressional acts like the Inflation Reduction Act and Bipartisan Infrastructure Law are good for contactors and will bring about a lot of projects in years to come, but this means the prospect of compliance challenges has only increased. Contractors intending to perform DBA-covered projects are advised to review these new requirements and contact their attorneys with any questions.

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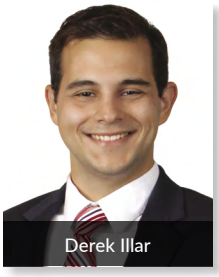
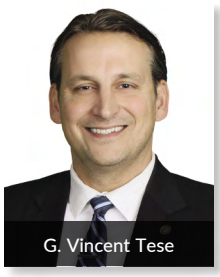
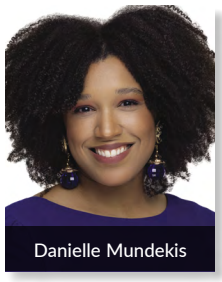
Building opportunities for diverse businesses in the construction industry


Derek Illar


G. Vincent Tese


Danielle Mundekis

Federal, state, and local governments have recognized that businesses, which people of diverse backgrounds own and operate, play a crucial role in contributing to economic growth and development, fostering innovation and competition, and advancing important social aims. They, therefore, have created programs that give diversely owned businesses certain advantages with respect to procurements contracts, training, and financing. Oftentimes, business owners of diverse backgrounds are unaware of these opportunities, especially with relation to formal certification as a qualification of how to qualify for them; that is, until now. Using the Commonwealth of Pennsylvania as an example, we will explain the benefits that businesses in the construction industry can receive as Small Diverse Businesses (SDBs) and how they can qualify as SDBs.

Once a business obtains status as a SDB, it can take advantage of the following benefits:

- Access to exclusive contracting and procurement opportunities within the Commonwealth, offering significant potential for business growth and profit.
- Qualifying for subcontracts under the Small Diverse Business Program for Low Bid Capital Construction Projects. Under this program, on larger projects with an estimated value above $300,000 (referred to as "Capital Projects"), the Commonwealth establishes Minimum Participation Levels (MPLs) requiring Prime Contractors to use SDBs for certain percentages of the work.
- An array of tailored-made programs and resources, such as the Mentor-Protégé Program. Through this initiative, SDBs receive guidance and support from seasoned professionals to compete for non-highway capital construction, supplies, and services procurement opportunities, which enhances their ability to secure these engagements.
- The opportunity to gain recognition for the purposes of similar programs and initiatives at the federal level and in other states.
- Eligibility for the Small Diverse Business Capital Access Program, managed by the Pennsylvania Industrial Development Authority (PIDA). This program, offered through the Pennsylvania Department of Community and Economic Development and administered by PIDA, provides low-interest loans and lines of credit to small diverse businesses that commit to creating and retaining full-time jobs within Pennsylvania. Loan applications are packaged and underwritten by a network of certified economic development organizations that partner with PIDA to administer the program.

To become an SDB, a business must satisfy several legal and regulatory threshold requirements. The law requires the business to:

1. Be duly registered in the Commonwealth of Pennsylvania;
2. Operate legally within the Commonwealth of Pennsylvania;
3. Employ no more than 100 full-time equivalent employees;
4. Maintain gross revenues under $38.5 million;
5. Not be a dominant force within an industry; and
6. Be owned (e.g., 51% or more) by a person that identifies as diverse.

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Building opportunities for diverse businesses in the construction industry

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If a business meets these parameters, it can embark on the process of obtaining certification as a diverse business. To do so, the owner(s) of the business will need to provide information and documentation to substantiate that he/she/they is/are a member of a diverse population. For the purposes of certification, the diverse populations include women, Black people, people who are disabled, veterans, and LGBTQ+. The Pennsylvania Department of General Services and the Bureau of Diversity, Inclusion, & Small Business Opportunities validates the status of small diverse businesses via certifications from accredited third-party entities. Examples of these third-party entities are: the National Minority Supplier Development Council, the Women's Business Enterprise National Council, the U.S. Small Business Administration 8(a) Program, the U.S. Department of Veteran Affairs, the U.S. Business Leadership Network, and the National Gay and Lesbian Chamber of Commerce.

Once an entity successfully completes the small business certification process, it will receive confirmation of its status, which will enable it to compete for contracts with the Commonwealth of Pennsylvania. Indeed, the Commonwealth of Pennsylvania maintains an online portal that permits SDBs to identify all the commercial opportunities that are available to them.

Whether you are a prime contractor, a specialty-service company (e.g., electrical, masonry, flagging and safety, etc.), or a supplier of raw materials, the SDB Program affords you numerous opportunities to build your business.

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Construction Law Group NEWS

Client Success

Pittsburgh-based Member **Tim Grieco** and associate **Gerard Hornby** recently secured a summary judgment ruling dismissing a developer's deficient design claim in the Court of Common Pleas of Philadelphia County.

Our client, an architect, brought suit against a Philadelphia-based real estate developer relating to architectural services performed by the architect but for which it was not paid. These plans were to be used for the construction of a mixed-use high-rise in downtown Philadelphia.

The defendant developer retaliated with wide-reaching counterclaims for breach of contract, tortious interference, and unjust enrichment, claiming that plaintiff did not complete the work, and the work that was completed was substandard. In sum, these counterclaims totaled in excess of $2 million.

After considerable time and effort vetting these counterclaims through discovery, the plaintiff moved for summary judgment in December 2022, arguing that the counterclaims were factually and legally unsupported.

The Court agreed with the plaintiff and, in a June 30, 2023, order and opinion, dismissed the counterclaims in their entirety. In addition, the Court denied the defendant's own motion for partial summary judgment on the plaintiff's claim for the lost profits it expected to earn on the project. A trial on the architect's claim is to be scheduled in 2024.

Construction Group Accolades

Eckert Seamans' Construction practice group was ranked by Best Law Firms® 2024 as a Nationally recognized practice in the area of Litigation – Construction.

Five Eckert Seamans attorneys were named among The Best Lawyers in America® for 2024 in the area of Litigation – Construction, including **Scott D. Cessar, F. Timothy Grieco, David M. McGlone, Bridget E. Montgomery**, and **Christopher R. Opalinski**. **Chris Opalinski** was also named 2024 "Lawyer of the Year" for Litigation – Construction in Pittsburgh.

The group was also recognized in the Chambers & Partners USA 2023 Guide as a leading firm in Pennsylvania for Construction law and by The Legal 500 as a leading law firm for Construction nationwide in 2023.

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