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Construction Law

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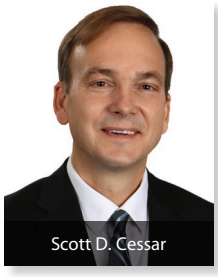
Implied warranties as to the plans and specs on a CM at-Risk project



Scott D. Cessar

In a traditional design/bid/build project, the owner retains the architect/engineer to design the project and, once the design is complete, puts it out to bid. As such, the owner, pursuant to the *Spearin* Doctrine, impliedly warrants the constructability of the plans and specifications. If the contractor relies, in good faith, on the plans and specs, the contractor will be entitled to recover additional costs arising from design defects.

In a CM at-Risk project, the owner engages professionals to design the project and, in addition, hires a CM (contract management) firm to provide a range of preconstruction services. These preconstruction services may include cost estimation, design review, value engineering and preparation and coordination of the bid packages. The CM firm then serves as the general contractor holding the subcontracts, directing the work of the trade contractors, and providing management and construction services.

This distinction in project delivery systems raises an interesting question: Does the extensive preconstruction involvement by the CM at-Risk in the design of the project eliminate the implied

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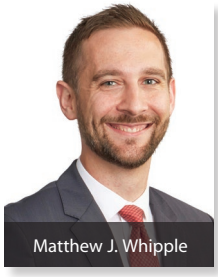
New executive orders for federal procurement: Caution to federal contractors and to subcontractors



Matthew J. Whipple

Over the past 18 months, the Obama administration has published a series of executive orders that place significant new burdens on companies competing for federal procurement contracts. The executive orders have wide-ranging effects, from protecting LGBT workers against discrimination to requiring mandatory disclosures of past violations of labor and employment laws to compelling worker benefits such as paid sick leave, transparent paycheck deductions, and increased minimum wage thresholds.

Seasoned federal contractors, used to dealing with the rigors of the Federal Acquisition Regulations, have largely been able to adapt to these new Presidential directives. For example, according to a White House Fact Sheet, all five of the largest

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Implied warranties as to the plans and specs on a CM at-Risk project
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warranty of the plans and specs by the owner under *Spearin*?

The question was considered in a recent case from the Supreme Judicial Court of Massachusetts in *Coughlin Electrical Contractors v. Gilbane Building Company v. Division of Capital Management and Maintenance (DCAM)*.

Coughlin arose from a CM at-Risk project administered by a Massachusetts state agency, DCAM, for the construction of a hospital. DCAM hired a designer to design the hospital. Gilbane served as the CM at-Risk for DCAM. Coughlin was the electrical subcontractor to Gilbane.

Coughlin filed suit against Gilbane alleging a 49 percent labor hour overrun based on Gilbane's alleged failure to schedule and coordinate the project and based on alleged design defects, including a discrepancy as to the amount of space in the ceiling to place the electrical work and a claim that design changes prohibited the work from being done in a logical order.

Thereafter, Gilbane joined DCAM to the case alleging that, if there were design defects, then DCAM was responsible based on the implied warranty of constructability of the plans and specs.

The trial court dismissed Gilbane's joinder of DCAM because the CM at-Risk method results in "material changes in the roles and responsibilities voluntarily undertaken by the parties," which extinguishes the owner's implied warranty of the plans and specs. Stated another way, the trial court concluded that Gilbane's consultation and involvement with the design as part of its preconstruction services immunized DCAM from liability for subsequently discovered design defects.

On appeal, the highest court of Massachusetts reversed the lower court and held that the owner in a CM at-Risk project may have liability for design defects based on a breach of the implied warranty of constructability of the plans and specs.

The court held that, although the relationship of the CM at-Risk and a general contractor in a design/bid/build project is substantially different, this, in and of itself, does not constitute grounds such that the CM at-Risk bears all responsibility for design defects and the owner none. The owner may or may not have accepted the CM at-Risk's design suggestions as to the plans and specs. The owner also engaged a designer to prepare the design and may be able to transfer liability to the designer. Further, and importantly to the court, the contract between Gilbane and DCAM did not contain any express waiver of the implied warranty.

Based on these considerations, the Massachusetts high court reversed the trial court and sent the case back to the trial court. At trial, Gilbane will be permitted to attempt to prove a breach of the implied warranty by DCAM. The greater Gilbane's design responsibilities and involvement during preconstruction, however, the greater Gilbane's burden will be to show that it reasonably and in good faith relied on DCAM's design.

For Gilbane to recover against DCAM on Coughlin's claims, Gilbane will, therefore, likely need to show that the design issues raised by Coughlin were not something that Gilbane, in good faith and in the reasonable exercise of its preconstruction services duties, would or should have discovered.

Coughlin, thus, teaches that determining liability for design issues, in most situations, will not turn on labels like "CM at-Risk." Instead, the determination will turn on a careful review of the contract clauses at issue and the facts as they relate to the particular design defects that serve as the basis of the claims.

Further, *Coughlin* suggests that owners in a CM at-Risk project would be wise to contractually disclaim the implied warranty of constructability of the plans and specs with a carefully worded clause in which the CM at-Risk acknowledges that, based on its extensive preconstruction services, the CM at-Risk has satisfied itself that the design is sound and is buildable in all respects.

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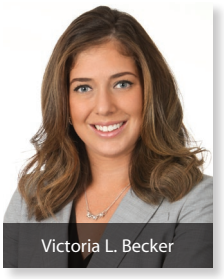
Bidding and supplier quotes: Accounting for deviations


Victoria L. Becker

In a recent state court decision, the Lycoming County Court of Common Pleas examined the issue of whether a supplier is entitled to payment from a contractor for an increase in costs over the amount quoted. *See RSJ Enterprises, Inc v. Bognet, Inc.*, Civ. A. No. 14-02,364 (Pa. Com. Pl. Nov. 24, 2015). Contractors often rely on quotes provided by suppliers in bidding construction projects, and any increase in supply costs over the quoted amount may result in a dispute over a request for additional payment. In *RSJ Enterprises, Inc.*, a supplier of architectural products requested a judgment for sums owed for additional materials provided to the contractor for use in a construction project.

The Court first examined whether the contractor relied on the initial material quotes given by the supplier when bidding the project. While contractors are entitled to rely on supplier quotes for materials, if they do not in fact rely on the quotes, they are not entitled to a claim for detrimental reliance. In this case, the supplier emphasized the deviation language placed in the quote which stated, "[i]f quantities or types deviate from those listed, price is subject to increase or decrease proportionately." Consequently, the supplier argued that since the quantities needed for the project increased, so should the price. Indeed, changes to a project after a contractor accepts a bid may require additional material, which the supplier would be justified in charging for in accordance with a deviation provision. However, if changes are made to plans prior to bidding and the contractor does not convey such changes to the supplier for its quote, and the contractor also makes its own calculations for materials, the contractor cannot claim that it detrimentally relied on the supplier's quote.

Second, the Court considered whether the contractor would be unjustly enriched without making an additional payment to the supplier. It is clear that a supplier confers a benefit to the contractor by supplying further materials to enable the contractor to complete its contract, but the issue is whether it is inequitable for the contractor to retain that benefit without additional payment. Here, the Court found that (1) the contractor's bid actually accounted for higher material costs than the supplier's quote, (2) the contractor was aware of discrepancies between its own estimates and the supplier quotes, and (3) the supplier provided additional materials merely at cost (i.e., the supplier did not realize a profit). Considering these circumstances, the Court awarded the supplier the invoiced amount for additional materials.

While the facts of this case are unique, the case illustrates a good practice point: Contractors should be aware of deviation provisions in supplier quotes and inquire into pricing schedules for incremental increases in materials. This inquiry may help protect contractors when bidding in order to account for price increases as a result of changes or mistakes that may occur when estimating and bidding a project.

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New executive orders for federal procurement: Caution to federal contractors and to subcontractors

(continued)

federal contractors, which receive a quarter of all federal contracting dollars, have already adopted compliant LGBT discrimination policies, and the vast majority of the top 50 contractors have done the same.

Other companies, however, may have a more difficult time complying. Many of the executive orders place new human resource and administrative encumbrances, which small businesses may be poorly equipped to implement without assistance. Further, some companies may not even be aware that compliance is required. Subject to certain monetary and contract-type thresholds, the new executive orders apply to subcontractors. This does not simply mean subcontractors working on a federal project site. Applicable regulations define a subcontractor as a company that enters into an arrangement for the purchase, sale or use of personal property or nonpersonal services that are "necessary to the performance" of one or more government contracts.

Although applicable precedent has recognized that this definition is not always clear, the definition of a subcontractor is often interpreted expansively. A "necessary" service might be performed on site, or it might be performed in a warehouse thousands of miles away. A "necessary" product might be provided by a subcontractor four steps down the supply chain, without direct knowledge of what the general contract requires and with no relationship to the government or the general contractor.

In general, a prime contractor must notify a supplier or subcontractor of potential obligations, such as by providing a form EEOC notice regarding compliance with nondiscrimination and affirmative action obligations. This may not always happen, however, and a lack of notice may not protect a subcontractor, as ignorance of the fact that a company is a covered subcontractor is not an excuse for failure to comply with applicable procurement laws.

It remains to be seen whether the Obama Administration's Executive Orders will continue into the next administration, but even if some do not, it is assured that federal procurement will continue to place significant demands on contractors. Subcontractors farther down the procurement chain, however, should also be sure to pay attention to these requirements. If your scope of work impacts a federal project, careful assessment should be made to make sure that your company stays on the right side of all statutory, regulatory and executive mandates.

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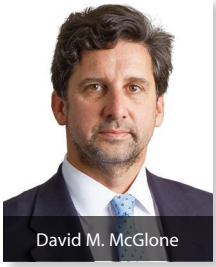
Woman-owned businesses and layers of certification: Barriers to compliance



David M. McGlone

To be wholly and completely certified as a Woman Owned Business Enterprise (WBE) is an exercise in peeling a very dense onion composed of many bureaucracies and regulatory schema.

At the federal level, at basis, a WBE must be 51 percent owned by a woman who is a United States citizen. She must also be the person who is truly in control of the company, and its board of directors. This also means management of the company and daily operations. She needs to be a full-time supervisor and, generally, if the corporation setup is more complex than a simple corporation, she (or another woman) needs to have a 51 percent interest in every entity that comprises the bidders.

There are designated Third-Party Certifiers. However, by submitting a daunting list of corporate documents, ledgers, birth certificates and other documents, a woman may self-certify without fear of her chances of winning the bid being impaired.

The documents supplied in search of certification are required to be posted to the Woman Owned Small Business repository.

Note that the company must also meet the standards for a small business as set by the SBA, as it is an SBA-administered program.

In many states like Massachusetts, there is no self-certification available. The applicant must be certified by the Commonwealth's state agency or the agency's designee. If the company is foreign to the Commonwealth, it must present its own state's certification. Obviously, if a bid is planned on the state level, it must be planned well ahead of time.

In Massachusetts, the woman must be in "dominant" control of the corporation, beyond the legal formalities. Massachusetts takes pains to list those qualities of the woman's relationship with her company by which the Commonwealth reserves the right to de-certify. The Commonwealth guards the spirit of the law and not just the letter. The flashpoints where de-certification could occur include a failure of the woman to maintain control of the company, lack of technical competence, and lack of thorough knowledge of the finances. Moreover, a sort of rebuttable presumption is created that if any man is holding a professional license, the Supplier Diversity Office may find that the woman is not in control and de-certify her.

Moreover, in Massachusetts, the woman's company must be wholly independent of other companies. It cannot share directors or key employees with another company. If an applicant company even shares resources with another company that is not woman owned, it may forfeit its certification.

Note that there is a public hearing on March 25, 2016, and comment period on the Massachusetts Regulations in which repeal of the above requirements is sought. However, it will be replaced with new regulations that substantially track the above requirements.

Finally, Massachusetts requires the woman-owned business to add its name to the Register to qualify for bids.

For Pennsylvania bidding, a woman can self-certify that she is a small business (less than 100 employees and limited gross sales), but to obtain certification that her company is a woman-owned business, she will need third-party certification. Her business must be 51 percent owned by her, and she must be a U.S. citizen or legal resident. She must hold the highest position in the company and be qualified to do that kind of work. Pennsylvania reserves a veto if the woman's business becomes too dominant in its field.

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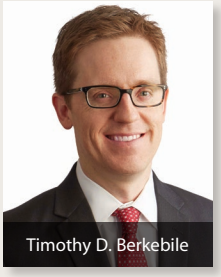
PA Commonwealth Court revisits rulings on Section 508 of the Public School Code and recovery of attorneys' fees


Timothy D. Berkebile

As with all public works projects, public school construction in Pennsylvania is complicated by a statutory structure that attempts to strike a balance between protecting the interests of the public and those of contractors and subcontractors. The Commonwealth Procurement Code provides, among other things, for competitive sealed bidding or proposals and other measures to combat corruption in public works. The aim is to ensure that work is awarded to the lowest responsible bidder. The Separations Act requires public owners to solicit separate bids and award separate contracts for plumbing, HVAC, electrical and mechanical work so that smaller specialized contractors are able to participate in public projects. In theory, this acts to increase competition. Pennsylvania's Prompt Pay Act, which is part of the Procurement Code, provides substantial remedies of penalty interest and attorneys' fees for contractors and subcontractors that are denied payment in bad faith on public construction projects.

Section 508 of the Public School Code is another statute that profoundly affects public school construction projects. This law provides that the "affirmative vote of a majority of all members of the board of school directors . . . shall be required in order to . . . [e]nter into contracts of any kind . . . where the amount exceeds one hundred dollars." School districts have relied on this language when arguing that oral directives in the field and orally agreed-upon changes are null and void after the work was performed. Until recently, courts have been sympathetic to this argument. For this reason, contractors engaged by school districts on construction projects have long been advised not to proceed with work beyond or different from the contracted scope until a change order has been signed under the authority of the school board. In practice, waiting for a signed change order under these circumstances is impractical. Any delay in proceeding with work has cascading effects on the schedule and coordination efforts with other prime contractors. Scheduling and political pressures often lead contractors to proceed without a written change order at their peril.

Two recent Commonwealth Court opinions have strengthened the Court's position addressing the problem created when a contractor is directed to proceed with additional or changed work by a school district representative only to be denied payment because the school board had not approved the modification. In *East Coast Paving & Sealcoating, Inc. v. North Allegheny School District*, a paving contractor was required by the school district to repair soft spots that occurred in the pavement due to the underlying ground being "soft." The repair of such soft spots was not included in the contractor's scope of work because the school district rejected a proposed unit price to repair any soft spots that occurred. When soft spots were discovered, the school district directed the contractor to perform the repair work, but later denied payment, in part, because the additional work was not approved by the school board. The Court ruled that it was not necessary for the school board to specifically approve additional or changed work necessary to complete the approved work. Section 508 only required that the paving project and its completion by the contractor were approved by the board. In *F. Zacherl, Inc. v. Flaherty Mechanical Contractors, LLC*, the school district orally agreed for a subcontractor to complete its scope of work after the prime contractor was terminated for cause. The school district then refused to pay for work performed because the oral contract had not been approved by the school board. The Court rejected this position because the scope of work was previously approved as part of the prime contract and, as part of the approval of that prime contract, the school district had approved the subcontractor's performance of that work.

Contractors should still insist on receiving authorized written change orders whenever possible, but these cases suggest that school districts should not rely on the lack of formal board approval in denying payment to contractors or subcontractors that performed work at the school district's direction.

PA appellate courts clarify the applicability of Prompt Pay Act and CASPA to contract with government agencies

In *East Coast Paving & Sealcoating, Inc. v. North Allegheny School District*, the Commonwealth Court also ruled that Pennsylvania's Contractor and Subcontractor Payment Act (CASPA), which provides for an award of penalty interest and attorneys' fees for substantially prevailing parties in payment disputes on construction projects, does not apply to construction contracts between a government agency and a contractor. Instead, Pennsylvania's Prompt Pay Act, discussed briefly above, is the applicable statute for such projects. However, in *F. Zacherl, Inc. v. Flaherty Mechanical Contractors, LLC*, the Commonwealth Court refused to apply the Prompt Pay Act to a dispute involving an oral contract that was not competitively bid as required by the Procurement Code (see brief discussion above). It does not appear that this issue is definitively resolved, however, as the concurring opinion argues that "government agencies should [not] be allowed to use their own failure to comply with statutory requirements to their advantage." The Court further denied recovery of attorneys' fees under Pennsylvania's statute regarding bad faith conduct in litigation because that statute only deals with bad faith conduct occurring during litigation. The bad faith acts complained of in construction projects typically occur well before litigation is commenced.

In *Clipper Pipe and Service, Inc. v. Ohio Casualty Insurance Co.*, the Pennsylvania Supreme Court further clarified that neither CASPA nor the Prompt Pay Act applies to construction projects where the owner is a federal government entity, regardless of whom the payment dispute is between. In cases involving federal projects, the parties are generally limited to remedies provided by contract and federal law.

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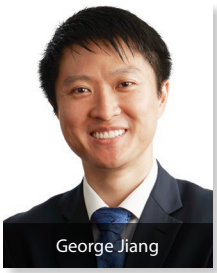
Differing site condition defense rejected


George Jiang

When formulating a bid on a construction project, it is important to distinguish between the site conditions directly supported by the owner's data and any assumptions made about the site conditions based on that data. This distinction is especially important when the bid documents are accompanied by a disclaimer provision that shifts to the contractor any risk of assumptions the contractor made that differ from the owner's data. The recent ruling by the Court of Appeals for the State of Washington in *King County v. Vinci Construction Grands Projets*, which resulted in the affirmance of a substantial judgment of $155.8 million in damages against the joint venture contractor VPFK, provides a cautionary tale illustrating the consequences of proceeding with a large project based on faulty assumptions made despite the presence of a disclaimer provision.

This litigation involved the Brightwater Project, a major expansion of King County's wastewater treatment system to better handle the increasing sewage from a region that encompasses Seattle and Redmond. After conducting a bidding process, King County engaged VPFK to construct portions of the tunneling work for a fixed price and within a specified time frame. The construction of the tunnels was plagued with difficulties and setbacks stemming from unexpected soil conditions, and the project was significantly delayed. King County eventually retained another contractor to complete one of the tunnels and sued VPFK for default.

In the ensuing action, VPFK asserted that the County breached the contract by failing to grant change orders and time extensions for differing site conditions based on bid documents that failed to specify the number of transitions between different kinds of soil conditions. These bid documents included the Geotechnical Data Report (GDR) and the Geotechnical Baseline Report (GBR), which interpreted the raw data from the GDR. The GBR identified a number of soils and soil groups that contractors could expect to encounter as well as the location of the boreholes and the locations of the soil groups present at different depths within the boreholes. Crucially, the bid documents included a provision stating that the contractor was to accept full responsibility for making assumptions that differed from the baselines set forth in the GBR. A warranty statement contained in the GBR further warned that these geotechnical baselines were not necessarily geotechnical fact. Rather, the GBR only gave a representative range of values for the actual site conditions and cautioned that the locations at which the conditions are encountered may vary.

VPFK retained consultants to analyze the bid documents and develop its tender for the contract. One of the consultants explained that he applied an assumption that there would be a continuity of material between two given boreholes. During construction, however, VPFK observed that the frequency of transitions between one soil condition and another was significantly higher than expected. As a result, VPFK frequently stopped work to adjust the boring machines, leading to numerous delays.

The Court of Appeals held that the disclaimer provision and VPFK's unwarranted assumptions based on its consultants' interpretations of the bid documents precluded it from asserting a differing site condition claim. As its consultants would testify, their reports did not predict the number of soil transitions along the tunnel's path and that such a task was impossible. Even the lead estimator for VPFK testified that it was not possible to determine the exact composition of the soils between the boreholes and that the contractor's estimate did not take into account the number of changes in the soil.

As this case shows, where the bid documents are silent, a contractor bears the risk of encountering any adverse site conditions. Contractors must therefore be aware of the gaps in information provided by the bid documents and take care not to fill them with unwarranted assumptions about the site conditions.

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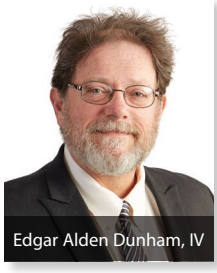
Arbitration clauses without express litigation waivers may be unenforceable in New Jersey


Edgar Alden Dunham, IV

In *Atalese v. U.S. Legal Services*, 219 *N.J.* 430 (2014), the New Jersey Supreme Court held that an arbitration clause in a consumer contract is not enforceable if the clause does not contain express language providing that the consumer is waiving his or her statutory right to seek relief in a court of law. While *Atalese* involved a traditional type of "consumer" contract, its holding would clearly apply to construction contracts that involve "consumers." A previous New Jersey Supreme Court case held an arbitration clause in a residential construction case unenforceable because the clause did not make clear that arbitration was the only remedy [*Marchak v. Claridge Commons, Inc.*, 134 *N.J.* 275 (1993)]. *Atalese* has since been cited in *Dispenziere v. Kushner Co.*, 438 *N.J. Super.* 11 (App. Div. 2014), which found an arbitration clause in a public offering statement for residential condominiums unenforceable.

Contracts for large, commercial construction projects are not typically considered "consumer contracts." Such contracts are usually carefully negotiated by sophisticated parties. Nonetheless, such entities can be considered consumers when they are purchasing goods or services that are not for resale or fall outside of the entity's area of expertise. For instance, a commercial entity that is a party to a construction contract for new facilities may be deemed a "consumer" for purposes of the New Jersey Consumer Fraud Act, *N.J.S.A.* 56:8-1, etc. It is not a leap to argue that under *Atalese*, any arbitration clause in a construction contract involving a commercial "consumer" must include an express waiver of litigation to be enforceable.

Interestingly, few of the standard-form industry commercial construction contract arbitration clauses contain this type the litigation waiver language required by *Atalese*. For instance, the standard form AIA A201 does not.

Contracts between subcontractors and general contractors are not "consumer contracts" because the work being performed by the subcontractor is passed on through resale. Nonetheless, there is an argument that one result of any flow-down clause in the subcontract (see ¶ 5.3 "Subcontractual Relations" in AIA A201-2007 for an example of a flow-down clause) would be to permit a party to a subcontract to render an arbitration clause unenforceable under the *Atalese* "consumer" requirement.

Of course, there are countervailing arguments that can be made against applying *Atalese* to construction contracts between sophisticated entities. But, at least in New Jersey, picking and choosing between contracts to decide whether to include an express waiver under *Atalese* is dangerous. The consequence of a wrong determination is the loss of the arbitration clause. The prudent solution is simple: Include the requisite waiver in *all* arbitration clauses. Adding it where it is not required doesn't harm anything. The waiver doesn't need to be complicated. An adequate waiver could simply say, "By executing this agreement, the parties waive their rights to resolve their differences through litigation in a court of law." Including the waiver language ensures that you will neither lose your carefully considered arbitration clause nor will you have to engage in debate as to whether a waiver was required.

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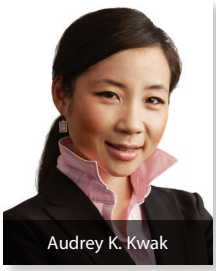
Redefining what is waivable: West Virginia agency's rejection of low bid for immaterial defect was improper


Audrey K. Kwak

Contractors bidding on public work, in theory, face a level playing field, with the underlying premise being that the lowest responsible bidder will be awarded the job. But in reality, this rule can be—and often is—unevenly applied. Low bids are often rejected for what seem to be inconsequential deficiencies in the bid, and conversely, nonconforming bids are found acceptable despite bid defects. Of course, public agencies are properly vested with considerable discretion to decide whether errors in bids are waivable or not. Courts—rightly so—are reluctant to interfere and second-guess that discretion.

But that discretion is not unfettered, as a recent West Virginia Supreme Court decision illustrates.

In *Wiseman Construction Company, Inc. v. Maynard C. Smith Construction Company, Inc. et al.* (November 10, 2015), Maynard (MCS) was the low bidder on a government construction contract for the renovation of the Lottery's headquarters building in Charleston, West Virginia. The Purchasing Division of the Department of Administration and the Lottery Commission (the Agency) awarded the contract to the second-lowest bidder (Wiseman) when it was discovered that MCS did not include references described in the bid documents with its bid.

While this sounds like a straightforward case of a noncompliant bid, in this case, MCS's omission was due to errors in the Agency's own forms—specifically, even though the qualification statement seeking references was described in the bid specifications, the approved bid form did not include any section in which to list those references.

When the bids were first opened, MCS was the low bidder and the initial recommendation was made to award MCS the contract. Wiseman took issue with this when it found that MCS had omitted the qualification statement, and the Agency then decided that it had no discretion to waive what it deemed to be a material and mandatory requirement. The contract was awarded to Wiseman.

MCS protested this decision, which the Agency denied. MCS then petitioned the circuit court for an order mandating that the contract be awarded to MCS.

The circuit court decision

The court granted MCS's petition, finding that the Agency's decision was not "rational" because the references requirement was ambiguous and without purpose. Despite the Agency's insistence that the references requirement was material and nonwaivable, the Agency's witnesses admitted that they had never contacted Wiseman's references, and that the architect on the project found both MCS and Wiseman to be qualified. Agency witnesses also did not know who had requested the list of references or for what purpose.

In its decision, the circuit court noted first that West Virginia law permits waiver of "minor irregularities in bids or specifications when the Director determines such action to be appropriate" before finding the Agency's conduct to be "shocking to the conscience of the [c]ourt."

The West Virginia Supreme Court's decision

On appeal, the West Virginia Supreme Court affirmed, finding the Agency's action not rational and that "the public interest of ensuring that tax dollars for public works are spent wisely predominates over the Agency's stringent adherence to faulty bid specifications." The Court noted that "MCS's failure to attach a separate sheet of references to the bid form was fatally dispositive yet, at the same time, utterly meaningless," which the Court deemed "nonsensical," offensive to "one's sense of fair play," and an arbitrary abuse of discretion.

As this case teaches, while bid protests are often challenging, they are not unwinnable. Agency action may seem unchecked, but courts are willing to take a close look and reverse agency action that elevates form over function and the public interest. In bidding on public projects, it is essential to keep this principle in mind.

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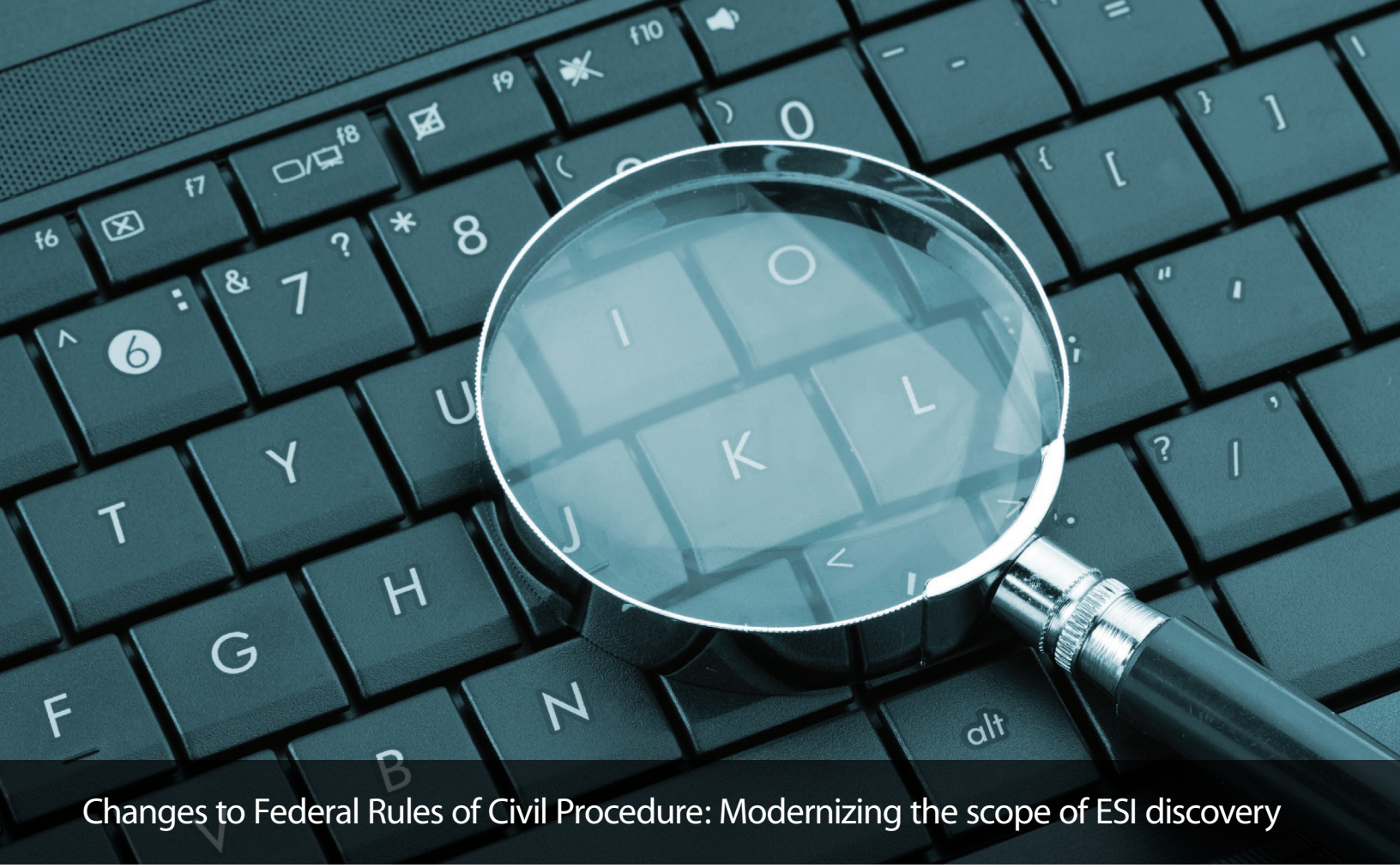
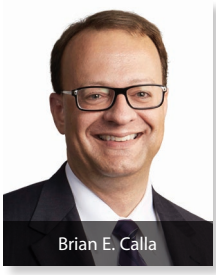


Changes to Federal Rules of Civil Procedure: Modernizing the scope of ESI discovery



Brian E. Calla

On December 1, 2015, changes to the Federal Rules of Civil Procedure (FRCP) affecting the discovery of electronically stored information (ESI) became effective for pending and future cases. At the core of the amendments is an effort to provide judges and lawyers with practical tools to help move the discovery process forward and keep costs under control. The changes to the FRCP reflect a general focus on cooperation and proportionality, but do not require extensive changes to existing practices by courts or litigants.

Generally, the amendments are intended to improve case management and discovery in federal litigation in response to the increasing demands of ESI. In a broad sense, the themes of the amendments are to:

- Promote early and active case management by increasing judicial engagement and requiring the parties and their counsel to work cooperatively in order to achieve a just, speedy and inexpensive resolution of every case (see FRCP 1, 4(m), 16(b), 26(d), (f)).
- Make discovery more proportional and effective by narrowing the scope of discoverable information and instituting best practices for discovery requests and responses (see FRCP 26(b), 34).
- Facilitate more effective Rule 26(f) meet and confers and to emphasize the importance of cooperation between the parties.
- Limit costly over-preservation of ESI by establishing a uniform sanctions plan that includes a reasonableness standard and a level of defensibility for missing ESI (see FRCP 37(e)).

Active case management is a theme throughout the rule amendments. The reduction of time for courts to issue a scheduling order is intended to reduce delays at the outset of litigation (see FRCP 16). This will make early case assessment and strong information governance policies in advance of litigation even more important. As soon as possible, litigants need to know:

- Where their data resides and the sources
- What types of data are implicated
- How many custodians are relevant
- What timelines are involved
- Whether international data is involved
- What types of legal hold protocols are in place
- How data will be reviewed and produced

Parties should develop an approach to e-discovery even if they have never had to produce ESI in litigation before. Having a formal discovery protocol for managing data, coordinating personnel (such as IT departments, international offices, etc.), and engaging outside help (such as legal counsel and technology providers) will become increasingly important to better deal with the shorter time frame requirements found in the amended FRCP 16.

The amendments to FRCP 26 restore the proportionality factors to their original place in defining the scope of discovery.

The amendments reinforce the Rule 26(g) obligation of the parties to consider these factors in making discovery requests, responses or objections. Proportionality reconciles discovery's scale and scope to the matter's specific needs in an effort to control costs. In most cases, the main factor that comes into play is expense. Does the burden or expense of the proposed discovery outweigh its likely benefit? What is the amount in controversy? The main push behind the change to FRCP 26 is to get judges and lawyers to look at ESI discovery as the tradeoff that it has always been, to try to get everyone thinking proportionally.

> *"Given the fast-paced and ever-changing arena where e-discovery best practices, the law and technology meet, the recent updates to the FRCP are a welcome guide for parties and their counsel to manage their ESI and the associated costs of document production."*

The amended rule also removes the previous "reasonably calculated to lead to the discovery of admissible evidence" language, in favor of an emphasis on the parties' obligations to consider proportionality throughout the discovery process. Under the amended Rule 26(b)(1), the relevant considerations in determining whether discovery is proportional to the needs of the case include:

- The importance of the issues at stake
- The amount in controversy
- The parties' relative access to relevant information
- The parties' resources
- The importance of discovery in resolving the issues
- Whether the burden or expense outweighs its likely benefit

The Committee Note emphasizes that the court and the parties have a continuing "collective responsibility to consider the proportionality of all discovery and consider it in resolving discovery disputes." The Notes also state:

> The burden or expense of proposed discovery should be determined in a realistic way. This includes the burden or expense of producing electronically stored information. Computer-based methods of searching such information continue to develop, particularly for cases involving large volumes of electronically stored information. Courts and parties should be willing to consider the opportunities for reducing the burden or expense of discovery as reliable means of searching electronically stored information become available.

Practically speaking, this focus on proportionality may cause parties to compromise more frequently when it comes to determining the number of custodians, time frames, data locations, search terms and other discovery parameters. Proportionality is almost always an issue in e-discovery. For example, if I see two new names copied on an important email, I might ask for a data collection from those individuals as well. The problem is that expanding the scope to two more corporate employees' data sets might yield tens of thousands of additional documents that need to be reviewed and prepared for production. Adding one or two more people to the search can have huge financial consequences to the responding party. Managing the litigation more efficiently with a mind for proportionality while working with critical team members such as legal counsel, IT departments and technology vendors will result in time and money saved in the long run.

Given the fast-paced and ever-changing arena where e-discovery best practices, the law and technology meet, the recent updates to the FRCP are a welcome guide for parties and their counsel to manage their ESI and the associated costs of document production. When the FRCP amendments to address ESI were first released in December 2006, Facebook had just been made public to users over the age of 13 and by August 2008 had around 100 million active users. The first iPhone was released to the public on June 29, 2007. Also, during this time period, the only "clouds" that concerned us were ones that sometimes required the use of an umbrella. By the time the 2015 FRCP amendments arrived, Facebook had over 1.5 billion active users, iPhones and smartphones had completely changed how we communicate with others and run our lives and businesses, and the "cloud" holds a lot more than moisture. It will be interesting to see how technology advances and how the law keeps up with it until the next FRCP update.

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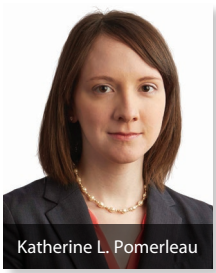
What happens in Vegas: "Mandatory" attorneys' fees not so mandatory in arbitration


Katherine L. Pomerleau

Do statutes requiring the mandatory award of attorneys' fees or costs also apply in arbitration proceedings? This is the issue recently addressed by the Supreme Court of Nevada in *WPH Architecture, Inc. v. Vegas VP, LP*.

This case involved an action for professional negligence brought by Vegas VP against WPH, relating to WPH's performance of architectural services for Vegas VP's condominium project. The parties had contractually agreed to arbitrate their disputes, and after an unsuccessful mediation, Vegas VP filed a demand for arbitration. Prior to arbitration, WPH made two offers of judgment to Vegas VP, both of which were rejected. The case proceeded to arbitration, and the arbitration panel ruled in favor of WPH, stating that each party was to pay its own costs and fees.

WPH appealed the portion of the order regarding the payment of costs and fees, arguing that the arbitration panel disregarded Nevada statutory law mandating that WPH be awarded reasonable attorneys' fees and costs. According to Nevada law, a party that makes an offer of judgment that its adversary does not improve upon is entitled to recover the reasonable attorney fees and costs it incurs. Further, a prevailing party in actions for more than $2,500 are entitled to recover their costs.

The Court agreed with WPH that the parties' action was governed by the substantive law of Nevada and the procedural rules of the American Arbitration Association. Further, addressing the issue for the first time, the Nevada Supreme Court agreed with those federal courts that consider the award of attorneys' fees to be a substantive, rather than procedural issue. Thus, the Court found that the Nevada statutes pertaining to the award of costs and attorneys' fees were substantive laws that applied to the parties' arbitration proceeding.

However, the Court went on to hold that since the Nevada statutes do not explicitly require the award of fees and costs in an arbitration proceeding, the arbitrators were not required to award such fees. In fact, the Court went on to state that no clear statute or authority exists that would require the award of attorney fees and costs in an arbitration proceeding.

This is clearly an important factor to be considered when drafting dispute resolution agreements, as it seems from this case that parties could unintentionally give up certain statutory remedies when choosing to arbitrate their disputes.

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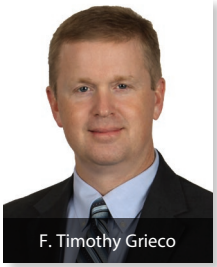
Can a statute of limitations start to run in a construction case before substantial completion?


F. Timothy Grieco

In *328 Barry Avenue, LLC v. Nolan Properties Group, LLC*, the Supreme Court of Minnesota wrestled with the question of whether a claim for a construction defect can accrue prior to the date of substantial completion. The Court ruled it could, but also stated that fact issues concerning ongoing construction activities and when the defect or injury was discovered may allow the claim to accrue after substantial completion.

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In *328 Barry*, the owner hired the general contractor to build a three-story commercial building. Construction began in 2008. During the punch-list phase in October 2009, the general contractor discovered a water leak in the location of a window. The stucco subcontractor was contacted, visited the project, and applied sealant to the window corners. Approximately one month later—in November of 2009—the stucco subcontractor was again contacted about water entering around the same window. The general contractor and the subcontractor conducted a "spray test" to determine the location of any leaking. While the testing revealed that leaking was still occurring, the record was unclear as to whether the general contractor or subcontractor made any further repairs at that time. Significantly, though, the owner testified that he believed the leakage problem had been remedied at that time and that no leaking occurred for the 10 months from November 2009 until August 2010. The project was substantially completed by May 2010.

However, in August 2010, the owner noticed water on the floor of the building in the vicinity of the same window. Throughout 2011 and 2012, investigations conducted by experts hired by the owner and general contractor confirmed the presence of construction defects relating to the presence of water at multiple windows. On June 14, 2012—more than two and a half years after the water issue was first noticed—the owner sued the general contractor, alleging failure to exercise reasonable care in performing its duties as general contractor, including negligent supervision of subcontractors and the negligent selection of building materials.

The general contractor moved to dismiss the owner's claim based upon the applicable Minnesota statute of limitations, which provides that "no action by any person in contract, tort or otherwise to recover damages for any injury to property . . . arising out of the defective and unsafe condition of an improvement to real property, shall be brought . . . more than two years after discovery of the injury." Minn.Stat. § 541.051, subd. 1(a). The general contractor argued that the injury—the water leakage—was discovered more than two years prior to the complaint being filed. In response, the owner argued that a construction defect claim cannot accrue prior to substantial completion and that the water leakage in 2009—far from being an actionable injury—was work that could have been completed or cured (and, in fact, was) prior to completion of the project. The trial court dismissed the owner's claim as time barred and the court of appeals affirmed.

The Supreme Court of Minnesota disagreed with the bright-line rule sought by the owner and ruled that nothing in the statutory language precluded the accrual of the claim (or, commencement of the statute of limitations) prior to the date of substantial completion. According to the Court, if the "injury" is "discovered" prior to substantial completion, the claim accrues at the point of discovery. The Court relied on the notable absence of the words "substantial completion" in Minnesota's statute of limitations and contrasted it with Minnesota's statute of repose—the latter explicitly extinguishing any claims arising 10 years after the date of "substantial completion."

However, in a twist, the Court nonetheless reversed the court of appeals and remanded the case to the trial court for a determination of when the "injury" was or should have been discovered. According to the Court, a genuine issue of material fact existed based upon "the lack of evidence of any leaks in the building for 10 months and the fact that construction activities were still being performed in the fall of 2009." The Court continued, "[o]n these alleged facts, one could conclude that the fall-2009 window leak had been repaired, so the actionable injury did not occur, and was not discovered, until August 2010."

Thus, while the Court eschewed any bright-line rule, it implicitly acknowledged the fact that ongoing construction activities may impact the determination of when an injury is or should be discovered. In a footnote, the Court also stated that the parties' written contract (which may govern inspection, warranties, remedies and dispute resolution at different stages of the project) may be relevant to determining precisely when a construction defect—identified before substantial completion—constitutes an "actionable injury."

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Construction Law Group NEWS

This issue marks an exciting milestone for us at *Construction Law* newsletter, as we proudly celebrate 10 years of providing clients and friends of Eckert Seamans with twice-yearly updates on developments in construction law. As always, we welcome and invite your feedback on the topics we explore in *Construction Law* newsletter, and encourage you to share the information with colleagues.

Matthew Whipple was recently promoted to the firm's membership (partnership). Since joining Eckert Seamans in 2007, he has demonstrated exceptionally strong legal skills and an unwavering commitment to providing clients with the highest level of service. Matthew frequently litigates construction-related disputes on behalf of companies at all points in the owner-contractor-subcontractor chain, and has particular expertise in federal procurement matters, including disputes under the Federal Acquisition Regulation. He earned his J.D. from the William & Mary School of Law.

Scott Cessar and **Chris Opalinski** were both selected for inclusion in *Pennsylvania Super Lawyers 2016* for Construction Litigation.

Vince Paluzzi and **Ed Dunham** recently contributed articles to the winter edition of the New Jersey Builders Association magazine, *Dimensions*. Vince wrote "New Jersey Supreme Court Addresses Application of Statute of Repose to Multi-phase Construction Project," and Ed wrote "Jury Demands in Construction Lien Claim Enforcement Actions in New Jersey." The publication is circulated to members of the NJBA, a housing industry trade association that provides continuing education and advocacy services for builders, developers, remodelers, subcontractors, suppliers, engineers, architects, consultants and other professionals.

The second edition of *Pennsylvania Construction Law: Project Delivery Methods, Execution and Completion* was recently released by the Pennsylvania Bar Institute. **Scott Cessar** and **Matthew Whipple** authored a chapter titled "Damages, Remedies and Alternate Dispute Resolution under Pennsylvania Law."

Tim Berkebile presented "Legal Update: Mechanics' Lien Law" at the Builders Association of Metropolitan Pittsburgh's 2016 Housing Professionals Education conference.

Matthew Whipple presented "Choose Your Own Adventure: Claims Under The Contract Disputes Act," during the Allegheny County Bar Association's Construction Law Section program Nuts and Bolts of Federal Contracting, as well as "Using Performance Standards to Mitigate Customer Disputes," at the Building Association of Metropolitan Pittsburgh's 2016 Housing Professionals Education conference.

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