



**RECENT COURT DECISIONS OF RELEVANCE
TO CONTRACT DOCUMENTS**

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1. **Issue:** Does a design professional's commitment to comply with the building code represent a heightened standard of care? *School Board of Broward County, Fla., v. Pierce Goodwin Alexander & Linville*. District Court of Appeal of the State of Florida (2014).

Summary: The school board retained an architectural firm to design the renovation of a high school, and new school facilities. The initial design called for a third floor balcony. A peer review of that design asserted that for fire safety reasons the building code required a separate stairway for the balcony. The architect disagreed, and believed that at a meeting on the issue it had persuaded the local building code official that no stairway was needed. After the project was bid and was underway, the building code official ruled that a stairway was needed. Some initial construction had to be reworked to accommodate a stairway. The school board sought to recover the extra costs from the architectural firm.

The 48-page owner-architect agreement contain this clause regarding the standard of care:

As to all services [Architect]...shall exercise a degree of care and diligence...in accordance with the customary professional standards currently practiced by firms in Florida **and** in compliance with any and all applicable codes, laws, ordinances.... [emphasis added]

The professional services agreement also contained two other statements to the effect that the architect's work would comply with applicable laws, regulations, and codes, and a statement that the architect's indemnification duty to owner applied if the architect had been negligent.

Decision: The trial court judge ruled that the applicable standard of care was "whether the architect prepared plans with ordinary and reasonable skill, which is a negligence standard." The school board argued on appeal that the contract's references to compliance with governing laws created a heightened standard of care—a "breach of contract" standard that was absolute, such that noncompliance with the building code established the architect's culpability, regardless of the professional standard of care.

On appeal the appellate court acknowledged that in the absence of the express contract clauses on code compliance, there would be no guarantee of design perfection and the standard would have been whether the architect used ordinary and reasonable skill, similar to that used by other architects, to draft plans that were code-compliant. However, the appeals court held that the code-related clauses raised the standard to what amounts to a warranty: the court ruled that the contract required the architect to "deliver plans that would be code-compliant, rather than merely requiring plans [to be] prepared with ordinary and reasonable skill services."

The court also held that the indemnity clause applied only to third-party claims, and hence had no bearing on the standard of care owed by architect to owner.

The case was returned to the trial court for new proceedings that would instruct the jury using the heightened standard of care, and allow expert testimony about code compliance without limitation by the common law standard of care.

Comment: The conventional wisdom has been that the common law professional standard of care is an overlay that should be used to analyze the performance of services by architects and engineers. Most of those services are performed in a contractual context, and most professional services agreements impose various tasks and requirements on the design professional. As long as express warranties, guarantees, and gimmicky standards (“absolute best services”) are avoided in contracts, the standard of care should apply in reviewing the professional services.

Whether stated in a contract or not, code compliance (and compliance with the law in general) is a basic expectation for professional services. As a practical matter there would be relatively few situations in which a design professional could deliver a design that was in conflict with the building code and yet meet the professional standard of care. However, there are some cases on the margin of code interpretation.

EJCDC® E-500 affirms that the traditional standard of care applies to all services performed by Engineer. 6.01.A. Logically this would include services in which the Engineer prepares a design that is meant to comply with the building code. The EJCDC standard of care clause itself is not diluted with the “**and** comply with the code...” wording that resulted in the separate and absolute standard created in the Florida decision. There is a subsequent provision, Paragraph 6.01.E, which requires that Engineer (and Owner) comply with applicable Laws and Regulations (which by definition includes codes). We may want to reflect on whether there are other ways to express or reinforce our intent.

The results in the Florida case might have been different if the architect had done more to document the “green light” that was supposedly given informally by the building code official. An uncertainty in the case is why the design was approved for purposes of proceeding with construction, without an adverse ruling at that point on the lack of a stairway.

As a final comment, every design professional should proceed with extreme caution in response to a critical comment from a peer review. Regardless of the standard of care, the risk of adverse consequences (not just during construction but also during the use of the school) was elevated substantially by the peer review criticism, and the architect’s decision to plunge ahead with the original design.

2. **Issue:** Architectural firm's entitlement to collect fees in a state where it is not registered. *DTJ Design, Inc., v. First Republic Bank*. Supreme Court of Nevada (2014).

Summary: DTJ is a Colorado-based design firm. It contracted with a Nevada developer to provide architectural services for a Las Vegas subdivision. Later, during a foreclosure of the property, DTJ sought to collect unpaid fees.

One of DTJ's architects was licensed in Nevada. Out of state A/E firms practicing in Nevada are required to register with the state (in some states this is referred to as obtaining a certificate of authority to practice). DTJ had not done so, nor could it have readily done so, because Nevada required that 2/3 of the ownership of an A/E firm must be by design professionals licensed in Nevada. By statute, only a registered firm is entitled to maintain an action to collect fees.

Decision: The Nevada Supreme Court confirmed the statutory rules, and rejected an argument that the services provided by the Nevada-licensed individual should be recoverable, as an exception to the general rule.

Comment: Although rules vary widely, in general an out-of-state firm must do the following: (a) a professional licensed in the host jurisdiction must be in responsible charge of the services, (b) the firm itself must be registered or have a certificate of authority to practice its A/E discipline in the host state, and (c) as a "foreign" business, under general corporate laws the firm must be registered to do business in the host state—usually this includes naming an agent who will accept service of process. Requirement (b) was the subject of the case, but in addition the court mentioned in passing that the Colorado firm had failed to comply with (c) as well.

3. **Issue:** May a Miller Act claimant give notice of claim via email? *United States ex rel. Cummins-Wagner Co., Inc., v. Fidelity and Deposit Co. of Maryland*. United States District Court for the District of Maryland (2013).

Summary: Federal construction project for the National Institute of Standards. Cummins-Wagner was a supplier to a subcontractor—a second-tier claimant for purposes of the Miller Act payment bond statute. The subcontractor failed to pay Cummins-Wagner, and it sought relief under the bond.

Second-tier claimants must give notice of claim to the prime contractor within 90 days of last providing labor or materials. Within that 90-day period the prime contractor, Milestone, contacted Cummins-Wagner directly to ask how much it was

owed by the subcontractor. Cummins-Wagner answered by email, detailing how much was owed and forwarding invoices.

After a time Cummins-Wagner, still unpaid, filed a lawsuit on the payment bond. The surety moved to dismiss, contending that the email to the prime contractor was not a legally sufficient notice.

Decision: The federal district court noted that although the Miller Act specifies methods for giving required notices, the key question in the federal courts has been whether the contractor received actual notice. Here, the contractor did not contest receiving the email report on the amount owed (in fact, the contractor had solicited the report). Without discussion of email's characteristics, the district court simply accepted that the transmittal was sufficient notice.

Comment: A "substance over form" ruling. Some courts will apply the "actual notice" test to contractually required notices. The prudent claimant will avoid the shadow of doubt by strict compliance with procedures (whether statutory or contractual).

- 4. Issue:** Scope of coverage of a contractor's pollution liability policy. *Acuity v. Chartis Specialty Insurance Co.* Court of Appeals of Wisconsin (2014).

Summary: During a construction project an excavation contractor ruptured a natural gas line. A resulting explosion destroyed a church, damaged nearby houses, and injured two utility employees. Various lawsuits ensued, including insurance disputes. The contractor's Commercial General Liability (CGL) insurer, Acuity, provided a defense and paid out on claims. Acuity contended that its insured's Contractor's Pollution Liability (CPL) carrier, Chartis, should share in the defense and claim costs.

CPL insurance protects contractors against accidental releases of pollutants that occur as a result of construction operations. The policy wording specifically refers to the "discharge dispersal, release or escape of any solid, liquid, gaseous or thermal irritant or contaminant" into the environment. The trial court held that natural gas was a contaminant that should not have been "loose in the environment" and therefore ordered the CPL carrier to share in the defense and claim costs. The CPL carrier disputed that an **explosion** was a "pollution condition" of the type insured against.

Decision: The Wisconsin Court of Appeals held that although a release of natural gas (an irritant or contaminant) might under some circumstances be an insurable event under CPL, in this case it was not contact with the natural gas, or its presence in the environment, that gave rise to claims, but rather its explosion and resulting fires. The nature of the various claims, as expressed in the lawsuits, did not fit within the scope of the CPL policy.

Comment: EJCDC's standard insurance provisions require that contractors carry both CGL and CPL. CPL is a relatively recent insurance product that was designed to cover risks that CGL does not (due to the CGL pollution exclusions). Here the CGL policy clearly covered the explosion and resulting damage. Thus the court of appeals decision appears to be consistent not only with the specific terms of the CPL policy, but also with the industry's comprehensive risk management structure for construction projects.

5. **Issue:** Contractor's right to pursue a claim against the project design professional for errors in the drawings and specifications. *LAN/STV v. Martin K. Eby Construction Co.* Supreme Court of Texas (2014).

Summary: The Dallas Area Rapid Transit Authority (DART) contracted with LAN/STV for the design of a light rail transit line. DART awarded the construction project to Eby. After beginning construction, Eby discovered that the design was full of errors, mostly in connection with existing conditions. Reportedly 80% of the project drawings had to be changed because of errors. Eby contended that its damages for delay and additional labor and materials were approximately \$14 million. Its attempts to pursue the claim under the contract with DART were only partially successful, partly due to procedural problems and partly on the merits. Eby settled with DART for \$4.7 million.

Meanwhile Eby filed a lawsuit against LAN/STV, alleging negligence in preparing the design. A jury agreed, awarding Eby a net judgment of \$2.25 million. LAN/STV appealed, and the case reached the Texas Supreme Court.

Decision: The focus of the decision was whether the economic loss rule barred the contractor from pursuing a claim against the owner's engineering firm. The court surveyed the history of the economic loss rule, nationally and in Texas, and concluded that the contractor, Eby, had no rights against the engineering firm, LAN/STV. The court cited the importance of preserving a boundary between contract and tort. Construction risks (including economic risks) can be allocated and managed by contract, resulting in predictability of results for the parties. By rejecting tort claims and limiting the parties to contract claims, "clarity allows parties to do business on a surer footing."

Comment: The Texas decision provides clarity in that jurisdiction to a common situation. Many state courts have taken the same position, but the law is less clear, or to the contrary, in some jurisdictions.

6. **Issue:** Architect's duty of care to future homeowners in designing residential building. *Beacon Residential Community Association v. Skidmore, Owings & Merrill*. Supreme Court of California (2014).

Summary: The Beacon is a 595-unit condominium building in San Francisco. The units were initially rented for two years, then sold to individual condo owners. After a time the new owners contended that as a result of design errors by SOM (teamed with HKS as principal architects), the building suffered from extensive water infiltration, inadequate fire separations, structural cracks, other safety hazards, and excessive heat gain resulting from substandard windows and ventilation.

One of the architects' defenses was that they owed no duty of care to subsequent owners of the building; their client had been the project developer, and their sole duty was to the client. The trial court agreed with this argument, and also found it significant that the architects' duty was to make recommendations to the client, but that final decisions as to the building's features were made by the client, not the architects.

Decision: The case ultimately made its way to the California Supreme Court. The court examined a long history of cases that had eroded the importance of privity (direct contractual relationship) as a defense to claims. The court found there was a long-established rule holding architects accountable to third-party homeowners. The court's specific holding was that "an architect owes a duty of care to future homeowners where the architect is a principal architect on the project—that is, the architect, in providing professional design services, is not subordinate to any other design professional—even if the architect does not actually build or exercise ultimate control over construction decisions."

Comment: The court expressed several reasons for its decision. Most fundamentally, the court noted that the architects' work on the project was plainly intended to affect future homeowners, and the ultimate aim was to provide safe and habitable residences for a specific, foreseeable, and well-defined class of potential claimants. There was no "specter" of vast numbers of lawsuits from an amorphous spectrum of third parties.

The decision noted that design professionals whose role on a project is minor and subordinate to the role or judgment of other design professionals are shielded from liability to third parties. It also disposed of the notion that the developer's ultimate decision-making power created a defense for the architect, noting the exclusive professional expertise of the architects and remarking that the project is not a "client-controlled environment" and that it would be bad public policy to make the client's interests paramount to the interests of the prospective homeowners in safety and habitability.

The court acknowledged the contract statement that there was no intent to create rights in third parties, but interpreted this as applying only to third-party beneficiary contract rights, and as not applicable to tort rights of third parties.