EJCDC
ENGINEERS JOINT CONTRACT DOCUMENTS COMMITTEE

RECENT COURT DECISIONS OF RELEVANCE TO CONTRACT DOCUMENTS

June 2010

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Issue	**Citation**	**Summary**	**Contract Document Implications**
1. Engineer's duty to defend owner in defective conditions case **[update]**	*UDC-Universal Development v. CH2M Hill*, California Court of Appeals, 2010	Residential condominium project. CH2M Hill provided engineering services to owner (developer). Homeowners Association (HOA) sued developer, alleging defective conditions including drainage problems, soil instability, erosion, and settling. HOA did not name engineer as defendant, and ultimately jury found that engineer had not been negligent and had not breached its contract. Owner-Engineer agreement contained a custom indemnification clause that included a defense obligation requiring engineer to defend owner with respect to "any claim or demand covered herein." Engineer rejected owner's tender of defense. After the trial, the Court of Appeals held that the duty to defend must be determined based on situation at the outset of the case, not at the end; whereas the actual indemnification duty does depend on the outcome of the case. Here, the allegations in the HOA complaint did not name CH2M, but the description of the defects did implicate the engineering work. Therefore a duty to defend existed at the outset, engineer should not have rejected the tender of defense, and subsequent jury findings were irrelevant.	EJCDC intentionally does not include a duty to defend in its indemnification clauses. This case has sparked some outcry, but the court was on solid ground in emphasizing the difference between a defense duty and an indemnity duty. The case stands out because it is rare for any member of the design and construction team to receive a clear, 100% exoneration from a jury. The wording of the custom clause was somewhat confusing and contributed to the engineer's hope that it could escape the defense obligation if engineer could prove it was without fault. **Update: Attempt to appeal failed. More disturbing issue is related California case (*Weathershield*) indicating that a contract**

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1. Engineer's duty to defend owner in defective conditions case *(continued)*	*UDC-Universal Development v. CH2M Hill*, California Court of Appeals, 2010	See above.	**must expressly disclaim duty to defend or duty will be assumed to exist, based on a California statute.**
2. Enforceability of Pay-if-Paid clause in subcontract.	*Universal Concrete Products v. Turner Construction*, U.S. Court of Appeals for the Fourth Circuit, 2010	Office tower project in Norfolk, Va. Owner went out of business due to economic downturn, and did not pay general contractor for concrete work performed by sub. Subcontract contained an unambiguous pay-if-paid clause (incorrectly referred to in the decision as a "pay-when-paid" clause). General Contractor's duty to pay sub was subject to "the express condition of payment [to GC] therefor by the Owner." Sub asserted that certain clauses in the prime contract created an ambiguity regarding the duty to pay subs, but the court found these arguments unpersuasive and concluded that the prime agreement and subcontract could be read together harmoniously on the subject of subcontractor payment. Court also noted that the governing state law, that of Virginia, included strong policy support for pay-if-paid clauses based on "freedom of contract." The court found no "paternalistic desire to protect one contracting party over the other" in Virginia law.	Assuming EJCDC policy is to give general contractors freedom to establish subcontract payment terms that fit the needs of the GC-Sub relationship, it is important to review whether any provisions in EJCDC C-700 could be construed as unintentionally dictating subcontractor payment terms; for example a review of lien waiver requirements.

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3. Highway engineer's scope of duty to motorists.	*Thompson v. Gordon,* Appellate Court of Illinois, 2010	New interchange and bridge deck replacement project. Professional services agreement spelled out scope of consulting engineer's duties, including design of new interchange, "improvements" to certain existing highway components, and design of "replacement" of bridge deck including related median. Years after completion of design and subsequent construction, motorists were killed when a car from the opposite direction jumped the median and crashed head-on. Lawsuit against engineers and others. Engineers moved for summary judgment and trial court granted the motion. On appeal, the Appellate Court first reviewed the substantive "scope of services" assigned in the contract. Improving the median was not in the scope, and engineers' design of a replacement median very similar to existing median was deemed sufficient. However, court then noted that the contract contained a standard of care requiring the "degree of skill and diligence normally employed by professional engineers… performing the same or similar services." Plaintiffs (estates of deceased motorists) submitted an expert's affidavit stating that an engineer has a duty to design with the safety of the public in mind, and should have required a tall "jersey barrier" to prevent jumps over the median. *(cont. next page)*	An engineer's general obligation to be mindful of the safety of the public while performing its services is nothing new. What is new is the notion that the routine standard of care can be construed as creating additional substantive duties beyond those set out in the scope of services. The standard of care is meant to be applied to the services that are performed, not to create new obligations, such as designing new safety barriers.

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3. Highway engineer's scope of duty to motorists. *(continued)*	*Thompson v. Gordon (continued)*	*(continued)* The court held that the standard of care created potential additional duties, over and above the scope of services, to consider safety improvements, and that further proceedings (a trial) would be needed to determine if positions taken in the expert's affidavit were correct. Dissenting judge lamented the "disturbing disregard" for precedent, and the "staggering" implications of the decision.	See above.
4. Does a contractual Limitation of Liability clause protect an individual design professional?	*Witt v. La Gorce Country Club,* Court of Appeal of Florida, 2010.	This case was previously reported (February 2009); this 2010 decision follows a rehearing. Witt is a professional geologist who did business as Gerhardt M. Witt & Associates. The firm entered into a contract to provide professional services on a water treatment system for a golf course. The contract included a limitation of liability (LOL) clause. The project was a failure and the owner sued the firm as well as Witt individually. The court held that (a) the LOL did not protect Witt, who was not a party to the contract; and (b) in all such cases there is an extra-contractual negligence claim available against the individual design professional, and a provision in a contract is invalid and unenforceable as to the individual.	The decision rests on provisions of the Florida A/E licensing statutes concerning the liability of design professionals. The result is that individuals are exposed to more liability than their firms. It is possible that the Florida Supreme Court would take a different view. There are strong public policy arguments that could be made in support of changing either the decision or the underlying statute. EJCDC recognizes that its LOL clauses (typically offered as options in Exhibit I) are not enforceable in all jurisdictions. The clauses expressly extend protection to employees.

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5. False Claims Act violation for submitting Application for Payment when contractor is in breach of contract.	*San Francisco Unified School District ex rel. Contreras v. Laidlaw Transit, Inc.,* Court of Appeal of California, 2010.	Contract to provide school bus service required buses to be in good working order for safety reasons, and also required buses to meet or exceed various pollution (emissions) control requirements. According to former bus company employees, SF school buses routinely did not meet contractually required standards for safety or pollution control. Employees initiated lawsuit based on California's False Claims Act, which imposes triple damages and attorneys fees for false claims against a public agency. Bus company countered that the contract did not require that pay applications be certified, nor was any express certification of compliance made in pay applications or elsewhere. Court held that certification of meeting contract requirements was implied in every payment application, and that bus company's payment applications were "False Claims" if buses were not in compliance with mandated standards.	EJCDC standard Application for Payment (EJCDC C-620) does include contractor's certification "that all Work….is in accordance with the Contract Documents." If such is not the case, then application is potentially a False Claim. A 2001 California False Claims Act case concerned the sale of potable water pipe to the City of Pomona. The pipe was not in compliance with specified standards, and was made of an inferior metal combination that did not minimize corrosion. Court there held that request for payment was a False Claim.

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6. Liquidated damages for failure to meet deadline for completing highway striping project.	*Highway Specialties, Inc. v State of Montana Dept. of Transportation,* Supreme Court of Montana, 2009	$370,000 contract to stripe highways, to be completed by onset of winter. Liquidated damages of $387/day based on MDOT rate for contracts of that dollar amount. Contractor started work two months late, was only half done when winter arrived, and completed work in the spring, 176 days late, resulting in L/Ds of $68,172. Contractor protested that liquidated damages were out of proportion to any actual damages that DOT may have incurred, and contended that L/Ds could not be imposed in a "contract of adhesion" and that the damages were "oppressive" and not within contractor's reasonable expectations. Court held that this was not a contract of adhesion because contractors were free to negotiate standard terms each year under a DOT process; damages were not oppressive or excessive given value to traveling public of having clearly marked roads; damages were completely predictable given that rate was stated in the contract, contractor was familiar with DOT projects, and contractor brought late completion on itself through late start.	Contractor here was tempted into challenging the L/Ds by a recently published Montana court decision that established seemingly favorable standards for judging an L/D clause. However, the standards when applied were really not so different from the typical rule that liquidated damages clauses will be enforced unless they are penalties or grossly excessive. The EJCDC L/D clause specifies that L/Ds are not intended as a penalty. Facts here were bad for the contractor, and no surprise that it was not successful in escaping the L/Ds. Montana DOT's use of a formula is not uncommon. Best practice for L/Ds is a project-specific determination of L/D amount, typically conducted by owner and engineer, and supported by documentation of the assumptions made and the process followed.

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7. Enforceability of Liquidated Damages provision	*New Athens Generating Co. v. Bechtel Power Corp.,* D.C. Superior Court, 2010, confirming award of arbitration panel.	$533 million power plant EPC contract included $149,000/day liquidated damages for unexcused delays in completion. L/Ds totaled $26.9 million, as Bechtel completed work over 200 days late. Arbitration panel held that the L/D daily amount would be enforced as long as it was not a penalty, which was dependent on whether the amount was unreasonable at the time the contract was negotiated. It is irrelevant if the amount in hindsight is higher than actual damages. A major factor in favor of presuming that the L/D amount was reasonable was the knowledge and sophistication of the parties with respect to power plant contracting. The two had entered into numerous previous EPC contracts with one another and otherwise, and were represented by competent and experienced negotiators.	As indicated in item 6 above, a well documented project-specific process should be followed to establish a defensible liquidated damages amount. The presumed reasonableness of the amount is enhanced if the contractor had the opportunity to negotiate the terms of the contract, and did not object to the proposed L/D amount.

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8. Elevator manufacturer's duty to warn design team that weather would affect elevator's performance.	*Village of Sturtevant v. STS Consultants et al.,* Court of Appeals of Wisconsin, 2010	Passenger rail station project. Engineer and architect developed design that included elevators in an open-air design with a nine-foot setback. Design team consulted with Otis Elevator while writing elevator specifications, but Schindler Elevator ultimately entered into a contract to supply the elevators. Undisputed that the Schindler elevators complied with the specifications. The elevators malfunctioned during rain and snow. The design team contended that Schindler should have reviewed the design and advised that the elevators would not be suitable for the intended purpose due to exposure to the elements. Court held that facts were undisputed and confirmed summary judgment for Schindler. As a matter of law Schindler's sole duty was to comply with the contract specifications, which it did. Schindler had no other role—the design team had not consulted with Schindler, but rather had sought advice from Otis.	The EJCDC construction documents require Contractor to report any errors that it discovers in the Contract Documents, during the bidding process and before and during construction. Such requirements in the Sturtevant project documents might have been applicable; however, intent of EJCDC clauses is not to impose design analysis duty on contractor, but rather to encourage reporting of obvious errors.

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9. Application of standard contract term that establishes starting point for statutory limitation period.	*Federal Insurance Co. v. Konstant Architecture Planning*, Appellate Court of Illinois, 2009.	Owner-Architect agreement (AIA) contained a clause that stated that statute of limitations for bringing a claim against architect would commence to run no later than the date of substantial completion. Illinois statute of limitations (for a claim that a house was poorly designed, resulting in moisture and mold problems) was four years from the date that the claimant knew or reasonably should have known that the design error had occurred. Court confirmed that the contract clause was enforceable and that the four year claim period began as of substantial completion. The claim was brought five years after substantial completion, and therefore was not timely.	For a claim period that is based on discovery of the error (such as the Illinois construction statute of limitation, and many tort statutes of limitations), the contract clause has the effect of shortening the limitations period if the error was not discovered until after substantial completion. Most states allow parties to a contract to shorten statutory claims periods if they wish to do so. EJCDC has a similar clause, establishing that a claim period begins no later than substantial completion, in E-500 (Owner-Engineer Agreement) and other E-Series documents.

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10. Exposure of county's environmental consultant to liability to developer	*Lake Almanor Associates v. Huffman-Broadway Group,* California Court of Appeals, 2009	Developer submitted application to construct a 1300 acre mixed use project. California law required preparation of an Environmental Impact Report. County retained an environmental consulting firm to prepare the EIR, with costs and fees to be paid by developer. The EIR contract specifically identified the proposed project and established a firm deadline for completion of the report. The consultant was late in preparing the report, and then submitted an unacceptable draft. The county terminated the consultant, billed the developer for the amount owed to the consultant, and hired a second consultant to complete the EIR. The end result of the delays, according to the developer, was inability to sustain the project and loss of sales and profits. The developer therefore sued the ineffective first consultant. The trial court and appellate court held that the developer did not have a claim against the consultant. The developer was held to not be a third-party beneficiary of the county-consultant EIR contract. The court of appeals pointed out that exposing county consultants to claims from developers might compromise their independence in evaluating a project's potential environmental impacts.	EJCDC professional services contracts contain "no third party beneficiaries" clauses. Other courts have reached different decisions on cases with facts similar to those in *Lake Almanor*. Of special concern to design professionals are situations in which the services rendered to a municipality are not exclusively for the public good, and where a known third-party is benefitting from and paying the bills for the services.