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Letter from the Editor

Welcome to the summer 2018 edition of our Under Construction newsletter. In this issue, to accompany the summer heat, we highlight several hot topic items affecting the construction industry. For example, delay and disruption issues can arise in any project. The first article introduces these issues and explains the legal requirements for both delay and disruption claims, and provides some practical ideas.

Next, we follow with a very recent decision by the National Labor Relations Board which held that two separate construction contractors constituted a single employer and a joint employer under pertinent labor law. We will be sure to keep an eye on how this decision plays out in the coming months.

Our third article looks at some of the recent legislation proposed by the California Legislature in this first half of 2018 surrounding the California Environmental Quality Act ("CEQA"). A brief summary of some of the proposed CEQA amendments is included for your review.

In recent years, a few law firms have made a cottage industry of enticing condominium home owners associations to sue the project developers over many issues, very often for alleged construction defects. Numerous homeowners' associations have filed lawsuits against developers, contractors, and builders for purportedly defective work. The recent Utah Supreme Court ruling in *Gables v. Castlewood-Sterling*, 2018 UT 04, reiterates what many courts seem to have forgotten. Our fourth article reminds us that in Utah unless a plaintiff has contractual rights, or has been assigned such rights, it cannot maintain a cause of action when privity of contract is an essential element of a claim.

Finally, our fifth article reviews the recent case of *United Riggers and Erectors, Inc. v. Coast Iron and Steel Company*, and how the California Supreme Court addressed whether a direct contractor can withhold payment from a subcontractor based on the "good faith dispute" exception pursuant to the state's prompt payment laws. Prompt payment laws exist in a number of jurisdictions and how courts address different aspects of prompt payment laws can provide valuable insights.

We hope you will find these articles informative and enlightening. Please let us know if you want us to address a specific construction issue in a future newsletter. Stay cool out there and have a safe and enjoyable summer!

Regards,

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James J. Sienicki

Delay and Disruption Claims

by James J. Sienicki and Creighton R. Dixon

Delay and disruption issues can come up in any project. This article offers an initial introduction and explains the legal requirements for both delay and disruption claims, and practical ideas.

The Law

Delay and disruption claims are two similar, but distinct concepts. As the *Bell BCI Co. v. United States* court summarized, "Although the two claim types often arise together in the same project, a 'delay' claim captures the time and cost of *not* being able to work, while a 'disruption' claim captures the cost of working less efficiently than planned."

Contractors have the burden of proving the same elements for both of these claims: liability, causation, and damages. They can usually establish the requisite liability by pointing to:

- Impacts due to errors and omissions in design documents (though not design-build contracts if caused by the contractor's design team);
- Impacts caused by having to perform work out-of-sequence;
- Delays which push the project into periods of adverse weather conditions; and/or,
- Effects of excessive overtime due to acceleration.

Causation can usually be shown if the events were:

- Unforeseeable at the time of contract or change order execution;
- Beyond the contractor's control;
- Caused by the owner or design professional (though not design-build contracts if caused by the contractor's design team); and/or,
- Caused by situations for which the owner assumed contractual liability (e.g. force majeure or differing site conditions).

The damages element is distinct for the two claims. Proving a delay claim requires the contractor to show it was delayed on one of its critical path activities because of someone else's actions, and how that delay cost it additional dollars in general conditions, standby costs, or otherwise. Typically, to obtain a time extension or additional compensation for extended performance based on the terms in the contract, the delay generally must affect overall project completion, meaning, the delay must be *critical*. Additionally, recovery may be barred to the extent the contractor was responsible for any concurrent delay or if the contract has a valid no damages-for-delay clause.

On the other hand, loss of productivity claims are instead concerned with unanticipated increases in the costs incurred to perform any given work activity. In other words, the contractor incurred more labor costs to get the job done because it had to work overtime, it had to use more employees than planned, or there was stacking of the trades or other causes making it less efficient. It is irrelevant for loss of productivity claims whether the impacted activities lie on the critical path, although loss of productivity is often a consequence of a prior delay. While it may not necessarily require a precise calculation, proving how the contractor was less productive typically requires utilizing a methodology recognized by the courts. Sample methodologies include: actual cost method (if actually tracked during the project); measured mile; similar work comparison; specialty and/or general industry studies; and, modified total cost method (some or all of which may require expert testimony).

The Project's Facts: Contract Provisions and Practical Issues During the Job

With the above general elements in mind, the specific contract's requirements are the next area to focus on. While contracts will vary, the contract's definitions and other pertinent sections are crucial. Focus on definitions and terms like: Substantial Completion/Time; Date of Commencement; Scheduling (i.e. Critical Path Method); Disruption/Lack of Productivity; Claim Provisions for Delays (Unexcused vs. Excused Delay) (Compensable vs. Non-Compensable Delays); Claims and Notices of Claims, No Damages for Delay and Disruption Clauses; and Concurrent Delays. Important provisions in the contract can include provisions relative to the schedule of work, the contractor's ability to manage and modify the work plan, schedule and sequence, and its ability to seek relief from the owner arising out of changes to and impacts upon its work plan and schedule. Notice and claims provisions will almost certainly affect the claims process.

Because they can govern how claims will be addressed, it is important everyone (owners and contractors) understand the contract's obligations and terms before contracting. Certain terms, such as a "no damages for delay/disruption" clause, could be the subject of negotiations.

After agreeing to terms, documenting the contractor and subcontractors' work is the next issue. Both the owner and contractors should carefully document the work during construction in order to prove or be able to defend against such claims on the project. The contractor typically has the burden of proving how the delay or disruption impacted it, and the amount of its damages. Generally, contemporaneous notes and explanations for deviations from the work plan (including photos/videos) are most persuasive. Other ideas owners and contractors can consider include:

- Detailed daily reports;
- Track and/or monitor actual costs directly attributable to the delay or disruption separately;
- Document and/or monitor time and resources and require the use of separate cost codes to track hours spent on work outside the original scope or caused by delays or disruptions versus hours spent or anticipated on base contract work;
- Use and/or require a uniform system of recording field labor and equipment productivity on a contemporaneous basis;
- Routinely compare actual labor and equipment productivity to as-bid or as-planned; and
- Prepare and/or review job cost reports at least monthly.

Even after work has started, the parties should understand the documents they are signing. Change orders, payment applications, and related lien waivers and releases may contain language which may fully resolve, waive, release, or otherwise affect delay and disruption claims.

Cumulative Impact Claims

Beyond the release and waiver concerns associated with signing a change order, the cumulative impact is another issue to consider. The cumulative impact is the corresponding ripple effect on the base contract and other change order work when a project requires numerous change orders. Cumulative impact problems are likely to follow:

- Work flow disruption;
- Out of sequence work;
- Lack of materials;
- Same work but different conditions;
- Base contract work performed in adverse weather conditions; and
- Significant overtime.

The same principles for delay and disruption claims apply to cumulative impact claims. Practically, this means parties may want to document the ripple effect and associated costs of numerous change orders as soon as they identify a possible cumulative impact claim. This can be difficult, and an expert may be necessary.

Consider Both the Prime Contract and the Subcontract Requirements

When any delay or disruption claim arises out of something for which the owner may be responsible, a contractor may want to work with their subcontractors to prove their claims. Given there are typically multiple tiers of contracts involved, it is important to evaluate what the subcontractors' responsibilities are. In addition to the prime contract's terms, consider looking at subcontract provisions covering the same issues discussed above, as well as delay or disruption claims caused by owner or for which owner is responsible, and delay or disruption claims caused by prime contractor or for which prime contractor is responsible. The subcontractor's remedies are likely limited by the prime contractor's obligations and responsibilities to the owner, and the prime contract. For example, the prime contractor is likely obligated to provide the owner written notice within a certain number of days of knowledge of the facts giving rise to the event for which the claim is made. Because the prime contractor is obligated to notify the owner within a certain amount of time, the subcontractor needs to tell the prime contractor even earlier.

Getting the Right Help

Finally, contractors and owners should consider finding the right help. Consultation with knowledgeable legal counsel and claims consultants early in the process may be helpful in analyzing potential claims. The attorney may want to keep work product and privilege protections in mind when hiring the consultant. The attorney and the consultant can analyze the relevant contracts, original work plan, impacts, costs incurred, and the likely factual and legal defenses.

When you meet, the lawyer may want to see:

- Signed contracts and work plans;
- Daily reports addressing labor and other resource utilization, as well as any project conditions that have delayed or impacted performance;
- Written notices and meeting minutes regarding any delays or impacts;
- Proof there was or was not follow up in a contractually proper and timely manner to present a quantification of time and/or money sought as relief; and
- Key Change Orders, Lien Waivers, and Payment Applications.

Before a claim is even filed, a consultant can be helpful for interpreting construction plans, explaining industry usage and standards, and offering a realistic analysis of the performance. This can help negotiate an early and advantageous settlement. If the attorney retains a consultant at the outset, the consultant may be able to help obtain and preserve important evidence for later use (site inspections; photographs/video; repair/redesign efforts; and damage mitigation efforts).

Conclusion

Delay and disruption claims are a complicated and fact-intensive issue for all parties involved. They require evaluating actions before the work (understanding the contracts), during the work (record-keeping), and after there is a problem (working with attorneys/consultants). Keeping these ideas in mind should help you navigate the next delay or disruption issue you come across.

The Labor Angle

by Gerard Morales

In a very recent decision the National Labor Relations Board (Board) held that two separate construction contractors constituted a single employer and a joint employer under

labor law. Both entities were, therefore, jointly and severally liable for remedying the unlawful termination of seven employees who had engaged in a strike against one of the contractors. *Hy-Brand Industrial Contractors, Ltd and Brandt Construction, Co.* 366 NLRB No.94 (2018). At the national level, regulation of commercial drone use is administered by the Federal Aviation Administration (FAA). The FAA's final rule for small, unmanned aircraft went into effect on August 29, 2016. The FAA has provided a summary of the key operational limitations for drones or unmanned aircraft systems (UAS) which, among others, include the following:

1. common ownership;
2. common management;
3. interrelation of operations; and
4. common control of labor relations.

Finding that all four factors were present, the Board held that Hy-Brand and Brandt constituted a single employer and were therefore jointly liable to remedy the unfair labor practices that were committed when the employees were terminated for engaging in the work stoppage.

The Board also held that Hy-Brand and Brandt were joint employers under current labor law. Under current law it is not necessary to show that one of the employing entities exercises actual control over essential terms and conditions of employment of the other entities. It is sufficient to show that one of the entities has the authority to do so.

Recent Developments In California CEQA Legislative Proposals

by Cary D. Jones*

The California Legislature has been active during 2018 in introducing legislation designed, in part (i) to exempt affordable housing projects in "Opportunity Zones" from the California Environmental Quality Act ("CEQA"), (ii) to limit the time for courts to rule on CEQA challenges, (iii) to clarify the standards that must be met for a court to enjoin a housing development project, (iv) to shorten the time within which a CEQA challenger can file an action against a public agency alleging a CEQA violation, and (v) to amend other general CEQA provisions. Here is a brief summary of some of the proposed CEQA amendments:

1. **AB-3030. Assemblywoman Caballero, D-Salinas (Feb. 16, 2018)**

   Qualifying affordable housing projects in low-income "Opportunity Zones," which have recently been officially designated by the federal government in California, may proceed without undergoing CEQA review if the project proponent certifies that the project is a "public work" or otherwise meets certain wage and hour requirements.

   i. The bill would exempt from CEQA a project that is financed by a qualified opportunity fund and that meets certain CEQA requirements.

   ii. As of May 18, 2018, the Department of the Treasury has designated 273 Opportunity Zones in Los Angeles County. Please visit the Opportunity Zones Resources page at the U.S. Department of the Treasury, Community Development Financial Institutions Fund, at https://www.cdfifund.gov/Pages/Opportunity-Zones.aspx.

2. **SB-1340. Senator Glazer, D-Orinda (Feb. 16, 2018)**

   Courts have 270 days to rule on lawsuits challenging housing projects. In an action alleging a violation of CEQA, the court may not stay or enjoin the siting, construction, or operation of a housing development project unless the court finds:

   i. The continued construction and operation of the housing project presents an imminent threat to public health and safety; or

ii. The project site contains unforeseen important Native American artifacts or unforeseen important historical or archaeological values that would be damaged by the housing project.

3. **AB-3099. Assemblyman Santiago, D-Los Angeles (Feb. 16, 2018)**

This bill would shorten the time periods within which a person is required to bring an action alleging that a public agency violated the CEQA requirements.

i. An action alleging that a public agency has approved a project that may have a significant effect on the environment without having determined whether or not it will have a significant effect on the environment will be commenced within 160 (instead of 180) days from the date of approval of the project (or commencement if the project is commenced without a formal decision from the public agency).

ii. An action alleging that a public agency has improperly determined whether a project may have a significant effect on the environment, or that an environmental impact report does not comply, must be commenced within 15 (instead of 30) days after filing notice.

4. **AB-2341. Assemblyman Mathis, R-Visalia (Feb. 13, 2018)**

(a) Except as specified, aesthetic effects of projects meeting certain requirements are not significant effects on the environment for the purposes of CEQA. A lead agency is not required to evaluate the aesthetic effects of a project and aesthetic effects shall not be considered significant effects on the environment if the project involves refurbishing, converting, repurposing, or replacing an existing building that is:

i. Abandoned, dilapidated, or has been vacant for more than one year;

ii. The building site is immediately adjacent to parcels that are developed with qualified urban uses . . .;

iii. The project includes the construction of housing;

iv. Any new structure does not substantially exceed the height of the existing structure; and

v. The project does not create a new source of substantial light or glare.

(b) These requirements shall not apply to either:

i. A project with potentially significant aesthetic effects on an official state scenic highway . . .; or

ii. A project with potentially significant aesthetic effects on historic or cultural resources.

(c) This section will be in effect until January 1, 2024, and then repealed.

5. **SB-1341. Senator Glazer, D-Orinda (Feb. 16, 2018)**

(a) In an action brought under CEQA, a plaintiff must:

i. Disclose the identity of a person / entity that contributes over $1,000 towards the costs of the action;

ii. Identify any pecuniary or business interest related to the project of any person / entity that contributes over $1,000 to the costs of the action.

(b) The plaintiff may request permission to withhold public disclosure of a contributor, which the court may grant if it finds that the public interest in keeping the information confidential clearly outweighs the public interest in disclosure.

(c) A lawsuit may not be brought challenging the approval of a housing project in a plan or project that has already been approved following the completion of environmental review.

6. **AB-1905. Assemblyman Grayson, D-Concord (Jan. 22, 2018)**

   In an action or proceeding seeking judicial review under CEQA, a court would be prohibited from staying or enjoining a transportation project that would reduce total vehicle miles traveled, that is included in a sustainable communities strategy, and for which an environmental impact report has been certified, unless:

   i. The continued construction and operation of the transportation project presents an imminent threat to public health and safety, or

   ii. The project site contains unforeseen important Native American artifacts or unforeseen important historical or archaeological values that would be damaged by the transportation project.

7. **AB-3027. Assemblyman Chavez, R-Oceanside (Feb. 16, 2018)**

   Attorneys' fees would be awarded to a prevailing plaintiff in an action or proceeding under CEQA, only if the prevailing plaintiff is either:

   i. A homeowner, property owner, or business owner, or a residential or commercial tenant whose tenancy is effective at the time the project application is submitted to the public agency, and that is located within a certain mailing radius, or

   ii. A 501(c)(3) or 501(c)(4) with an active membership of at least 50,000, formed primarily for the purpose of protecting the environment.

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* Cary Jones would like to thank summer associate Christina LaBarge who assisted with this article.

Utah Still Thinks Privity of Contract is Important

by Parker A. Allred

In recent years, a few law firms have made a cottage industry of enticing condominium home owners associations to sue the project developers over many issues, very often for alleged construction defects. Numerous homeowners' associations have filed lawsuits against developers, contractors, and builders for purportedly defective work. The recent Utah Supreme Court ruling in *Gables v. Castlewood-Sterling*, 2018 UT 04, reiterates what many courts seem to have forgotten. Specifically, *Gables* is a good reminder that unless a plaintiff has contractual rights, or has been assigned such rights, it cannot maintain a cause of action when privity of contract is an essential element of a claim.

In *Gables*, a developer planned a large residential development. Once the development was completed, the developer drafted and recorded the Declaration of Covenants, Conditions, and Restrictions (CC&Rs), by which the developer retained control of the HOA until a certain number of units were sold. In 2008, the target number of units had been sold and the developer turned over control of the HOA to the members. A short time later, the HOA claimed it began noticing many purported construction defects in the structural components of the development. As it investigated the extent of the damages, the HOA retained an expert who estimated that the damages exceeded $4,600,000.00. As a result, over the next several years, the HOA levied assessments on its members to pay for such costs, but then ultimately decided to sue the developer for damages.

Several parties were named in the suit, but whether the HOA was in privity of contract with the developer, and thus had standing to assert a claim for breach of implied warranty, was a key issue. There was no contract between the developer and the HOA; so, the HOA argued that the CC&Rs and the Real Estate Purchase Contracts created privity of contract.

The trial court disagreed with the HOA and granted summary judgment in favor of the developer, finding that the HOA had no right to sue third parties for damages on behalf of its members. An appeal ensued.

On appeal, the HOA raised additional arguments, but the Utah Supreme Court really only considered whether the CC&Rs somehow established privity of contract between the HOA and the developer. Utah law requires privity of contract to assert a claim for breach of the implied warranty of workmanlike manner and habitability. In fact, Utah Code §78B–4–513 provides that "an action for defective design or construction may be brought *only* by a person in privity of contract with the original contractor, architect, engineer, or the real estate developer" (emphasis added), but that "[n]othing in this section precludes a person from assigning a right under a contract to another person, including to a subsequent owner or a homeowners association." Ignoring this statutory proclamation of Utah policy, the HOA argued that the CC&Rs granted the HOA broad authority to act on behalf of its members, and inferred that under the CC&R's, the members had effectively assigned the HOA their rights to assert claims against third parties.

Although the court recognized that claims could be assigned in this context, it also made clear that under Utah law, an assignment of claims required specific language that demonstrated a manifestation that the parties intended something be transferred or assigned. And here, the CC&Rs demonstrated no such intent. In particular, the court noted that if a contractual provision lacked the words "assumes" "assigns," "transfers," or "conveys" of a specific subject matter, then that provision fails to manifest an intent to transfer or assign a right. In other words, words matter. Thus, because nothing in the CC&Rs demonstrated any intent whatsoever of the HOA's members to assign, transfer, or convey their contract rights to the HOA, the HOA had no rights to pursue against third parties. The Utah Supreme Court affirmed the lower court, and ruled that the HOA could not maintain an action against the developer for lack of privity.

While this case transcends construction litigation, it is a useful reminder that the participants in construction projects, from owner to the finish subcontractor, need to mind the contract p's and q's to keep and understand their rights.

California Supreme Court Clarifies "Good Faith Dispute" Under California's Prompt Payment Law

by Michael J. Baker

In recent case of *United Riggers and Erectors, Inc. v. Coast Iron and Steel Company* ___ Cal. 4th ___ (May 14, 2018 Case No. S231549), the California Supreme Court addressed whether a direct contractor can withhold payment from a subcontractor based on the "good faith dispute" exception pursuant to the state's prompt payment laws.

The issue in *United Riggers* was whether the good faith withholding exception applies to any dispute between the parties or only disputes directly related to the specific payment that would otherwise be due. The court held that the dispute must be directly relevant to the specific payment that would otherwise be due. *United Riggers* resolved the split of authority between two other California cases, *Martin Brothers Construction, Inc. v. Thompson Pacific Construction, Inc*. (2009) 179 Cal. App. 4th 1401, which held that any bona fide dispute can justify withholding of retention, and *East West Bank v. Rio School District* (2015) 235 Cal. App. 4th 742, which held that only disputes related to the retention security functions can justify withholding payment. It should be noted, that while *United Riggers* concerned the dispute over the correct interpretation of California Civil Code section 8014 (withholding of retention), the breadth of the Supreme Court's ruling appears to put an end to similar interpretation issues under other prompt payment statutes in California. Thus, for contractors who occasionally use as leverage or otherwise the "good faith" withholding provision to justifying nonpayment to a lower tiered party or contractor, it now appears that this will be contrary to California's prompt payment laws, at least when it comes to a dispute that is not directly related to the specific payment that

would otherwise be due.

In *United Riggers*, the owner contracted with Coast Iron to provide "miscellaneous metals" for work to construct an amusement ride at Universal Studios. Coast Iron, in turn, subcontracted with United Riggers to perform certain work. As is typical, the subcontract executed by United Riggers provided that Coast Iron would withhold 10 percent of amounts billed by United Riggers as retention to be paid at the end of the project. At the end of the project, Coast Iron requested that United Riggers submit its final change orders together with any outstanding change order requests. In response, United Riggers sent a letter to Coast Iron demanding $274,150.40 as compensation for "the mismanagement and/or delay deliveries caused by Coast Iron, as well as $70,384 in an outstanding change order request." Coast Iron's response was a rejection of the claim. United Riggers sought to recover all these sums as well as prompt payment penalties. Following a bench trial, the court issued a statement of decision denying relief to United Riggers on all its claims, finding that United Riggers had failed to follow the subcontract's procedures with respect to many change orders and that United Riggers had failed to show that Coast Iron was responsible for the actual expenses incurred by United Riggers. The trial court further found that prompt payment penalties were not appropriate because "there was a good faith dispute between Coast Iron and United Riggers… that entitled Coast Iron to withhold payment of retention." At the Court of Appeal, the Court affirmed as to United Riggers common law claims but reversed as to United Riggers' statutory claim on the prompt payment statute, finding that the good faith withholding exception to disputes must specifically relate to the specific payment at issue and that this interpretation was more in line with what the state legislator had contemplated when enacting the prompt payment statute. Accordingly, the appellate court determined that Coast Iron could not use the parties' dispute over mismanagement of the project as the basis for good faith withholding of United Riggers' retention. This appellate decision contributed to the split of already existing authority which has now ultimately been resolved by the California Supreme Court. This case should remind those in current disputes which involve the withholding of retention to review their current positions and the consequences thereof given the clarification of the law.

While the *United Riggers* case resolved a split of authority as to what a bona fide dispute has to relate to in order to justify withholding retention, it is important to note that some California prompt payment statutes, other than those related to retention, are waivable in writing. Therefore, this case may remind parties to review their contracts to determine whether and where prompt payment can be waived in order to manage risk.

Lastly, this case seems to clarify that when deciding to withhold a payment subject to prompt payment penalties a direct contractor may delay payment when the sufficiency of the subcontractor's construction-related performance is the subject of a good faith dispute, when liens or other demands from third parties expose the direct contractor to potential double payment, or when such payment would result in the subcontractor receiving more than the minimum amount both sides agree is due. In effect, the payor must be able to present a good faith argument for why all or part of the withheld monies themselves are no longer due. Moreover, this case seems to clarify that what a direct contractor may not do is withhold a retention that is an undisputed amount, because a dispute has arisen over whether additional amounts over and above the retention might also be owed.