Managing Construction Projects

Presented by:

Heber O. Gonzalez

Shughart, Thomson, & Kilroy, P.C.

Jeffrey B. Rosen

Polsinelli Shalton Welte Suelthaus PC

G. Steven Ruprecht, Esq.

Brown & Dunn, P.C.

Heather F. Shore

Brown & Dunn, P.C.

Overland Park, KS • May 23, 2007

Lorman Education Services
P.O. Box 509
Eau Claire, WI 54702-0509
Phone: 866/352-9539 • Fax: 715/833-3953
E-mail address: customerservice@lorman.com
Web site: www.lorman.com

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A DETAILED OVERVIEW OF THE CONTRACT FOR CONSTRUCTION

THE FUNDAMENTALS OF CONSTRUCTION CONTRACTS: UNDERSTANDING THE ISSUES

CONTRACT FORMATION - BIDDING - PUBLIC AND PRIVATE MISTAKES AND PROTESTS

DEFICIENT PLANS AND SPECIFICATIONS

THE FUNDAMENTALS OF CONSTRUCTION CONTRACTS: UNDERSTANDING THE ISSUES

DELAY AND DISRUPTION IN CONSTRUCTION

MANAGING CONSTRUCTION PROJECTS

LIEN CLAIMS - BOND CLAIMS - PROMPT PAYMENT ACTS - RETAINAGE STATUTES

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The learning objectives met in attending this program are:

- The attendee will be able to review design and performance specifications.
- The attendee will be able to discuss differing site conditions and changes.
- The attendee will be able to identify general and special lien requirements.

A Detailed Overview Of The Contract For Construction

Prepared and Presented by:

Heather F. Shore
Brown & Dunn, P.C.

A DETAILED OVERVIEW OF THE CONTRACT FOR CONSTRUCTION

Before the parties begin work on a project, they must first agree upon the terms of the construction contract. The written construction contract is a legal document that governs the parties' relationships throughout the course of the project. It sets forth the parties' respective rights and liabilities, as well as the scope of work and payment.

There are a number of different types of contracts used in the construction industry, some of which are handcrafted and some of which are merely printed forms issued by different industry organizations.

I. The Different Contract Types:

Owners, contractors and subcontractors have several different types of contracts to choose from when negotiating provisions that will govern their affairs on a construction project. Construction contracts frequently come in various broad categories including the following:

(a) lump sum contracts;

(b) unit price contracts;

(c) cost plus contracts;

(d) cost plus contracts with a guaranteed maximum price;

(e) design/build contracts;

(f) construction management contracts (with contractor at-risk and not-at-risk); and

(g) Job order contracts (JOC's) (indefinite supply contracts)

A. Lump Sum Contracts.

A lump sum contract is the traditional and most common type of contract used in the construction industry. The owner and contractor agree upon a fixed price for the completion of the work. Under the lump sum arrangement, the contractor bears all risk of loss with respect to the actual costs of completing the work within the scope defined by the owner's construction documents. Typically, lump sum projects are competitively bid, and they are commonly used for government work. Generally, if a contract is sent out by a government agency for competitive bidding, the bidders have little flexibility in negotiating the terms and conditions of the contract.

B. Unit Price Contracts.

A unit price contract is based on specified unit prices for estimated quantities of work. Unit price contracts are typically used on construction projects where the scope of the work to be performed is known by the parties, yet the precise quantities needed for the work are not yet determined. The owner pays only for the actual units or quantities that are constructed or supplied by the contractor. Typically a unit price contract concerns an easily measured quantity of work that needs to be performed, such as volume of earth removed, rock removed, concrete placed, etc. Different unit prices may be given for different anticipated volumes of work, thereby ensuring that volume discounts can be passed on to an owner while reducing the risk that a contractor may take in placing a low unit price on a small volume of work. Unit price contracts are common in public works project such as highway, dam, and bridge building projects.

C . Cost Plus Contracts.

Cost plus contracts are also popular with private owners. In a cost plus contract, the owner pays for the actual cost of the project plus either a flat fee or a percentage of the project costs. The contractor is required to substantiate the costs expended in performing the work in order to be paid. An advantage of a cost plus contract is that the owner only pays for the work that is actually performed by the contractor. The perceived disadvantage of a cost plus contract is the fact that the contractor has little incentive to keep the construction costs down. There is a small body of law, however, that has emerged in connection with cost plus contracts wherein courts impose upon the contractor a "fiduciary relationship" with respect to the owner that compels the contractor to manage and control the costs. This contract method appears to have limited use, and experience dictates that it is generally favored where an owner retains a large degree of control over the scope of the work and the labor, material, equipment and supplies to be furnished. However, a cost plus contract places more of a management burden on the owner. As a result, another variation of this contract type has emerged, which is the cost plus with a guaranteed maximum price.

D. Cost Plus with a Guaranteed Maximum Price Contracts.

The cost plus with a guaranteed maximum price contract is similar to a cost plus contract in that the owner only pays for the work that is actually performed by the contractor, plus a fixed fee. However, in addition, these contracts include provisions regarding a guaranteed maximum price for the construction. The advantage of that provision is that a contractor cannot charge for all of the work on the project without any bounds. Evidence of a breach of fiduciary duty to control costs is not necessary in order to deal with cost overruns. If work costs exceed the guaranteed maximum price, then the

contractor is simply responsible for the difference. These contracts frequently include shared savings clauses where the parties split cost savings when the cost of the work is less than the guaranteed maximum price. This is intended to provide an incentive for the contractor to keep the actual costs of the work down. This type of contract is very popular with private developers where projects are on a fast track. Developers often want to commence construction before a complete design is finalized and a lump sum price is established.

E. Design/Build Contracts.

In a design/build contract, an owner contracts with a single entity for both the design and construction of the project. A design/build contract is generally structured as a lump sum contract. However, it also may be written as a cost plus contract or a cost plus a fee with a guaranteed maximum price contract. Design/build contracts may enable construction to begin earlier and proceed faster due to the fact that the design need not be completely finished and ready for bid before construction can begin. This is also true because the shop drawings and submittal process is more streamlined with the single source responsibility. The design/bid contract delivery method has the advantages of speed, reduced cost and single source responsibility. *See Strain-Japan R-16 School District v. Landmark Systems, Inc.,* 965 S.W.2d 278 (Mo. App. 1998) (regarding a contractor's ability to furnish design services without compliance with Missouri designer licensing law). *See also Design-Build on Government Projects*, Ch. 8, in The Architect's Guide to Design-Build Services (G. William Quatman, II, *et al*. eds., 2003) (authored by Heather F. Shore, Esq); Kansas Committee on Appropriations House Bill No. 2394 (2006), concerning an Act for alternative project delivery construction and procurement regarding design/build construction and construction management in the State of Kansas

for public works; Missouri House Bill No. 1223 (2006), for public construction addressing prequalification procedures for bidders, construction manager at-risk delivery systems, design/build construction and job order contracting, including provisions regarding selection of contractors and the contracting process.

F. Construction Management Contracts.

Construction management contracts provide for the owner to retain a contractor (or even an architect, engineer or other person) in a management capacity to review plans and specifications and assist in budget preparation for the project, as well as manage the execution of the work. Construction management contracts typically take two forms; the at-risk form and the not-at-risk form. In the at-risk form, in addition to providing consultation, the manager may contract directly with some or all of the tradesmen and suffer the risk of loss for any cost overruns, nonperformance, or defects and deficiencies in the work. In the not-at-risk form, the manager may take bids from tradesmen but the owner contracts with them directly and suffers any attendant risk of loss during the course of performance. The manager simply assists in the work execution, among other management responsibility.

G. Job Order Contracts (Indefinite Supply Contracts).

Job order contracts (JOC's) generally involve a firm fixed price competitively bid procurement process with an indefinite quantity of work. This delivery system is designed generally for small to medium size construction projects, and it is also used for repair projects. These types of contracts are generally are used in the public setting as opposed to the private market and have as a primary feature the ability to contract multiple projects at one time avoiding the expense of competitively bidding each, every and all of the small projects.

II. Standard Form Agreements:

The use of standard form agreements when drafting construction contracts is recommended because construction contracts have become very complicated. The provisions in the standard forms are generally recognized and accepted within the industry, and they have been tailored by use and experience to coordinate obligations for various responsibilities. Forms are available from the American Institute of Architects (AIA), the Engineering Joint Contract Documents Committee (EJCDC), and the Associated General Contractors (AGC), just to name a few. The AIA documents are frequently used in building construction and projects overseen by architects. The EJCDC documents are used more frequently for heavy and highway construction such as roads, dams, bridges and tunnels, where the designer is more likely to be an engineer rather than an architect. The AGC forms are frequently used and are considered reasonably balanced. They do not, however, enjoy the same popularity as the AIA documents, which are generally thought to be more evenly balanced in terms of the rights and liabilities of the parties.

Regardless of the standard form that is used by the parties, the forms need to be reviewed and individual provisions or terms negotiated in order to tailor the terms and scope of the services and work to the subject project. Automatic tailoring is not recommended unless specific requirements of the project mandate it.

III. The Ten Most Important Clauses of the Construction Contract (With Two More to Make an Even Dozen):

For illustration purposes only, reference may be made from time to time to the AIA documents because they are the most comprehensive and widely used standard form agreements in the construction industry.

A. Payment.

One of the most sensitive areas for all the parties involved in the construction project is the payment process. Owners, as well as lenders, are concerned about overpaying the general contractor before work is completed and about holding sufficient retainage as security. On the other hand, general contractors and subcontractors are concerned about prompt payment. Any delay in the cash flow can essentially force the general contractor or subcontractor to finance the project, which may ultimately result in the contractor's insolvency.

1. The Types of Documents Necessary for Payment.

The AIA form contains requirements for progress payments. First, the contractor initiates the process by submitting an Application for Payment to the architect on a monthly basis. The application generally is itemized and notarized and supported by substantiating data. The owner will require supporting backup documents such as lien waivers, certified payrolls, schedule updates, test results and lien waivers. Because lien laws may differ, owners and lender should examine lien laws of the state in which the project is located before specifying these requirements. R.S.Mo. § 429.010, *et seq.* and K.S.A. § 60-1101, *et seq.* *See also Tharp v. Keeter/Schaefer Investment, L.P.*, 943 S.W.2d 811 (Mo. App. 1997) (holding that the release of lien rights for a progress payment does not include the release of rights to collect retainage withheld); R.S.Mo. § 429.005 (a contract clause waiving a mechanic's lien right is against public policy in Missouri and, therefore, unenforceable).

Before the contractor submits the first Application for Payment, however, the contractor must submit a Schedule of Values subject to the architect's approval. This schedule allocates portions of the contract price to designated work functions. The

architect then uses this schedule to scrutinize the applications as a check and balance system to front-end loading by the contractor (increased values placed on work at the beginning of the job) and advance payments prior to work being accomplished.

2. Payment Timing.

If possible, the parties should establish their own deadlines for the payment process. The AIA documents generally set forth suggested payment procedures, but they leave it up to the parties to insert particular dates for payment. The parties should always specify the deadlines for the payment process by filling in the blanks; however, in doing so, the parties must be mindful of any laws governing the timing of payment. For example, Kansas' proposed Senate Bill 333 which, if passed, will govern public construction projects, sets forth a requirement of payment of no later than 30 days after the owner receives an undisputed payment application.

Contractors should also consider the Prompt Payment Acts in both Missouri and Kansas, which establish limits on the amount of time that a contractor may withhold payment from the subcontractor once the contractor has been paid the amounts owed to the subcontractor by the owner. *See, e.g.,* K.S.A. § 16-1803 (requiring payment to the contractor within 30 days from the date following the owner's receipt of a timely, properly completed, undisputed request for payment; requiring that the subcontractor receive payment within seven business days from the contractor's receipt of payment from the owner [this Act applies to projects involving new construction of more than 4 units]); R.S.Mo. § 431.180 (requiring that payment to the subcontractor be timely made in accordance with the schedule for payments set forth in the parties' contract on projects involving new construction of more than 4 units).

B. Retainage.

Under most contracts, the owners retain a specified percentage from the progress payments until the end of the project which protects the owner in the event of a contractor breach or subcontractor liens. Retainage provides an incentive for the contractor to finish the work. Typical retainage amounts range from 5-10%.

Because contractors or subcontractors do not typically obtain retainage until the end of the project, this process essentially forces them to finance part of the work. Several states have sought to limit such inequities by imposing limitations on the amount of retainage, both in the public and private sector. R.S.Mo. § 436.300, *et seq.* (capping total retainage at 10% on Missouri private projects, allowing for substituted security, declaring retainage to be trust funds, mandating line item release of retainage and allowing for retainage of 150% of the value of punch list items); Missouri Public Works and Prompt Payment Act § 34.057(1) (allowing retainage of 200% of the value of a punch list item). *See also Epic, Inc. v. Kansas City, Mo.*, 37 S.W.3d 360 (Mo. App. 2001). In 2005, Kansas adopted the Kansas Fairness in Private Construction Act, K.S.A. § 16-1804, which allows an owner and, in turn, a contractor, on a private project to withhold up to 10% of retainage and which requires the contractor to pay the subcontractor its retainage within 7 business days from the date that the contractor receives retainage from the owner. Senate Bill 333 is currently being considered by the Kansas Legislature. If Senate Bill 333 passes, it would, among other things, limit the amount of retainage to 10% on public work's projects and will trigger additional interest if retainage is not timely paid.

Some contracts reduce or eliminate retainage as a certain portion of the work is completed. For example, if 50% or more of the work has been completed to the owner's satisfaction, the retainage may be reduced or eliminated completely. Other contracts

exempt certain parts of the billing from retainage, such as construction manager's fee, materials, general conditions, or the general contractor's own labor.

C. Third Party Roles.

To further complicate the construction contract process, the drafters must assess the third party roles of entities such as the architects and the lenders. The architect must have time to review the Application for Payment before approving it; the AIA form generally provides for seven days to do this. The lender's role also likely will impact the payment process because it may require lien waivers before any funds are released for progress payments. The lender may also want to independently verify work in place to insure the amount of the progress payment made is proper. Thus, additional time will likely be required to perform that function.

D. Interest on Late Payments.

The AIA documents provide an option of determining interest rates to be applied for late payments. A fair method is to use the interest rate that the owner is being charged on the construction loan for the project. By doing so, the owner would be discouraged from using the contractor as a financing source. In the absence of an interest provision, a default rate is provided by statute in both Missouri and Kansas. R.S.Mo. § 408.020 (9%); K.S.A. § 16-201 (10%).

E. Provisions for Billing Disputed Work.

Most construction contracts provide that any work disputed by the owner may not be billed. On the other hand, the owner may direct this work to be done through the process of a construction change directive with the amount to be paid for the work to be determined at a later time. The contractor may bill for this work up to the amount agreed to by the owner, which treats both parties fairly.

IV. Pay When Paid/Pay If Paid Clauses:

Payment clauses that seek to allocate payment risks tend to fall into either one of the following two categories:

1. Pay when paid clauses; and

2. Pay if paid clauses

Pay when paid clauses allow reasonable delay before the general contractor must pay the subcontractor.

Conversely, pay if paid clauses state that the general contractor's obligation to pay the subcontractor does not arise until the owner has paid the general contractor. That is, payment from the owner is a condition precedent to payment by the general contractor to the subcontractor. Courts will not view a clause as creating the latter category unless it explicitly states that the payment is a condition precedent. *See American Drilling Co. v. City of Springfield, Mo.*, 614 S.W.2d 266 (Mo. App. 1981); *Havens Steel Co. v. Randolph Engineering Co.*, 613 F. Supp. 514 (W.D. Mo. 1985). *But see* R.S.Mo. § 431.183 (contingent payment clauses do not prohibit the filing of a mechanic's lien); K.S.A. § 16-1803 (same).

The AIA documents have chosen a middle ground in attempting to assist the parties with avoiding any dispute regarding pay when paid/pay if paid clauses while attempting to protect the owner's interest. The AIA clause provides that the contractor promptly pays each subcontractor upon receipt of payment from the owner out of the amount that was paid to the contractor on account of that subcontractor's work. The clause is deliberately vague and states only what the prime contractor shall do if it is paid.

Some states have enacted prompt payment statutes for both public and private projects. Such statutes specify that after receiving payment, the contractor must pay the

subcontractor in a specified time. R.S.Mo. § 34.057.1 (Missouri Public Prompt Payment Act) and R.S.Mo. § 431.180 (Missouri Private Prompt Payment Act). *See also Vance Brothers, Inc. v. Obermiller Construction Services, Inc.*, No. WD62876, 2005 WL 147144 (Mo. App. January 25, 2005), *aff'd*, 2006 WL 44355 (Mo. January 10, 2006) (holding that the Private Prompt Payment Act applies only to contracts with periodic or scheduled payments); Missouri Senate Bill No. 800 (currently pending in the Missouri Legislature) to amend Section R.S.Mo § 431.180, to state that the Act applies to both lump sum and scheduled payment contracts. The Kansas Fairness in Private Construction Act, K.S.A. § 16-1802 *et seq.*, prohibits the waiver of a right to litigate, mechanic's lien rights and subrogation rights except in cases where there is wrap-up insurance; states that a pay when paid clause is not a defense to a bond claim or a mechanic's lien claim; states that an owner should pay a contractor within thirty days after receipt of an undisputed pay application; and, provides for payment to subcontractors within seven days after receipt of payment by the contractor from the owner (and an 18% interest penalty if not timely paid). The Kansas Act also allows contractors and subcontractors to suspend work if not timely paid and to receive a time extension and demobilization and remobilization costs for any delay. This provision excludes residential construction and public works. *See also* K.S.A. § 75-6401 and *D-1 Construction, Ltd. v. Unified School District No. 229,* 14 Kan. App.2d 245 (1990).

V. The Contractor's Design Responsibility:

A. Design Review.

Generally, construction projects are designed by architects or engineers, and built by the contractor who simply follows the plans and specifications. Every project involves details of construction that are not specified in the plans and specifications—that

is just the nature of construction. Nevertheless, most contractors know how those details should be completed. The situation can be complicated, however, with respect to certain types of work that are routinely designed by subcontractors specialized in the field, including mechanical, electrical and sprinkler systems, to name just a few. The contractor is generally responsible for following the plans and specifications and is liable for not conforming to them.

The contractor generally is not responsible for problems caused by the design and/or the design team. If the design is found to be defective, then the contractor typically bears no responsibility; the contractor may be entitled to extra compensation for any loss that it incurs because of the design problem. Some owners may seek to shift this allocation of responsibility back to the contractor by imposing a duty on the contractor to review the plans and specifications and attempt to discover design errors and inconsistencies before starting work. Contractors should resist this shifting process by arguing that architects (or engineers) have more time and skill, and are charged with the responsibility, to prepare the design, and it is unfair to shift that burden to a contractor who has limited time or skills to review and understand the design during the bidding phase. These types of liability-shifting provisions are often found in supplementary conditions or in amendments to the standard form General Conditions, and they must carefully be considered prior to agreeing to the contract.

B. Shop Drawing Review.

Contractors are typically required to provide shop drawings with respect to how they plan to supply the details of the design that are not specified in the contract documents. These designs are shown on shop drawings prepared by each subcontractor, and they illustrate how the subcontractor will handle its part of the work. Generally,

these documents are submitted to the designer through the general contractor for review and a stamp of approval.

Many disputes arise from the shop drawing process. Architects and engineers attempt to avoid responsibility for the sufficiency of the detail in the shop drawings by reviewing and/or stamping them only for general conformity with the project design, while disclaiming any assurance that they are proper and will meet the intent of the contract documents. Subcontractors and contractors, on the other hand, argue that review and acceptance of their shop drawings gives the drawings the same legal effect as the original contract documents, such that they can be relied on by the contractor. Subcontractors and contractors typically also argue that approved or stamped shop drawings are the fault of the reviewing design professional if they prove to be incorrect or defective.

Disputes also arise from the speed of the shop drawing process. Time is important and costly on a project, and the parties must be attentive to the length of the process of shop drawing submittal, review and return. This process may severely impact the contractor's ability to meet the owner's schedule provided in the contract documents. Documentation is very important in those instances where the contractor or subcontractor is waiting on a submittal review that is delaying its work at the project.

VI. Differing Site Conditions:

One of the biggest challenges to cost estimating in advance of any work being performed by the contractor is estimating the costs associated with constructing those areas that are not visible. It is not uncommon for a contractor to encounter a physical condition, usually subsurface, that was not anticipated by the parties at the time of the contract. Examples are underground rock, water, obstructions such as buried fuel tanks,

buried foundation structures, utilities, fiber optics, etc. These add to the cost of completing the work. Often these unanticipated physical site conditions, or "differing site conditions", provide grounds for construction claims. Note, however, differing site conditions typically do not provide a basis for deeming the contract null and void or for arguing that there was no meeting of the minds at the time of contracting.

A. Type I Claims.

The Type I differing site condition exists when subsurface or latent (non-obvious) physical conditions at the site differ materially from those indicated in the contract. As noted above, these could be rock, water, underground utilities, etc. In order for a contractor to recover increased costs associated with these types of conditions, the contractor must prove the following facts: First, the contractor must show that the contract actually indicates the subsurface condition that forms the basis of the contractor's claim. It is important that the documents say something about the condition in order for there to be a misrepresentation. Second, the contractor must demonstrate that it relied on such indications and that the contractor's interpretation of the contract and the indication was reasonable. Third, the contractor must demonstrate that the conditions encountered were materially or substantially different from those conditions indicated in the contract and that they were not reasonably foreseeable. Again, it is important that the documents indicate something about the conditions so that a difference can be measured. Finally, the contractor must show that the damages claimed are directly attributable to the unforeseen conditions and not the contractor's own lack of a proper bid, inefficient operations, etc.

B. Type II Claims.

Where a contract fails to indicate a subsurface or latent condition altogether, a contractor still may be entitled to claim extra monies for encountering differing site conditions. Under a Type II claim, the contractor may assert that it encountered a condition that differed from conditions usually found on similar projects. A Type II claim is not concerned with the precise representation that was made in the contract documents or the difference that was found on the site. Rather, a Type II claim is concerned with what is usual and normal for the type of work involved and what is different from that about the particular site. In order for the contractor to recover, the contract must be silent on the subsurface or latent condition that forms the basis of the claim.

However, the absence of contract language regarding conditions makes the contractor's proof of a Type II claim more difficult. Recovery on a Type II claim requires both a subjective and objective inquiry. The contractor must first establish the type of conditions that would normally be encountered on a similar project. The contractor must then show the conditions that were actually encountered and prove that those conditions differed materially or substantially from the physical conditions that would ordinarily be encountered at a similar project. Finally, the contractor must show that the conditions caused an increase in the cost of performance and that increase was not attributable to the contractor.

The AIA documents provide for a standard changed condition clause in the General Conditions. AIA document A201. Section 4.3.4 of A201 defines the type of differing site conditions described above, while Section 4.3.6 provides the remedy for the contractor who encounters the condition. The AIA General Conditions also require that

the contractor notify the owner, who, in turn, investigates the encountered conditions and determines whether the conditions differ materially and whether the conditions actually caused the contractor to incur additional costs.

C. Exculpatory Clauses.

In addition to standard contract clauses governing differing site conditions, a contract may also include clauses that absolve a party from any liability for a changed or unforeseen condition, or even deficient plans and specifications.

1. Pre-bid Inspection.

Many contracts include a clause requiring the contractor to examine the construction site before submitting a bid on the project. This type of clause is typically included in the contract in order to shift some of the risk from the owner on to the contractor. A pre-bid inspection clause usually requires that any condition that "should have been seen" by the contractor during a pre-bid inspection will be deemed disclosed and, therefore, not the subject of a claim.

2. Duty to Discover Obvious Errors.

It is also common to include a clause that requires the contractor to examine the contract documents and discover any patent or obvious errors. Such a clause may also require the contractor to discover conflicting provisions or ambiguities and notify the owner of the same so that the owner can clarify such ambiguities by addendum before the bids are opened. Like the pre-bid inspection clause, the duty to discover patent errors clause shifts some of the risk of loss from the owner back to the contractor. Generally, a contractor is bound only to "discover" those ambiguities and errors a reasonably prudent contractor would find. There is no duty to perform a plan review. The intent generally is for the contractor to report what is otherwise found and not remain silent on those issues.

3. No Damages for Delay Clause.

Today many construction contracts also contain a "No Damages for Delay" clause regarding the contractor's right to adjust the contract price for encountering differing site conditions. The presence of a no damages for delay clause can have an effect on a contractor that encounters either a Type I or Type II differing site condition. Often times encountering these types of conditions not only involves the cost of removing them or dealing with them directly, but, it may also impact the schedule for the project. In a case where the schedule is impacted, the contractor may only be entitled to additional time to complete the work but not an equitable adjustment for the delays and impact on the contractor's general conditions and overhead. Missouri generally recognizes the effectiveness of such a clause in the private setting, *Roy A. Elam Masonry, Inc. v. Fru-Con Construction Corp.*, 922 S.W.2d 783 (Mo. App. 1996); but not in the public setting where the law provides that they are void as against public policy, except for contracts with the Missouri Department of Transportation. *See* R.S.Mo. § 34.058. At least one case in Kansas, *Peter Kiewit & Sons v. State Highway Commission,* 184 Kan. 737, 339 P.2d 267 (1959), implies that a no damages for delay such a clause would be construed strictly against the drafter.

D. Handling Changed Conditions.

For owners it is important to disclose all that is known about the conditions on the project and to give the contractor access to all prior drawings. Owners should also use standard clauses, as any ambiguities will be construed against the drafter. An owner should pay close attention to the bidder's questions and disclose any information in the owner's possession in response to those questions. An owner should also respond

promptly to any notice by the contractor of a differing site condition and investigate the alleged condition as required by most differing site condition clauses.

Contractors, on the other hand, should ask for and pay careful attention to existing drawings. They should also attend pre-bid inspections and ask questions at those meetings. It is also important for the contractor to keep careful cost records where possible, and to maintain joint cost records with the owner if feasible. Contractors should give prompt notice of any differing site conditions encountered on the project, as well as errors and ambiguities in the plans and specifications.

VII. Dispute Resolution or Similar Clauses:

Having a pre-agreed procedure to resolve disputes and claims on the project is vital to any construction contracts. Most construction contracts employ a process by which claims and disputes are first heard and decided by the design professional. If necessary, a dispute may proceed to mediation and conclude in arbitration or a lawsuit. Often this approach is the best process, but not always. Owners and contractors should consider a number of factors in making a decision about how their disputes should be resolved. Some of these factors include the project size, the complexity of the project, the number of parties involved, the complexity of contractual relationships, the risk to both the owner and the contractor, and the length of construction. It may be that the three tiered approach is inefficient or that litigating disputes may be more appropriate than arbitration.

It is often said that arbitration is faster and cheaper than litigation, but that is not always true, particularly in complicated construction cases. Arbitration may, however, insure that disputes which are very technical in nature are heard by parties who are trained to hear and decide such technicalities in light of the applicable facts and law.

Unless parties agree contractually, or unless it is allowed by the governing arbitration rules, joinder of parties or multi-party arbitrations may be precluded in many jurisdictions and under many contracts. Yet at the same time those jurisdictions may allow consolidation or joinder of parties in court litigation. Therefore, if the nature of the project likely may involve disputes between more than two parties, it is important to consider whether the parties would prefer that the dispute resolution process allow for joinder and consolidation of parties and claims. Often times a construction contract might indicate that proceeding in court is the appropriate venue, but proceeding in arbitration likewise can be appropriate if all of the contract documents among the owner, designer, contractor and subcontractor provide for consolidation and joinder.

Also, discovery in arbitration is limited, and it is intended to be a more streamlined process. If significant discovery is necessary, consideration should be given to another dispute resolution process. The subpoena power of arbitration panels is usually limited to requiring the production of documents or witnesses at a hearing; but if discovery is necessary from third parties not in privity, it may be difficult to secure that discovery pre-hearing.

The 1997 edition of the AIA construction documents contains an arbitration provision in the General Conditions (AIA A201). However, whether or not you utilize a form contract there are necessary elements to be considered in crafting an arbitration provision including the following:

1. All claims must be put in writing and be addressed to a previously identified individual.

2. Parties must make claims within a finite period of time from the discovery of the claim.

3. Parties must continue performing other obligations under the contract documents notwithstanding the fact that claims are being made.

4. Parties must commence mediation within a finite period of time from when the claim is submitted to the design professional.

5. Parties must file arbitration demands within a finite period of time from that same benchmark.

6. Parties must designate an applicable set of rules (or a jurisdiction) as well as the location for both the mediation and the arbitration.

VIII. Liquidated Damages:

Time is money in construction. An owner may suffer significant losses when a project is delivered late. Major disputes arise with respect to an owner's losses for late delivery. To address these issues, owners frequently use liquidated damage clauses in construction contracts. These clauses almost always work by assigning a daily charge for substantial completion of the work later than the scheduled date. Often in public contracts the daily charge will go beyond substantial completion to final completion.

A. Enforceability of Liquidated Damages Clauses.

The standard rule of law is that the courts will enforce liquidated damages as long as the clause does not constitute a penalty. *See, e.g., Standard Improvement Co. v. DiGiovanni*, 768 S.W.2d 190 (Mo. App. 1989). The courts will generally find that to be the case only when an owner is not suffering any damages at all from the passage of time. Nonetheless, when liquidated damages are grossly disproportionate to the owner's actual damages, courts or arbitrators may intervene and refuse to enforce them. *See Goldberg v. Charles Chevrolet, Inc.*, 672 S.W.2d 177 (Mo. App. 1984). An owner can avoid this risk by a few simple considerations. First, the owner can avoid the use of the word "penalty"

in referring to these types of damages in a contract. Second, if the damage figure seems a bit high, the owner should include in the contract language explaining the importance of prompt completion and the serious nature of the harm from late completion and explaining specifically the types of damages that will be suffered. Third, the owner can bolster the enforceability of a liquidated damage clause by offering an early completion bonus to the contractor.

1. Elements of Liquidated Damages.

The liquidated damage sum should be a combination of the lost profits from late completion and administrative expenses from continued oversight of the project coupled with the cost of disruption to move into the project. In the public and not-for-profit sector, calculating the damage can pose a challenge. Loss of revenue may be the critical factor for a highway or bridge project. One approach may be to take the daily interest cost or the capital cost of the project as of the completion. Another approach might be to evaluate the cost based upon the value that the project is intended to ultimately provide the user. There really is no simple solution.

Another approach for liquidated damages is to have a step liquidated damages by which the daily rate rises after a certain point. For example, an owner may charge one price for a major delay and another price for a minor delay. This approach may allow the owner to avoid appearing punitive. The owner may also assess one charge for failing to meet a substantial completion date and another rate for failing to meet a final completion date at a reduced rate.

IX. Delays and Extension of Time:

Every construction project has a schedule that determines in advance the sequence of work. For the owner, a schedule provides the answer to the owner's number one concern: When will the project be finished?

The contract documents dictate which party is responsible for the delay and whether the contractor is entitled to an extension of time or for reimbursement of costs incurred as a result of the delay.

A. Types of Delays.

1. Nonexcusable Delay.

Generally, nonexcusable delays are those delays caused by or within the control of the contractor or his subcontractors. Examples of nonexcusable delays include equipment problems, slow work, poor management, poor coordination, lack of manpower, lack of equipment, etc. In such a case, the contractor bears all the responsibility for the delay and will not be entitled to any additional time on the schedule or monetary compensation for the cost of the delay to the contractor.

2. Excusable Delay.

Excusable delay, on the other hand, is the type of delay that falls outside of the control of either party. This type of delay may involve labor disputes, severe weather, national shortage of materials, etc. The owner is required to give the contractor additional time to finish the project but may not necessarily be required to pay the contractor any money since neither the owner nor the contractor had any control over the event.

In some cases the owner may require the contractor to finish the contract by the original scheduled date even though an excusable delay appears. When this happens, the

owner has "accelerated" the work and may have to pay the contractor for any costs incurred as a result of such acceleration. Often these costs are substantial because acceleration requires additional crews, overtime, double shifts, accelerated material deliveries, etc. "Escalation" costs are somewhat related and typically result from a schedule shift where completion is delayed by the owner beyond the original completion date and the contractor suffers increased costs due to escalation in labor and material or equipment costs.

3. Compensable Delays.

As noted, not all excusable delays are compensable. Compensable delays are those delays for which the owner bears responsibility and must give the contractor not only additional time, but additional money. Examples of compensable delays may be design changes, errors that slow down the progress of the work, interference with site access not anticipated by the contractor, excessive change orders, failure by the owner to secure necessary building permits, or delayed decision making by the owner resulting in work delays.

4. Concurrent Delays.

Occasionally, two different types of delays will overlap on a particular project. Such occurrences are commonly referred to as concurrent delays. The parties must independently identify and evaluate these delays. If the delays would cause the project to be delayed for a similar or the same period of time, the delays are considered to be concurrent. It is not easy to apportion responsibility in situations involving concurrent delays. One established rule, however, is that where a compensable delay for the contractor is concurrent with a non-excusable delay, the period of delay is reclassified as excusable. For example, where an owner-related design change delay may overlap with

the contractor's lack of equipment to perform the work in any event. Thus, the contractor may receive additional time to complete the work but will not be compensated for the costs incurred as a result of the delay. If the concurrent delays can be "allocated" in time to the owner and/or the contractor, then the contractor may only receive extensions for that portion of the owner delay which exceeds the contractor's own delay.

X. Indemnification and Insurance:

Generally there are three types of indemnification clauses that are typically included in a construction contract. The first is often called the "board form" indemnification clause where the indemnitor accepts all risk of loss even if the indemnitee is 100% responsible. Early cases found these types of clauses unenforceable unless expressly stated. More recently, additional limitations are being placed. For example, in Missouri it is against public policy to insert such a clause into a contract, and such clauses are generally not enforceable unless insurance is in place to cover the risk. The risk is limited to the insurance and the cost of the insurance is paid for in the contract. *See* R.S.Mo. § 434.100. *See also* Kansas Special Committee on Judiciary Senate Bill (2006) regarding indemnification provisions in construction contracts in Kansas providing that an indemnification provision requiring an indemnitor to indemnify the indemnitee for his own negligence would be void against public policy. This would be true without regard to any insurance provisions.

The second type of indemnification provision that may be found is called "intermediate form" where the indemnitor takes all risk unless the indemnitee is 100% responsible. This is a shared risk concept involving comparative fault. *See Dillard v. Shaughnessy Fickel and Scott Architects, Inc.,* 884 S.W.2d 723 (Mo.App. 1994).

The third form of indemnity is called the "limited form". In that instance, the indemnitee takes risk only for its own negligence. *See* R.S.Mo. § 434.100.

As noted, insurance often fills gaps left by indemnity. Moreover, insurance provides an incentive to the indemnitor to assume indemnity obligations since it can insure them and pass the costs associated therewith back to the indemnitee, who is usually the owner.

When drafting contract provisions that involve indemnity and require a party to obtain insurance, it is also important to require inclusion of the indemnitee in that policy as an additional insured. The most common document requested to insure that a party has been included as an additional insured is a Certificate of Insurance. These are commonly given on construction projects. However, Certificates of Insurance are not policies of insurance; rather, they are only informational documents. Without an express amendment to the policy adding the indemnitee as an additional insured, there may very well not be coverage. Also, it is important to require that the policy may continue on without interruption until completion of the work. Many policies also have completed operations coverage and it is important to deal with that issue and make sure that it is retained for some reasonable period of time. Finally, it is important to require notice of cancellation of any policies to assure that the risk remains insured.

XI. Notice of Claim Requirements:

Most construction contracts require parties who are asserting a claim to provide prompt notice to the other party of that claim. The AIA documents contain many sophisticated schemes of notice, most of which apply when a contractor encounters a field condition that will delay the work or cause cost overruns. The typical clause requires notice of a claim within a certain number of days of the time the claimant learns

of the facts leading to the claim and in any event prior to the date on which the claimant begins to expend extra funds for which it will seek compensation.

There are several reasons for inclusion of notice of claim requirements, including:

1. Notice of a claim gives the recipient an opportunity to gather information relating to the claim before it is lost. Notice permits the parties to measure, photograph, or sample the buried structure or the rock that the claimant claims will lead to the additional cost. If the recipient of a claim is not given notice, the claimant may remove the rock or the structure before the recipient has the chance to preserve evidence that may very well govern entitlement to the claim.

2. Notice may enable the parties to reach an agreement regarding the amount of the loss and the claim after prompt investigation and thus avoid further claims and litigation.

3. The notice requirements may help assess whether the claim is genuine. Recipients of claims often believe that once the claimant completes the project and discovers that the project lost money, the claimant begins asserting claims in an attempt to recoup that loss. Requiring and providing prompt notice at the time of the event in question helps avoid afterthoughts and these negative inferences or assumptions.

4. The recipients of the claims have to manage and budget their construction project and make decisions based on information available to them. If the recipient does not learn until late in the job that there will be cost overruns, it has less ability to arrange financing, manage the budget, make alterations or changes in the project design, or exert other efforts to save the money that may be needed to cover the claim.

Often claimants seek to circumvent notice requirements by arguing that it would be inequitable to enforce technical requirements of a notice clause where the purpose of

the clause, in fact, has been met; such as where minutes of job meetings confirm actual discussions and consideration of a potential claim. In effect, the claimant will argue that that the recipient has "actual notice" of its claim. However, merely showing that the recipient had knowledge of the field condition at issue may not prove compliance with the notice clause. For example, if a recipient is aware that the contractor has encountered an underground condition that is slowing the progress of the work or is costing extra money to remove, then that does not necessarily mean the recipient understands that the contractor considers it to be an owner-related problem for which the recipient is to pay the claimant extra costs.

This distinction is important because if the contractor plans to effectively spend the owner's money, the owner is entitled to give direction on whether and how to proceed, how much to spend, modification of any design issues, dictation of means and methods, etc.

XII. Termination Clauses:

A. Termination for Convenience.

Termination for Convenience clauses allow an owner to cancel a project after the construction contract has been executed, for any reason. This usually only happens when something very dramatic occurs on the project; for instance, the owner looses all of its financing, the owner is having financial problems, permits to do the work are not issued or are withdrawn, etc.

These clauses generally provide that an owner must pay the contractor its actual costs up to the point of notice of termination for convenience. The contractor may also receive demobilization costs. If any overhead costs have not been recovered through billings for the work performed to date, the contractor may seek to be compensated. On

occasion, the parties provide for the payment of lost profits on the unperformed portion of the work although owners generally resist any obligation to pay lost profits for work not performed.

B. Termination for Cause by the Owner.

The AIA form A201 contains a basic clause concerning owner termination for cause and provides that the owner may terminate the contract if the contractor persistently fails or refuses to supply properly skilled workers and materials, fails to pay its bills to subcontractors and suppliers, persistently disregards applicable laws, ordinances or rules, or is otherwise guilty of any substantial breach of the contract which is nothing more than a "catch-all" phrase which might include failure to provide insurance, bonding, or other technical requirements.

The AIA scheme requires that the architect (or the design professional appointed to fill that role for the project) certify that the cause exists, and then owner may, without prejudice to other rights and remedies, terminate the contractor after providing further written notice (typically seven days). These provisions are often negotiated to provide multiple notices or to extend the notice time and to give rights to cure. If the cost to complete the work exceeds the unpaid balance of the contract sum, which is almost always the case, the contractor is responsible for the amounts over and above the contract sum. It is helpful to add a provision that the surety, by issuance of its bond, agrees to likewise be held responsible.

C. Termination for Cause by the Contractor.

Contractors seldom wish to terminate contracts. However, in some instances job conditions may be so unbearable that a contractor decides to take that dramatic action of terminating the contract for cause. Contractors typically may terminate if the owner fails

to make payment for thirty days or if the architect fails to recommend payment for thirty days, through no fault of the contractor. The AIA contracts require that the contractor provide seven days written notice to the owner and the architect prior to terminating the contract. However, a procedure preferable to termination for cause by the contractor is to follow any procedures in the contract for alternative dispute resolution. For example, a contract may provide for mediation or arbitration during the course of the work on an accelerated track. These provisions should be included in the contract and taken advantage of to avoid a contractor leaving the project.

Experience and case law dictates that any time a contractor leaves a project prior to its completion, no matter what the reasons, that contractor's actions will be looked on unfavorably except in the most extreme of circumstances.

XIII. Incorporation by Reference and Flow Down Clauses:

Incorporation by reference and flow down clauses are generally found at the beginning of any written contract and they typically provide that various other documents and writings referred to in the contract are incorporated into the contract as if fully set forth therein, and that those referenced documents become part of the terms and provisions of the contract between the parties. Incorporation by reference provisions are enforceable. *See, e.g., State ex rel. Union Indemnity Co. v. Shain*, 66 S.W.2d 102 (Mo. 1933). Generally it is not necessary to attach the incorporated documents to the contract being signed, *Wasson v. Schubert*, 964 S.W.2d 520 (Mo. App. 1998); *Dillard v. Shaughnessy Fickel and Scott Architects*, 943 S.W.2d 711 (Mo.App. 1997), however, it is always good practice to do so. Even so, some cases have indicated that it is not even necessary that the documents exist at the time. For example, plans or specifications that

have not yet been developed fully for distribution and construction but which have been otherwise identified. *See, e.g., Wasson v. Schubert supra*.

One of the most significant issues with respect to documents incorporated by reference, particularly for subcontractors, is that general contractors are reluctant, in most instances, to provide copies of those documents in full to the subcontractor. It is rare that a general contractor will allow the subcontractor to view his price, schedule, or cost breakdown. Subcontractors should be keenly aware of this difficulty and insist on seeing any documents to which the contractor intends to hold them.

The flow down clause, on the other hand, is a simple clause which provides that; for example, the subcontractor shall assume to the general contractor all obligations which the general contractor assumes to the owner with respect to the subcontractor's scope of work. Likewise, these clauses generally provide that the liabilities will flow the same way. *Air Cooling & Energy, Inc. v. Midwestern Construction Company of Missouri, Inc.*, 602 S.W.2d 920 (Mo. App. 1980).

Often there is a dispute between subcontractors and contractors about which clauses, terms, provisions and conditions flow down. For example, do only terms and conditions regarding the subcontractor's scope of work flow down or do all conditions flow down including terms and conditions contained in the general and supplementary provisions regarding insurance, bonding, dispute resolution, notices of claim, alternative dispute resolution, etc.? *See, e.g., Jim Carlson Construction, Inc. v. Barley*, 769 S.W.2d 480 (Mo. App. 1989) (providing that an arbitration clause is incorporated into a subcontract through incorporation of the contractor's general conditions with the owner). *But see Metro Demolition & Excavating Co. v. HBD Contracting, Inc.*, 37 S.W.3d 843 (Mo. App. 2001) (holding that arbitration cannot be incorporated into a subcontract by

reference; but reaching that conclusion apparently because the general contract did not exist at the time when the subcontract was signed). This logic may conflict or run afoul of the logic in *Wasson v. Schubert supra*, and *Dillard v. Shaughnessy Fickel and Scott Architects supra*. Therefore, close attention to these kinds of provisions should be paid by the drafter.

As a general proposition, however, to the extent that there is conflict between the provisions of the subcontract and the general contract, most courts will hold that the more specific provisions of the subcontract prevail over provisions of the general contract or the provisions of documents incorporated by reference into the general contract.

Heather F. Shore, Esq.
911 Main Street, Suite 2300
Kansas City, MO 64105-5319
Phone: 816-292-7000
hshore@browndunn.com
www.browndunn.com

The Fundamentals Of Construction Contracts: Understanding The Issues

Prepared and Presented by:

Heather F. Shore
Brown & Dunn, P.C.

THE FUNDAMENTALS OF CONSTRUCTION CONTRACTS: *UNDERSTANDING THE ISSUES*

I. Review of Basic Contract Principles:

A. Contracts.

1. Definitions.

A contract can be defined as an agreement made upon sufficient consideration either to do, or to refrain from doing, a particular lawful act. A contract has been defined as an agreement, obligation, or legal tie by which a party binds itself, or becomes bound, expressly or impliedly, to pay a sum of money or to perform or omit to do some certain act or thing. Also, a contract has been variously defined as a private, voluntary allocation by which two or more parties distribute specific entitlements and obligations. Another definition is a promise or a set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty. A contract is not a law, nor does it make law. It is an agreement plus the law that makes the ordinary contract an enforceable obligation.

2. Contract Types.

There are two basic types of contracts; express and implied. An express contract may be either oral or in writing. An implied contract, on the other hand, may be implied in fact, by the words and conduct of the parties; or implied in law. An implied in law contract is one made for the parties by the courts to assure that one party to an obligation receives what his actions merit and the other party to the obligation is not unjustly enriched.

3. The Five Requirements of a Valid Contract.

(a) The Necessary Elements.

The elements of a valid contract have been variously stated by courts at different times as: (1) parties competent to contract, (2) a proper or lawful subject matter, (3) the exchange of consideration, (4) the mutuality of agreement or assent on both sides, and (5) the mutuality of obligation.

A contract is made at the time the last act necessary to its formation is done. It is usually completed at the place where the offer is accepted. Thus, if a contract is made by telephone, it is made where the acceptor speaks. While the existence of a contract is question of fact, whether a certain or undisputed state of facts establishes a contract is a question of law for the courts.

(b) Competent Parties and Lawful Subject Matter.

To form a contract it is necessary that there is a party capable of contracting and a party capable of being contracted with on the other side. In other words, to enter into a valid, legal agreement, the parties must have the capacity to do so. No one can be bound by a contract who does not have legal capacity to incur at least voidable contractual duties. Each case involving competency to contract must be decided on its own facts. *Brown v. United Missouri Bank, N.A.*, 78 F.3d 382 (8th Cir. 1996) (applying Missouri law).

(c) Consideration.

No contract will exist without sufficient consideration. Consideration may be a benefit to the promisor or a loss or detriment to the promisee. It may take the form of a

right, an interest, or profit accruing to one party, or some forbearance, detriment, or responsibility given, suffered, or undertaken by the other party. It may also consist of the creation, modification, or destruction of a legal relationship. Consideration is, in effect, the price of the bargain and the price paid for a promise. It is something given in exchange for a promise. Consideration is what distinguishes a contract from a gift.

(d) Mutual Assent.

There must be mutual assent or a meeting of the minds on all negotiated terms between the parties and on all the essential elements in terms of the contract to form a binding contract. *Dougan v. Rossville Drainage District*, 270 Kan. 468, 15 P.3d 338 (2000). In some jurisdictions, the parties must also have a present intent to be bound by their agreements. It is not necessary that the assent of both parties be given at the same time. Also, it is not necessary that communication of the assent be simultaneous. The omission of a material element from a contract renders the contract unenforceable because there has been no meeting of the minds of the parties. A valid contract requires a manifestation of mutual assent to the bargained for exchange.

For example, a subcontractor may supply pricing to a general contractor for the general contractors' bid to the owner. The general contractor then advises the subcontractor that he is the low bidder. The general contractor asks for a bond and a liquidated damage provision. The subcontractor attends the preconstruction conference, submits a schedule of values and obtains an insurance certificate. However, he does not start work. The general contractor and subcontractor thereafter cannot agree on whether the subcontractor will provide a bond or agree to a liquidated damage provision. One might argue that these are material elements to the contract and, therefore, no agreement

has been formed.

4. The Requirements of Offer and Acceptance.

(a) Offer.

A valid offer identifies the bargained for exchange between the parties and creates a power of acceptance in the party to whom the offer is made. The formation of a contract generally requires both an offer and an acceptance. *Hyken v. Travelers Insurance Co.*, 678 S.W.2d 454 (Mo. App. 1984). However, the words used by parties in negotiating for a contract derive their primary importance from the standpoint of whether they express and achieve mutual assent, rather than whether they constitute an offer and acceptance. Although manifestation of mutual assent to an exchange ordinarily takes the form an offer or proposal by one party followed by an acceptance by the other party, a manifestation of mutual assent may be made even though neither offer nor acceptance can be identified and even though the moment of formation of the contract cannot be determined.

(i) Price Quotes.

Whether a communication naming a price is a quotation or an offer to contract depends upon the intention of the owner as it is manifested by the facts and circumstances of each particular case. Generally, a price quotation or proposal is not an offer to contract, but is an invitation to enter into negotiations or a preliminary solicitation of an offer. *Nordyne, Inc. v. International Controls & Measurements Corp.*, 262 F.3d 843 (8th Cir. 2001) (applying Missouri law). However, a price quotation, if detailed enough, can amount to an offer to contract creating the power of acceptance in the person to whom it is offered, if it reasonable appears from the price quotation that assent to the quote is all

assent to the quote is all that is needed to ripen the offer into a contract. *Nordyne, Inc. supra.* Factors that are relevant in determining whether a price quotation is an offer include the extent of prior inquiry, the completeness of the terms of the suggested bargain, and the number of persons to whom the price quotation is communicated. *Nordyne, Inc. supra.*

(b) Acceptance.

To constitute a contract there must be an acceptance of the offer as noted above. Until the offer is accepted, both parties have not assented to the terms and, therefore, there is no mutual assent. In language used often by the courts, their minds have not met or there is no meeting of the minds.

Acceptance is defined as a manifestation of assent to the term so the offer made by the offeree in a manner invited or required by the offer. Whether an offer has been accepted is a question of fact. The effect of acceptance is to convert the offer into a binding contract. *Tebeau v. Ridge*, 261 Mo. 547, 170 S.W. 871 (1914).

(c) Delivery.

Delivery is ordinarily essential to the validity and operation of a contract. However, neither manual transfer nor any particular form of ceremony is necessary to constitute good delivery, which may be by acts without words, words without acts, or by both words and acts. *Wilkie v. Elmore*, 395 S.W.2d 168 (Mo. 1965). Although physical delivery is frequently the only method by which acceptance is to be expressed, it is not an absolute necessity unless so intended by the parties. If the parties understand that the contract has been executed and is in operation, it will be considered as delivery. In the absence of direct evidence, the delivery of a contract is presumed where the concurrent

acts of the parties recognize the contract's obligations. Delivery of a contract is largely a matter of intention of the parties, and such delivery may be actual or constructive.

5. Formal Requisites.

(a) Oral Contracts.

An oral contract is ordinarily no less binding than one that is reduced to writing. However, a statute may require certain contracts to be in writing, and an oral or parol contract is unenforceable where a statute so requires.

(b) Written Contracts.

The principal statute that is raised in this connection is the "statute of frauds". This statute applies to contracts specified within the statute which are required to be in writing and, absent a writing, are found not to exist. For example, Section 432.010, *et seq.*, R.S.Mo. (assignment of wages and certain leases); and Section 400.2-201, R.S.Mo. (sale of goods for greater than $500.00); and K.S.A. § 33-101, *et seq.* (i.e., land leases exceeding one year in length); and K.S.A. § 84-2-201 (sale of goods over $500.00).

Where the parties indicate a definite intention not to be bound until a written agreement has been made, such an agreement will be a prerequisite to the formation of a contract. Except for some contracts, the form of which may be closely regulated by statute, no particular form is necessary to create a promise or covenant and all that is essential that from a fair interpretation of the language, it appears that the parties have agreed to do or refrain from doing certain acts in question.

(c) Multiple Writings.

A contract may be stated upon several different writings which are construed together. Indeed, a complete contract may be gathered from letters, writings, telegrams,

and, presumably, e-mails between the parties, where they in fact relate to the subject matter of the contract and are so connected with each other that they may be fairly said to constitute one document relating to the contract.

(d) Partly Written and Partly Oral Contracts.

In the absence of statute requiring that a contract be in writing or evidenced by a writing, a valid contract may be partly written and partly oral. A verbal acceptance of a written offer will form a valid contract that is partly written and partly oral. The rule that all preliminary negotiations and agreements are to be deemed merged into the final settled instrument executed by the parties does not prevent a contract from being partly oral and partly in writing. This rule does not apply, however, where is appears from an inspection of the documents themselves that it was intended to express the full and complete agreement and intention of the parties.

6. Definiteness and Certainty.

To be enforceable, an agreement or contract must be "definite and certain" as to its terms and requirements. Or, on the other hand, it must contain provisions which are capable in themselves of being reduced to certainty, even if there are some formal imperfections in the contract. To have a valid contract, all terms should be definitely agreed upon, and the failure to agree to even one essential term means there is no agreement to be enforced. The test for the enforceability of an agreement is whether both parties have manifested an intention to be bound by its terms and whether the terms are sufficiently definite to be specifically enforced by a court. However, an agreement to the essential terms of a contract does not mean that the terms must be set out in the plainest language. It does not follow that parties must share identical, subjective, opinions as to

the meaning of the terms.

Generally, an agreement to agree is unenforceable. This is because its terms are so indefinite that it fails to show a mutual intent to create an enforceable obligation. The parties' obligations must be identified so that the adequacy of performance can be ascertained. Letter of intent, for example, often run afoul of this rule.

An agreement will be rendered unenforceable if its terms are not reasonably certain. The trier of fact determines whether an agreement has been made and what the terms of the agreement are. Ambiguity will exist if a contract is reasonably susceptible of more than one meaning. No enforceable contract comes into being when parties leave a material term for future negotiation, creating a mere agreement to agree. However, it is not required that all terms of agreement be precisely specified, and the presence of undefined and unspecified terms will not necessarily preclude the formation of a binding contract. In determining whether the mistake has a material effect on the agreed exchange of performances, account is taken of any relief by way of reformation, restitution, or otherwise.

More simply stated, to be binding, a contract must generally be sufficiently definite to permit a determination by a court of a breach and the application of a remedy.

Mutual expressions of agreement may fail to consummate a contract for the reason that they are not complete, due to some essential term or terms not being agreed upon. *Wilkinson v. Shoney's, Inc.*, 269 Kan. 194, 4 P.3d 1149 (2000). However, even if a contract is ambiguous, it should not be held void for uncertainty if there is a possibility of giving meaning to the agreement. *Lindsey v. Jewels by Park Lane, Inc.*, 205 F.3d 1087 (8th Cir. 2000). Once a trial court determines that a contract is ambiguous, it is for a jury

to determine the true meaning of the contract terms.

7. Ambiguities.

If the terms are not definite and certain, then an ambiguity exists in the contract. In such case, the court will gather, if possible, the intention of the parties from the contract as a whole or as often stated, from the "four corners" of the contract. Accordingly, the fundamental and cardinal rule in the construction or interpretation of a contract is that the intention of the parties is to be ascertained by the fact finder. *Liggatt v. Employers Mutual Casualty Co.*, 273 Kan. 915, 46 P.3d 1120 (2002), and *Berman v. Berman*, 701 S.W.2d 781 (Mo. App. 1985). Effect is to be given to by the fact finder to that intention if it can be done consistently with legal principles. *McBride Electric, Inc. v. Putt's Tuff, Inc.*, 9 Kan. App.2d 548, 685 P.2d 316 (1984); *Berman supra.* If only one reasonable meaning can be ascribed to the contract when viewed in context, that meaning necessarily reflects the parties' intent. To determine the intentions of the parties to a contract, the court will look not only to the written contract, but also to any extrinsic evidence regarding the parties' intent at the time the contract was made.

If the language used by the parties is plain, complete and unambiguous, the intention of the parties must be gathered from that language, and from that language alone. *Liggatt supra,* and *Needles v. Kansas City*, 371 S.W.2d 300 (Mo. 1963). This is true no matter what the actual or secret intentions of the parties may have been. Presumptively, the intent of the parties to a contract is expressed by the natural and ordinary meaning of the language used, and such meaning cannot be perverted or destroyed by the courts through construction for the parties are presumed to have intended what the terms say. Only when the contract language is ambiguous may a court

turn to extrinsic evidence of the contracting parties' intent.

8. Mistakes Between the Parties.

In general, a mistake can be defined as a belief that is not in accord with the actual facts. A mistake in a contract is an unintentional act or omission arising from ignorance, surprise or a misplaced confidence.

Mutual mistake is a defense to contract formation while a unilateral mistake is not. Mutual mistake results when both parties to a contract share a common assumption about a vital existing fact upon which they based their bargain or agreement and that assumption turns out to be false. Because of the mistake, a quite different exchange of values occurs from the exchange of the values the parties contemplated. Under the doctrine of mutual mistake, a contract can be reformed (altered) or rendered voidable if it can be shown that the parties were both mistaken about a basic fact which is material to the agreement. However, only if avoidance is just and reasonable and will not unfairly prejudice the rights of an innocent third party, will a contract be reformed. Reformation is the appropriate remedy when the mistake is one as to expression, while voidance is the proper remedy where a mistake goes to a basic assumption on which the contract was made and has a material effect on the agreed exchange of performances.

If partial performance has occurred on one side, the mutual mistake doctrine does not mechanically cancel all remaining obligations on the other side and thereby allow the nonperforming party simply to retain the benefit conferred by the partial performance. On the contrary, the doctrine permits the court to grant relief only on such terms as justice requires. The doctrine of mutual mistake is limited to cases in which both parties were reasonable in their inconsistent interpretations of the contract and in which neither party

party is more at fault than the other. Moreover, a mutual mistake of fact cannot lie as to a future event. Mutual mistakes must concern past or present facts, not unexpected facts that occur after the document is executed.

9. Changes or Modifications.

Parties to a contract are not forever locked into its terms. Accordingly, parties to an existing contract may, by mutual assent, modify its terms. This is so provided the modification does not violate law or public policy and provided there is consideration for the new agreement or that the new agreement satisfies a statute or is made under circumstances making consideration unnecessary. Accordingly, it is entirely competent for the parties to contract to modify or waive their rights under it ad engraft new terms upon it. *Holyfield v. Harrington*, 84 Kan. 760, 115 P. 546 (1911); *Shutt v. Chris Kaye Plastics Corp.*, 962 S.W.2d 887 (Mo. 1998). Further, the parties to a contract are ordinarily free to change it after making it as they were to make it in the first instance, notwithstanding provisions in it designed to hamper that freedom or regardless of contractual provisions to the contrary. *Twin River Construction Co., Inc. v Public Water District No. 6*, 653 S.W.2d 682 (Mo. App. 1983).

A valid modification of a contract must satisfy all the criteria essential for a valid original contract. *Zumwinkel v. Leggett,* 345 S.W.2d 89 (Mo. 1961). This includes offer acceptance and consideration. One party to a contract may not unilaterally alter its terms. Modification of a contract requires the mutual assent of both parties to the contract. *Fast v. Kahan*, 206 Kan. 682, 481 P.2d 958 (1971); *Rimer v. Hubbert*, 439 S.W.2d 5 (Mo. App. 1969). Mutual assent is a requisite element in effecting a contractual modification as it is in the initial creation of a contract. *Meyer v. Diesel Equipment Co., Inc.*, 1

Kan.App.2d 574, 570 P.2d 1374 (1977). A request, suggestion, or proposal for an alteration or modification to a contract that is made after an unconditional acceptance of an offer and not assented to by the opposite party does not affect the contract then in full force and effect by reason of the acceptance. The minds of the parties must meet as to any proposed modification.

The original contract may provide for methods and procedures for modification; this is not unusual. The contract's method of modification is not an exclusive method -- the parties may waive the method of modifying the contract (and may waive any other right under a contract).

There is some confusion in the cases as to the necessity of consideration for the modification of a contract and some authority dispensing with it, at least under certain circumstances. *Holyfield v. Harrington*, 84 Kan. 760, 115 P. 546 (1911). Nevertheless, many courts support the general principle that a contract modification must be supported by valid consideration. *Parkhurst v. Investors Syndicate*, 128 Kan. 7, 23 P.2d 589 (1933). This is generally true unless: (1) The modification can be supported on principles of estoppel or waiver, such as where it has been acted upon by the parties until it would work a fraud or injury to refuse to carry it out, or (2) A statute makes the consideration unnecessary.

Although a simple contract completely reduced to writing cannot be contradicted, changed, or modified by parol or oral evidence of what was said and done either prior to or at the time it was made, by the rules of common law it may be appropriate for the parties to add written provisions (prior to any breach of the contract) to waive, dissolve, or abandon the contract or to add to it, change it, or modify it, or any of its terms.

Coonrod & Walz Construction Co, Inc. v. Motel Enterprises, Inc., 217 Kan. 63, 535 P.2d 971 (1975); *George F. Robertson Plastering Co. v. Magidson*, 271 S.W.2d 538 (Mo. 1954). Therefore, extrinsic evidence may be relied on to establish that the parties modified their agreement after its execution. Generally, however, the contract required by the statute of frauds to be in writing cannot be validly changed or modified as to any material condition therein by subsequent oral agreement so as to make the original written agreement as modified by the oral one an enforceable obligation.

However, a course of dealing is sufficient to establish modification of a contract if the circumstances surrounding the parties' conduct are sufficient to support a finding of a mutual intention that the modification be effective and if such intention is shown by clear, unequivocal, and convincing evidence (either direct or implied).

The rule followed by the courts generally is that unless a contract is required by law to be in writing, the contract can be modified orally as well, even though it provides that it can be modified only in writing. Such a stipulation in the original contract may become inoperative because of modification or rescission, waiver or estoppel, or an independent contract. Some jurisdictions, however, have statutes providing that a written contract containing a provision against oral modification cannot be changed or altered by an executory agreement unless it is in writing.

Finally, where possible, a modification agreement should be construed in connection with the original contract. All circumstances surrounding the negotiations held prior to the execution of the modification should be examined. The modification of a contract results in the establishment of a new agreement between the parties which pro tanto supplants the affected provisions of the original agreement, while leaving the

balance of the agreement intact. Although the effect of the modification is the production of a new contract, it consists not only of the new terms agreed upon, but of as many of the terms of the original contract as the parties have not abrogated by their modification agreement.

Heather F. Shore, Esq.
911 Main Street, Suite 2300
Kansas City, MO 64105-5319
Phone: 816-292-7000
hshore@browndunn.com
www.browndunn.com

CONTRACT FORMATION
Bidding - Public And Private
Mistakes And Protests

Presented By:

Jeffrey B. Rosen

Polsinelli Shalton Flanigan Suelthaus PC
700 West 47th St., Suite 1000
Kansas City, MO 64112
(816) 753-1000
jrosen@pswslaw.com

I. BIDDING.

The bidding process has traditionally been the first interaction between the owner and the contractor. In competitively bid jobs, the bidding process is also the first major opportunity for disputes to arise. For this reason, understanding the rules of the bidding process is important to all parties involved: the owner, the design professional preparing the bidding documents, the general contractor, the subcontractors and the suppliers.

A. Types of Bids.

1. Public Bids.

The bidding process differs with the type of bid and the type of owner involved in the project. Almost all construction projects for federal, state or local governments involve competitive bidding. The competitive bidding ordinance or statute will frequently require that the governmental body enter into a contract with the "lowest and best" bidder. **K.S.A. 19-214; 75-3741 ("lowest responsible" bidder**); **Bridge & Iron Co. v. Labette County, 98 Kan. 292, 296, 158 P. 8.** See also, **KAT Excavation, Inc. v. City of Belton, Missouri, 1999 WL 311704 (Mo. App. W.D. 1999).**

Bids are typically opened in public and all bidders are informed of the results at the same time. A governmental owner may reject all bids if they all sharply exceed the budget account or the government's own estimate of what the project should cost. Often the government must reject bids that are not "responsive" or are not received from a “responsible” bidder.

The term “responsible” bidder simply means bidder must have the resources available and experience necessary to perform the project work. **Gilbert Central Corp. v. Kemp, 637 F. Supp. 843,847-48 (D. Kan. 1986).**

The term "responsiveness" means that the bid must be in strict compliance with the material terms and conditions of the invitation to bid. The contract must be the contract advertised. **Gilbert Central Corp. v. Kemp, 637 F. Supp. 843,847-48 (D. Kan. 1986), R.D. Andersen Const. Co. v. City of Topeka, 228 Kan. 73, 612 P.2d 595 (1980); and Williams v. City of Topeka, 85 Kan. 857, 118 P. 864 (1911).**

"Responsiveness" focuses on whether (1) the bid submitted is an offer to perform the exact task spelled out in bid invitation and (2) acceptance will bind contractor to perform the work in accordance with the invitation. For this reason, bids which are qualified or which contain exceptions are vulnerable to being declared "not responsive" and being rejected. Public owners are ordinarily obliged to reject such bids because they are not submitted on an equal footing with the other bidders and thus defeat the fairness of competitive bidding system. **Bridge & Iron Co. v. Labette County, 98 Kan. 292, 296, 158, P. 8.**

Bid Protests on Federal Government construction project (which are beyond the scope of this article), or injunction actions on Missouri or Kansas state, county or municipal jobs and which are discussed below), typically are filed when (1) a low bidder is denied a job because the state government finds its bid to be nonresponsive or (2) a second low bidder believes the first low bid is nonresponsive and so the second low bidder should be awarded the job.

In Missouri, a "disappointed bidder" generally has no legal "standing" (power or right) to sue the state (or county or local) government in such circumstances (in an effort to procure the job for itself or stop the government from awarding the job to the apparent low and best bidder). Missouri law only allows such a bidder to sue in very limited circumstances: (1) If it can evidence abuse or corruption or basic unfairness in the propriety of the bidding process itself. **Metropolitan Express Services, Inc. v. City of Kansas City, Missouri, 23 F.3d 1367 (8th Circuit 1994) [in which the federal court allowed a disappointed bidder standing to**

challenge the propriety of the procurement itself] (2) If it can find a friendly taxpayer to sue the government because it would be impacted adversely if the job, say, is awarded to the second low bidder (viz., accepting a higher bid means spending more taxpayer money). In either case, if the contractor can sue the state (or county or local) government in Missouri, it is entitled to sue for **money damages and to enjoin** the government from awarding the job to anyone other than it.

In Kansas, to the contrary, a disappointed bidder DOES have standing to sue, but can only sue for injunctive, not monetary, relief**. Sutter Brothers Construction Co., Inc. v. City of Leavenworth, 238 Kan. 85, 708 P. 2d 190 (KS 1985).**

2. <u>Private Bids</u>.

Unlike bidding in the public sector, bids in the private sector are generally opened in private and there is no obligation to award the contract to the lowest responsive and responsible bidder. Further, the private owner has the opportunity to review "non-responsive bids" and to enter into contracts with bidders who have varied the terms of their bid.

Generally, the private owner has no obligation to enter into any contract based on bids and the opening of bids may be only the first step in a "bid shopping" procedure. For this reason a contractor presenting a bid in the private sector may properly wonder if there will be true competition or whether the award is to a favored contractor with the owner using the bidding process as a negotiating tool. Frequently, inquiry to the owner, the owner's design professional and other industry sources will give the contractor an inclination of whether there is to be a "true competitive bid."

B. <u>Withdrawal of Bid Due to Clerical Mistake</u>.

In the rush to put together a bid, it is not uncommon for a mistake to be made. Most public contracts and many private jobs require some form of security for a bid, typically a bid bond. This security may be lost if the contractor is the successful (low) bidder but cannot subsequently perform. A contractor who discovers an error in his bid and therefore

cannot perform within that price faces this risk. In some circumstances, however, a mistaken bid can be withdrawn without penalty or prejudice.

Obviously, the sooner a contractor can discover a mistake in a bid and call it to the attention of the owner, the more likely it is that the contractor will be able to avoid a penalty. Mistakes in bids are commonly found after the low bidder, bothered by an unreasonably large discrepancy between his bid and the next lowest bid, reviews his or her bid calculations and discovers an error. Once the contractor is certain that an error has been committed, the most important thing for a contractor to remember is that **IMMEDIATE ACTION MUST BE TAKEN.** A court may interpret a contractor's failure to give prompt notice as an election to absorb the bid mistake. **Massman v. United States, 102 Ct. Cl. 699, 60 F. Supp. 635, cert. denied, 325 U.S. 866 (1945)**.

The contractor, upon discovery of a bid mistake, should send a written explanation to the owner describing in detail (1) the mistake and (2) the amount of the bid that the contractor actually intended to submit. The contractor should immediately request a meeting with the owner. The request should be made in writing. If a meeting is held, the contractor should send a letter to the owner confirming the discussions at the meeting, describing the mistake and identifying the amount of the bid the contractor actually intended to submit.

In states other than Kansas and Missouri, there are many cases, which support a contractor's right to withdraw a mistaken bid stemming from an honest **clerical error**, provided the awarding party will not be materially damaged. **Dick Corp. v. Associated Elec. Co-op Inc., 475 F. Supp. 15 (W.D. Mo. 1979)** and, among others, **Chernick v. U.S., 372 F.2d 492 (Ct. Cl. 1967)**. **Mistakes in judgment**, however, as opposed to mere clerical errors, generally do not justify a contractor to withdraw his bid. In **Missouri State Hwy. Comm'n v. Hensel-Phelps Const. Co.,** 634 S.W.2d 168 (Mo. 1982), for example, the court refused to grant relief to a contractor who failed properly to interpret a state sales tax law and "labor precedent" which lead to higher material and labor costs. See also, **American Shipbuilding**

Aydin Corp. v. United States, 669 F.2d 681 (1982) and **National Line Co. v. United States, 607 F.2d 978 (Ct. Cl. 1979)**, among others.

By comparison, the Kansas Supreme Court in **Triple A Contractors, Inc. v. Rural Water District No. 4, 226 Kan. 626, 603 P.2d 184 (1979)** took a minority position and refused to grant relief to a contractor for even clerical errors. The contractor's bid was $170,000 lower than the next lowest bid and $490,000 lower than the engineer's estimate. The court said, "We can see no occasion to make a distinction between a clerical error and an error in judgment." See, in accord, **Anco Const. Co., Ltd. v. City of Wichita, 233 Kan. 132, 135, 660 P.2d 560 (1983)**, in which the Kansas Supreme Court (1) reaffirmed Triple A. Contractors, Inc. and (2) refused to allow Anco to correct a $95,794 clerical error in its bid. Anco made a mathematical error. It failed to transfer $95,794 for certain electrical instrumentation from its recapitulation sheets to its lump sum bid. The Court refused to allow Anco to withdraw its bid since Anco did not notify the City of its mistake **until after the bid opening had begun**. **See, also, Albers v. Nelson, 248 Kan. 575, 580, 809 P.2d 1194 (1991) and Squires v. Woodbury, 5 Kan. App. 2d 596, 599, 621, P.2d 445 (1980), rev. denied 229 Kan. 671 (1981)**.

As a result of the unfairness inherent in the **Triple A** and **Anco** court cases, the Kansas Legislature **in 1995** enacted new law which provides bidders some relief from clerical errors on **public contracts.** In Kansas Senate Bill 115 (March 30, 1995) the legislature allows relief (withdrawal or correction of a bid) in the following circumstances:

A. BEFORE BID OPENING - Any bidder may correct or withdraw its bid (without penalty) before bid opening; Sec. 2.

B. AFTER BID OPENING - *MISTAKE IN JUDGMENT* - No correction permitted; Sec. 3.

C. AFTER BID OPENING - *"NONJUDGMENTAL" MISTAKE"* – "Awarding Authority" *shall* permit a bidder to withdraw its bid (without penalty) [Sec. 5] ***if***:

(i) The bidder notified the awarding agency of the nonjudgmental mistake within two business days after the bids were opened [Sec. 5]; and,

(ii) The nonjudgmental mistake is evident on the face of the bid [Sec. 5(a)]; or

(iii) The bidder establishes by clear and convincing evidence that a nonjudgmental mistake was made [Sec. 5(b)].

D. VERIFICATION OF MISTAKE - The new law also provides that the awarding agency *may* request a bidder to verify its bid if the agency has reason to suspect a nonjudgmental mistake [Sec. 4]. Upon receipt of such a request a bidder may verify or withdraw its bid; provided, however, that it respond one way or the other within two business days after receipt of the request. Failure timely to respond means that the bid (mistaken or not) is considered verified as submitted!

Accordingly, although the new Kansas law gives limited relief for "nonjudgmental" bid mistakes, the lesson to learn in Kansas is to act fast or you will lose what limited rights you have!

In addition to the relief provided by the common law, certain governmental regulations provide bid mistake relief in connection with government contracts; **Federal Acquisition Regulations, FAR Section 14.406-1, et seq.**

It must be noted, however, that the timing of the notification of bid mistake and the nature of the error are vital in determining whether a contractor will be relieved from a bid.

Also remember that there is no similar law in Missouri. In Missouri, court decisions provide a contractor's only guidance; and **Dick Corp.** (Page 7 infra) and **Hensel Phelps** (Page 7 infra) are the leading cases.

C. Correction of Bid Before Award Due to Clerical Mistake.

On the one hand, courts (except those in Kansas prior to the 1995 legislation) have been fairly cooperative in allowing contractors **to withdraw** a bid that is in error. On the other hand, courts impose more difficult burdens of proof on a contractor who seeks **to reform or amend** its bid upward (or downward) and still retain the job (or obtain the job by displacing an otherwise low bidder). Even proof of a clerical error does not automatically allow reformation.

Courts have generally ruled that in order to allow the reformation of a bid, a contractor must demonstrate by clear and convincing evidence (i) the existence of the bid mistake and (ii) the amount to the bid which the contractor actually intended to submit. **Triple A. Contractors, Inc. v. Rural Water District No. 4, 226 Kan. 626, 603 P.2d 184 (1979)**; **Dick Corp. v. Associated Elec. Co-op, 475 F. Supp. 15 (W.D. Mo. 1979); U.S. v. Hamilton Enterprises, Inc., 711 F.2d 1038 (Fed. Cir. 1983); Jasmar Inc. v. United States, 442 F.2d 930 (Ct. Cl. 1971); Chris Berg, Inc. v. United States, 426 F.2d 314 (Ct. Cl. 1970); and Chernick v. United States, 372 F.2d 492 (Ct. Cl. 1967) FAR Section 14.406-3.**

In **Dick Corp. v. Associated Elec. Co-op, 475 F. Supp. 15 (W.D. Mo. 1979)**, the court permitted reformation of a contract where the estimator failed to transfer the correct dollar amount form a bid worksheet to a bid summary sheet. The error resulted in a $1,000,000 difference in the bid. The court permitted reformation because it found "clear and convincing evidence" of both the existence of the mistake and the bid price the contractor actually intended to submit.

D. Correction of Bid After Award of Contract or During Construction.

Generally speaking, an error in the dollar amount of a bid becomes increasingly more difficult to correct after award of the contract, and particularly after commencement of construction. In addition to proving the existence of the bid mistake and the amount of the intended bid, the contractor must also prove that the owner knew or should have known of the

mistake before awarding the contract. **Anco Const. Co., Ltd. v. City of Wichita, 233 Kan. 132, 660 P.2d 560 (1983)** (no relief for unilateral mistake); and **Bromley Contracting Co. Inc. v. United States, 596 F.2d 448 (Ct. Cl. 1979)**. For example, in **Ruggerio v. United States, 420 F.2d 709, 713 (Ct. Cl. 1970)**, the court stated:

> . . . [W]hat we are really concerned with is the overreaching of a contractor by a contracting officer when the latter has the knowledge, actual or imputed as something he ought to know, that his bid is based on or embodies a disastrous mistake and accepts the bid in face of that knowledge.

Normally, it is only in this instance that a contractor is allowed additional compensation for work necessitated by the mistake. A great disparity in bids is helpful to a claim but it is not always sufficient. **Triple A. Contractors, Inc. v. Rural Water District No. 4, supra; Anco Const. Co., Ltd. v. City of Wichita, supra**; and **Aydia Corp. v. United States, 669 F.2d 681 (Ct. Cl. 1982)**. The key is whether the owner knew or should have known of the error.

E. Mistakes in Subcontractor's Bid to Contractor.

The problems with bid mistakes also arise at a second level--the subcontractor's bid to a contractor. This problem can be viewed both from the perspective of the prime contractor as well as that of the subcontractor. A contractor relies upon the subcontractor's bid, as a component of a larger bid to the owner. If the subcontractor refuses to perform at the earlier quoted price, the contractor could be prejudiced by having to hire another subcontractor to perform the work possibly at a higher price. Thus, a contractor is often interested in seeking to enforce the subcontractor's bid.

On the other hand, the contractor who is awarded the contract, may decide to earn more profit from the project by attempting to find a lower bid for the subcontractor's work, than that which was quoted prior to the award. In this instance, the subcontractor is the one who wishes to enforce the right to perform the subcontract at the price quoted.

Although the law has been changing in these two areas, some principles have been

established.

1. A Contractor Typically Can Enforce a Subcontractor's Bid.

Prevailing case allows a contractor to enforce a subcontractor's bid.

Originally, however, early court decisions held that a subcontractor's bid in this situation does not constitute a binding contract. **James Baird Co. v. Gimbel Bros., Inc., 64 F.2d 344 (2nd Cir. 1933)**. The James Baird Co. case specifically held that in this situation a subcontractor's bid to a contractor was not a binding promise. Sensing that such thinking placed a contractor in a precarious situation, more recent (and now prevailing) decisions have ruled that a subcontractor is bound to honor its bid to a contractor in certain situations. The cases have relied primarily upon **Section 90 of the Restatement of Contracts (Section 89 Restatement of Contracts (Second))**, which provides as follows:

> A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise.

For example, in **Drennan v. Starr Paving Co., 51 Cal.2d 409, 33 P.2d 757 (1958)**, the California Supreme Court held that when a subcontractor knew that the prime contractor would be relying upon its bid, in making a larger bid on a construction contract, the subcontractor was bound to perform pursuant to the bid. A number of other cases have likewise held that the subcontractor can be bound to honor its bid because of the reliance upon it placed by the prime contractor; **Janke Const. Co. v. Vulcan Materials Co., 527 F.2d 772 (7th Cir. 1976); Debron Corp. v. National Homes Const. Corp., 493 F.2d 352 (8th Cir. 1974); and N. Litterio Co. v. Glassman Const. Co., 319 F.2d 736 (D.C. Cir. 1973)**.

2. A Subcontractor Typically Cannot Enforce Its Right to Perform.

Although it appears that the contractor can bind a subcontractor to its pre-award bid, the opposite does not appear to be true. A subcontractor cannot require a contractor to hire it

to perform subcontract work based upon a bid made prior to the contractor's successful award of a construction contract. This is based upon the principle that the subcontractor's bid is merely an offer that the contractor is not required to accept. As stated in the dissenting opinion in **Mitchell v. Siqueiros, 528 P.2d at 1081**:

> The general is fully protected but the sub remains vulnerable if the general, after winning the bid, engages in the unethical practice of bid shopping (using the low bid already received to pressure other subcontractors into submitting even lower bids). Despite universal disapproval by the commentators, this would appear to be the present state of the law in construction industry contracts.

F. Summary

In summary, bid mistakes, at the prime contractor or subcontractor level, must be addressed **immediately, before the bid opening has begun and in writing**. Relief for a clerical error in Kansas may **only** be available **if you act promptly**.

II. KNOWING WHAT TO DO WHEN THE PLANS AND SPECIFICATIONS ARE DEFICIENT

Prepared and Presented by:

G. Steven Ruprecht
Brown & Dunn, P.C.
911 Main Street, Suite 2300
Kansas City, MO 64105-5319
Telephone: 816-292-7000
Facsimile: 816-292-7050
Email: sruprecht@browndunn.com

DEFICIENT PLANS AND SPECIFICATIONS

The Spearin Doctrine and Its Acceptance

A long established principle of construction law acknowledges that an owner who furnishes detailed specifications to a contractor impliedly warrants that those specifications will be fit for the purpose for which they are intended. In 1918, the Supreme Court recognized an owner's implied warranty of specifications in United States v. Spearin, 248 U.S. 132 (1918). In Spearin, a construction site flooded due to the collapse of a sewer that the contractor had relocated to the owner's specifications. The Court found that the presence of a dam within the sewer caused the flooding and that the contractor had complied with the owner's specifications and said:

> "When one agrees to do, for a fixed sum, a thing possible to be performed, he will not be excused or become entitled to additional compensation because unforeseen difficulties are encountered. [Citations omitted.] Thus, one who undertakes to erect a structure upon a particular site assumes ordinarily the subsidence of the soil. [Citations omitted.] But if the contractor is bound to build according to plans and specifications prepared by the owner, the contractor will not be responsible for the consequences of defects in the plans and specifications. [Citations omitted.] This responsibility of the owner is not overcome by the usual clauses requiring bidders to visit the site, to check the plans, and to inform themselves of the requirements of the work. . . ."

Spearin enunciated two propositions relating to an owner's implied warranty of specifications. First, an owner-furnished design specification warrants the suitability of the completed end product. Second, the warranty will not be "overcome by general clauses in the contract requiring the contractor to examine

the site, to check up on the plans, and to assume responsibility for the work until completion and acceptance." These propositions commonly referred to as the Spearin doctrine, have become a widely accepted part of state and federal construction contract law, both in the public and private sectors. Missouri and Kansas recognize the Spearin doctrine, including the concept that the owner implied warranty of the plans and specifications trumps the contractor's express warranties. Clark v. City of Harrisonville, Missouri, 348 S.W.2d 369 (Mo. App. 1961); Bernard McNemany Contractors, Inc. v. Missouri State Highway Commission, 582 S.W.2d 305 (Mo. App. 1979); Sanders Plumbing &. Htg., Inc. v. City of Independence, Mo., 694 S.W.2d 841 (Mo. App. 1985); Sandy Hites Co. v. MSHC, 149 S.W.2d 828 (Mo. 1941); North County School Dist. R-1 v. F&D Co. of Maryland., 539 S.W.2d 469 (Mo. App. 1976); Eveready Htg. & Sheet Metal, Inc. v. D.H. Overmyer, Inc., 476 S.W.2d 153 (Mo. App. 1972); Green Construction Co. v. Kansas Power & Light Co., 1 F.3d 1005 (10th Cir. 1993); *cf.* Saddlewood Downs, L.L.C. v. Holland Corp., Inc., 33 Kan.App.2d 185, 99 P.3d 640 (2004).

In Ideker, Inc. v. Missouri State Highway Comm'n., 654 S.W.2d 617 (Mo. App. 1983), the court of appeals held that Missouri case law recognizes a cause of action *ex contractu* in the nature of breach of warranty. In Ideker, the general contractor filed suit against a governmental entity with whom it was in privity claiming that the plans prepared by the governmental entity were faulty, thereby

causing the contractor to incur extra expense. The court declared six elements to the cause of action:

1. A positive representation by the government
2. Of a material fact
3. Which is false or incorrect
4. Lack of knowledge by a contractor that the representation of the material fact is false or incorrect
5. Reliance by the contractor.

See Massman Const. Co. v. Missouri State Highway Commission, 31 S.W.3d 109 (Mo. App. 2002), regarding the lack of knowledge element – contractor claimed that a rock revetment that the contractor itself had placed in the river ten years earlier hindered its work on bridge piers.

In Green Construction Co. v. Kansas Power & Light Co., *supra*, a Spearin type implied warranty was urged by a contractor who contended that information provided by the owner concerning subsurface conditions was inaccurate or incomplete causing a constructed dam to crack. The Tenth Circuit, applying Kansas law, acknowledged that if the owner impliedly warranted the specifications, and breached that warranty, the contractor could recover. However, the court qualified Spearin application stating that an implied warranty would be found only where the owner made unequivocal affirmative statements which were false or misleading.

In Unnerstall Contracting Co., v. City of Salem, 962 S.W.2d 1 (Mo. App. 1997), the Missouri Court of Appeals for the Southern District refused to find a seventh element necessary to assert a warranty claim under Ideker. The court

specifically refused to find as a necessary element the intent by the government that the contractor rely on the positive representation. *Id*. at 8. The court's analysis distinguished between contract and warranty claims on one hand and tort claims on the other, reasoning that, because Ideker is founded in contract, intent is not a necessary element. But the court noted that the speaker's intent that the representation be acted upon is an element of a cause of action for fraud. *See also* Leo Journagon Construction Co. v. City Utilities, City of Springfield, Mo., 116 S.W.3d 711 (Mo. App. 2003), contractor failed to make a case of a positive misrepresentation.

In Unnerstall, the court distinguished Murphy v. City of Springfield, 738 S.W.2d 521 (Mo. App. S.D. 1987), noting in Murphy that the plaintiff was a subcontractor who was not in privity of contract with the government. Therefore, in Murphy, the plaintiff's claim was in tort and not contract. Unnerstall is helpful because it contains a jury instruction setting forth the verdict director for an Ideker type claim.

In Green Construction v. Kansas Power & Light Co., *supra*, Green sought recovery of extra costs for construction of an earthen dam asserting that Kansas Power & Light impliedly warranted the plans. The court found at 1009:

> "Generally, absent fraud, the party who agrees to complete construction for a fixed cost must absorb any loss resulting from unforeseen conditions. [* * * Citations omitted] When a contract contains a site inspection clause, it places a duty on the contractor to exercise professional skill in inspecting the site and estimating the cost of work. [Citation omitted] Thus, Green is not entitled to additional compensation merely because the project was more

> expensive due to unexpected soil moisture. [Citation omitted] Green may still recover, though, if KPL impliedly warranted the plans and specifications, and then breached that warranty. [Citation omitted] An implied warranty will only be found where the owner made unequivocal affirmative statements which were false or misleading. [Citation omitted] Such a warranty is not avoided by standard clauses disclaiming responsibility for the accuracy of data. [Citation omitted] (Emphasis supplied)

The Spearin Doctrine Justification and Rationale

Justification

The initial justification for an implied warranty of specifications was derived from the "superior knowledge" doctrine, which based owner liability on the assumption that the owner had a superior knowledge or expertise in a given area, upon which a contractor might rely in undertaking a project. As the Spearin doctrine became more widely recognized and refined, the justification changed. Contractors and owners are now assumed to possess an equal amount of "expertise" in a particular method or design. Unless an owner has knowledge which is not reasonably available to bidders, a contractor will be expected to act on the knowledge available to it. Accordingly, owner liability for defective specifications is now based upon the fact that the owner has provided the specifications, and a contractor may assume the specifications are adequate for their intended use:

> "[A] contractor who takes detailed plans and specifications from the owner has a right to rely upon the professional judgment and experience of those employed by the owner to develop those plans and specifications . . . ."

Rationale

The rationale for preservation of implied warranties stems from a desire to insure the opportunity for "intelligent bidding". If an owner-supplied specification is not warranted, the burden shifts to the contractor to make excessive and often cost-prohibitive pre-bid inquiries regarding the accuracy of the owner's factual representations about the design and the site. The impact of these inquiries may threaten the viability of smaller contractors who typically have less resources to allocate toward achieving award. The additional expenditures would reduce competition by decreasing the number of bids received and increasing prices. Alternatively, those contractors not discouraged from submitting bids may simply allocate the cost of their pre-bid inspection to their bid price, again resulting in added expense to the owner.

Scope of the Implied Warranty

"Design" vs. "Performance" Specifications

A contractor should be cautioned that many of the principles of the Spearin doctrine are still not universally accepted. The minority view has held that a contractor, by submitting its bid, agrees to assume the risks associated with defective specifications. However, an overwhelming majority of states have recognized some form of the Spearin doctrine as the law in that jurisdiction.

Even the jurisdictions that have embraced the Spearin doctrine have placed some limitations on its scope. For example, owner-supplied specifications may be of two types, "design" specifications or "performance" specifications. Design

specifications explicitly state the materials to be employed and the exact method of performance and permit no deviations. *See e.g.* Trustees of Indiana University v. Aetna Cas. & Sur. Co., 920 F.2d 429 (7th Cir. 1990), where University specified a particular brick product which failed. Performance specifications, on the other hand, specify the results to be achieved and leave the precise method and means of achieving that performance to the contractor. *See* Stuyvesant Dredging Co. v. US, 834 F.2d 1576 (Fed. Cir. 1987).

One of the first issues a contractor must address in seeking to prove that an owner has impliedly warranted a specification is to establish that it is a design specification. Detailed design specifications contain an implied warranty by the owner that if they are followed, an acceptable result will be produced. *See* Fruin-Colnon Corp. v. Niagara Frontier Transport Auth., 585 N.Y.S.2d 248 (App. Div. 1992). Normally, a contractor will not prevail on an implied warranty claim for an equitable adjustment involving performance specifications. Only in the very rare case where the specifications call for a performance which is impossible to achieve will relief be given.

Mixed Design/Performance Specifications

Increasingly, a contractor's focus is to prove that a specification with both design and performance elements is fundamentally of the design type. Large-scale construction contracts often contain a mixture of both design and performance specifications. The contractor has the burden of proving that the specifications are "design" rather than "performance" in nature. The type of specification is not

always clear from the language of the contract. For example, a detailed design specification often provides for contractor discretion in the method, thereby creating a limited performance specification. However, general clauses in the contract requiring a contractor to install or construct a "complete job" or "properly functioning" product are not sufficient to convert detailed design specifications into performance specifications. More commonly, a performance specification may be held to function as a design specification if the methods, products and order of performance are inordinately controlled by the owner.

General Qualifications on Warranty

In addition to a requirement that the specifications in question be design specifications, the Spearin doctrine has been interpreted over the years to encompass several other fundamental qualifications. For example, liability for defective specifications can extend to an owner even when the owner did not actually prepare the specifications. Where an owner chooses an architect/engineer to prepare specifications, the owner is still liable for any defects in those specifications when the architect is acting as an agent of the owner. Notwithstanding, an architect who prepares defective specifications is not totally insulated from liability. Courts have held that a contactor may directly sue the architect for negligent preparation of specifications. Chubb Group of Ins. Cos. V. C. F. Murphy and Assoc., 656 S.W.2d 766 (Mo. App. 1983); Westerhold v. Carroll, 419 S.W.2d 73 (Mo. 1967); Tamarac Dev. Co. v. Delamater, Freund & Assoc., 675 P.2d 361 (Kan. 1984).

It is well settled that an owner's implied warranty of specifications does not guarantee the specifications to be perfect. Rather, the warranty applies to major defects which would substantially increase a contractor's costs. Thus, contractors are expected to anticipate the need to make minor deviations from complex contract documents. To the extent a deviation causes increased costs to the contractor, those minor costs may be disposed of under the "changes" clause of the contract.

The owner's implied warranty of the accuracy and suitability of its specifications has been held not to include a general warranty of the commercial availability of the products the contractor may need to complete the job. An exception to this rule is where an owner specifies a product by name, it warrants both that the named product will be available and that the commercially available product will itself be free of defects. Similarly, where the owner requires the use of a "standard product", the owner has impliedly warranted the commercial availability of a standard product meeting the owner's specifications.

Another rule of law related to the Spearin doctrine that requires mentioning is the "Government Contractor" defense. This doctrine provides that when a public contractor performs according to government specifications, that contractor is shielded from liability to a third party who is injured as a result of contact with the end product. The "Government Contractor" defense is derived from the basic premise that the Government and its agencies are immune from tort liability. Therefore, where a public construction contractor performs in strict accordance

with Government-provided specifications, the contractor is also immune from liability when a third party is injured at the site, so long as that contractor has not acted negligently.

Recovery Under The Spearin Doctrine

Disclaimers

When a specification problem arises during the performance of a contract, one of the first questions the parties normally ask is, "which party assumed the risk of any excess costs associated with resolving the problem?" Owners frequently attempt to avoid liability under the implied warranty of specifications by including disclaimer clauses in contracts. The success of a disclaimer will vary based upon a consideration of several factors.

Many construction contracts include vague boilerplate clauses that require bidders to inspect the site, check the specifications and drawings, and to familiarize themselves with the requirements for performance. Generally, an owner may not shift the risk to the contractor through the use of vague boilerplate disclaimers. Bernard McNenany Contractors, Inc. v. Missouri State Highway Commission, 582 S.W.2d 305 (Mo. App. 1979); City of Columbia, Mo. V. Paul Howard Co., 707 F.2d 338 (8th Cir. 1983); Green Construction Co. v. Kansas Power & Light Co., 1 F.3d 1005 (10th Cir. 1993).

In Hayes Drilling, Inc. v. Curtiss-Manes Construction Company, Inc. v. Board of Education, South Callaway R-2 School District, 715 S.W.2d 295 (Mo. App. 1986), the court held that a drilling contractor was not required to make its

own independent site investigation of subsurface conditions prior to bidding on a subcontract and was entitled to additional compensation for removal of unforeseen obstructions. The specifications in Hayes allowed Hayes the right to make its own borings at its own expense; however, the specifications did not require that Hayes make its own test borings. Hayes was entitled to rely on the boring logs in the contract which showed no rock which could amount to the obstructions which required extraordinary efforts. In addition, there was a unit price bid for removal of obstructions at $800.00 per cubic yard which indicated a concern for that cost or more expensive drilling and which caused the court to conclude that that unit price was of additional persuasiveness that Hayes did not have to go beyond what was shown on the boring logs prior to bidding. In other words, there was a contingency for unit price remuneration provided for in the bid and the School District accepted it. In Hayes, the court concluded that Hayes was not put on notice that it should make any independent investigation of subsurface conditions and had a right to rely on the representations in the core borings as being complete and accurate.

In Green Construction Co. v. Kansas Power & Light Co., *supra*, the court said at 1009:

> "However, where a contractor has a duty to make an independence inspection, reliance on the owner's specifications may very well be unreasonable. [Citation omitted] An owner does not create an implied warranty by providing some soil information but instructing the contractor that the information may not be complete and that all independent site and soil investigation is required. [Citations omitted] This contract . . . squarely placed the risk of uncertainty as

> to site and soil conditions on the contractor. There was no implied warranty."

In Sanders Plumbing & Htg. v. the City of Independence, Mo., 694 S.W.2d 841 (Mo. App. 1985), the court held the contractor had a viable contract action against the City based upon inaccurate representations of core borings. The court said the City's disclaimer, which stated that the data showing the results of the test holes borings was not part of the contract and disclaimed any guarantee of accuracy of the data, and was ineffective based upon the contract documents. The court held the contractor should be paid when it does what it is required to do under the plans and specifications where a contractor is constructing a project according to another's plans.

Notwithstanding the ineffectiveness of general disclaimers, a limited allocation of risk is permitted where an owner expressly discloses a known risk and the contractor still agrees to perform. However, a successful disclaimer must expressly state that information provided in the contract is potentially unreliable. The owner may insulate himself from liability by only making affirmative representations about a particular condition. Failure to make disclaimers, a limited allocation of risk is permitted where an owner expressly discloses a known risk and the contractor still agrees to perform. However, a successful disclaimer must expressly state that information provided in the contract is potentially unreliable. The owner may insulate himself from liability by only making affirmative representations about a particular condition. Failure to make any representations

about a site condition will not allocate the risk to an owner if it possesses no special knowledge of a latent defect. As one court noted, "Silence alone is not actionable."

Courts have consistently held that when major elements of the work are omitted from the contract, the owner assumes all liability for the defective specifications. Air Cooling & Energy, Inc. v. Midwestern Constr. Co. of Mo., Inc., 602 S.W.2d 926 (Mo. App. 1980), held that core boring information in that case was not warranted as accurate and, therefore, Air Cooling could not rely upon the borings but rather should have made an independent site investigation. The court denied recovery for its cost of removing extra rock. However, as stated by the court in Sanders, the holding in Air Cooling is limited by the court's decision in Ideker, Inc. v. Missouri State Highway Comm'n. The rationale of both Ideker and Sanders was that if the owner makes a positive representation of a material fact relied upon by a contractor in calculating its bid which turns out to be false or incorrect after the work is commenced and occasions additional expense, the contractor finds himself in the position of one who undertakes one contract but is confronted with the performance of another. Since the owner would get the benefit of another contract and if the performance of that other contract entails more expense than was calculated in submitting its bid, the owner should be the one to bear the added cost rather than the contractor because the owner is the beneficiary of necessary but unbargained for work resulting from its positive representation of a material fact which turned out to be false or incorrect. Ideker,

as followed by the court in Sanders, holds that boiler plate disclaimers like the ones found in those cases (which are also similar to the one in Air Cooling) does not negate the representations made by test results where those results are positive representations of material fact.

Proving The Elements Of A Claim Under The Spearin Doctrine

A contractor who has attempted to comply with defective specifications, and thus incurred additional costs, has a claim for an equitable adjustment. To prevail under an implied warranty theory a contractor must prove the following:

a. The contractor has complied with the specifications;

b. The specifications were defective; and

c. The defective specifications were the cause of the delay or problem.

First, recovery under the Spearin doctrine requires strict compliance with owner-supplied specifications. If a contractor fails to comply fully with even faulty design specifications, recovery under the implied warranty is precluded. Heman Construction Co. v. Mason, 112 Kan. 648 (1923). Second, a contractor must prove that the specifications were indeed defective. Proving that specifications furnished by an owner are defective may require testimony as to industry practice, expert analysis of calculation and design, or a comparison of conflicting contract documents.

Finally, the contractor must demonstrate a causal link between the employment of the defective specifications and the occurrence of some delay or problem with the end product. A mere showing that a design specification was defective and that a contractor adhered to that specification will not permit recovery unless the contractor can prove that the increased costs were a direct result of the defective specification.

Exceptions To The Spearin Doctrine

Contract Ambiguity/Duty to Inquire

Patent Ambiguity

One frequently asserted exception to the Spearin doctrine concerns the requirement that a contractor inquire into any obvious error in drafting, a gross discrepancy, or an inadvertent but glaring gap in the contract documents. This is commonly referred to as a patent ambiguity. If the ambiguity is so obvious that a reasonably prudent bidder should have detected the discrepancy and sought clarification prior to submitting its bid, a contractor has a duty to inquire of the owner the true meaning of the contract before submitting its bid or its proceeds at its own risk. The parties conduct after the contract may likewise be used to determine if the ambiguity was patent. The duty to inquire prevents contractors from taking advantage of owners while protecting other bidders by ensuring that all bidders bid to the same specifications. In addition, it materially aids the administration of contracts by requiring ambiguities to be raised before bid opening, potentially avoiding costly litigation.

Latent Ambiguity

If an ambiguity in the contract specifications and drawings is determined to be latent, a contractor is entitled to relief if it reasonably relied upon its interpretation of the drawings. Courts will apply the reasonable and prudent contractor standard on an ad hoc basis to determine if the ambiguity is patent and glaring. The owner, as drafter of the contract, bears the burden to use language that clearly conveys its intent. If the language used is reasonably susceptible to

more than one meaning as an objective indication of the parties' intent, the specification is ambiguous and will be interpreted against the drafter.

Evidence of industry custom or trade usage may be presented to show the intention of the parties where a term is judged to be ambiguous. At least one court has held that industry custom or trade usage can be used to explain a term of art or determine more appropriate interpretations of the contract terms in light of the contractor's previous experience and the understanding of the parties. However, other courts have held that neither a contractor's belief nor customary industry practice can make an unambiguous contract provision ambiguous, or justify departure from its terms.

A contractor has an obligation before bidding on a contract to inquire about obvious omissions or discrepancies in the drawings or specifications. A contractor who fails to inquire at the time of bidding may not successfully make a claim based on its interpretation of the contract language, no matter how reasonable its interpretation may be.

The owner, however, is also obligated to disclose any adverse information that could have a material effect on bids or the contractor's ability to complete the work.

G. Steven Ruprecht
Brown & Dunn, P.C.

The Fundamentals Of Construction Contracts: Understanding The Issues

Prepared and Presented by:

G. Steven Ruprecht, Esq.
Brown & Dunn, P.C.

THE FUNDAMENTALS OF CONSTRUCTION CONTRACTS: *UNDERSTANDING THE ISSUES*

VII. Dispute Resolution Provisions

A. Alternative Dispute Resolution ("ADR")

What is ADR

ADR is an all-encompassing and somewhat imprecise term embracing every method and means possible to resolve a dispute short of a final courtroom determination. ADR can be used separate and apart form litigation and in conjunction with litigation at virtually any stage of the process.

The various common forms of ADR are:

- Negotiation
- Early Neutral Evaluation
- Mediation
- Moderated Settlement Conference
- Arbitration
- Mini Trial
- Summary Jury Trial
- Rent a Judge

The principal feature of ADR is that the parties have a great deal of control in fashioning the method and means for resolution of their dispute.

Negotiation for Settlement

Negotiation is very simple. The parties sit down and discuss their problem and try to arrive at an agreed solution. Success depends in large part on the good faith of both parties involved. One of the advantages of negotiation is that it is the least costly of all

ADR techniques. It requires some preparation but not as much as some of the other techniques. There is no special setting in which the negotiation must be held.

Some disadvantages are that the parties often assume passive roles while the lawyers take more active roles; it is non-binding and often adversarial.

Early Neutral Evaluation

This procedure involves a non-binding case evaluation conference. It is attended by both the parties and the attorneys involved in the dispute and presided over by an expert in litigation selected by the parties.

Again, the advantage is low cost. It is similar to mediation but may have more steps involved once the neutral evaluator begins the process. The idea here is to send the parties off by themselves to settle their dispute.

There are very few disadvantages.

Mediation

Mediation is a forum in which an impartial person, known as the mediator, facilitates communication between the parties to promote reconciliation, settlement or understanding among them. It is often used as a settlement tool and the parties, rather than the lawyers, assume more active roles. The procedure generally followed is a simple introductory session where the ground rules are set down, statements made and the parties try to find areas of agreement and dispute. The parties are then separated and they communicate offers and counteroffers to each other with the mediator acting as a communicator of information and a buffer to the parties' emotions.

Some of the principal advantages of mediation are that it is simple and

economical and may obtain a quick result. The parties are also allowed to maintain an on-going business relationship while they keep their dispute both private and confidential.

Some of the disadvantages are that mediation is non-binding and no judgment or ruling is reached. There may be little benefit to a mediation if a novel question of law is involved or credibility of witnesses are important or the opposing party or counsel are untrustworthy or unlikely to compromise.

Moderated Settlement Conference

This is a forum for a structured negotiation between attorneys and clients often presided over by a judge. When it is used in connection with litigation under the authority of a judge, it generally requires the parties to appear at the conference with settlement authority. The attorneys make oral case presentations to the judge stating the relevant facts and law involved in the dispute. The moderator then assists in trying to foster a settlement. Again, it is similar to mediation but generally held at the courthouse in connection with litigation.

The advantages are similar to those of mediation in that the costs are low and it forces the parties to evaluate their case early.

The disadvantages are that it is non-binding and the parties, who are already engaged in litigation, may be compelled to reveal facts that they may wish to keep private for a while longer.

Mini Trial

This is a procedure by which each party summarily presents its position through lawyers and experts, either to an impartial third party or a selected representative knowledgeable in the field of the dispute. The parties may use witnesses to develop their positions followed by rebuttal and questions concerning the presentations.

Some of the advantages are that it is quick, will maintain relations of the parties as private and confidential, it is flexible and involves key personnel of the parties in active roles.

Again, the disadvantages are that it can be more expensive to prepare for than mediation and is non-binding.

When mini trials are used, there is often disagreement between the parties whether some or all of the discovery in the case should be concluded before the mini trial. Also questions arise as to whether the impartial third party or "advisor" should express his or her opinion to the parties about what he or she thinks about the case. Again there is that desire to conceal information which might be harmful.

Summary Jury Trial

This is simply an abbreviated presentation of the facts of the case before a selected and agreed jury. Usually no witnesses are used in a summary jury trial but statements of the parties suffice. In this instance, an advisory opinion is rendered. The technique generally is used after the parties complete discovery when the case is ready for trial.

Some of the advantages are is that it allows for the evaluation of a case before multiple unsophisticated neutrals, much like a jury, and may serve as a basis to settle the

case when the advisory opinion is rendered. If there is no settlement, the case proceeds to trial.

The disadvantages are obvious. There are costs involved and the result is non-binding.

Rent A Judge

In this instance the parties hire a third party to act as a judge. The party might be a retired judge or some other individual with knowledge. They present the facts, the law, witnesses and experts and expert testimony but in an abbreviated form. It is similar to a mini trial or a summary jury trial, but slightly more formal.

Many of the advantages and disadvantages are the same as a Mini Trial and Summary Jury Trial.

From an "advantage" standpoint, the idea of ADR is to bypass the overwhelmed, understaffed and overcrowded courts so as to proceed to resolution of a problem in less time and for a lower cost. At the same time the parties may be able to preserve their relationships without an all out war. ADR is designed to be flexible, confidential and either binding or non-binding depending on the wishes of the parties. It allows for the sue of specialized expertise in the resolution of disputes and a certain amount of autonomy and control by the parties.

As to general "disadvantages," there usually is no discovery involved in the process or discovery is severely curtailed so that the development of facts is hampered. Also, judicial control is limited and there are few controls on the neutral evaluators unless placed upon them by the parties. Oftentimes the quality of justice can suffer in that legal

principles may be subsumed and precedent ignored under these outcome driven procedures. Justice and fair play may take a back seat to "bright line" technical legal principles. Also, unanticipated remedies may be applied for which there may be no judicial review. Unless ADR is carefully controlled, there may be a higher degree of unacceptable results.

When to Use ADR

Clearly, a party might use ADR when the advantages outweigh the disadvantages.

As a rule of thumb there are several important things to look at, including the dollar value of the claim. Certainly ADR would be more valuable in smaller disputes than larger disputes because of the lesser costs. This is not to say that it could not be equally valuable in the larger disputes. Another rule of thumb is to evaluate opposing party and its counsel. If the opposing party and its counsel are reasonable people who intend to be objective about the situation, ADR will certainly work to your advantage. Another rule of thumb is to determine the complexity of the facts or the law. As noted above, legal principles may take a back seat to facts in ADR. Certainly if your facts are extremely complex, it makes more sense to consider ADR than to put those facts in the hands of an unsophisticated judge or jury.

How Prevalent is the Use of ADR?

In 1991, the ABA Forum Committee on the Construction Industry conducted a survey of attorneys who belong to the committee to determine their experience with ADR. Eighty percent of the attorneys responding indicated they had participated in binding arbitration, sixty-five percent in mediation, thirty percent in non-binding

arbitration, twenty-one percent in mini trials and only ten percent tin summary jury trials. Clearly, the most popular methods of ADR are negotiation, mediation and arbitration.

What is Submitted to ADR Generally?

In the construction industry, the most prevalent disputes submitted are defective work, payment disputes, project delays and changes. The least prevalent disputes submitted are jobsite administration questions, differing site condition issues and personal injury and property damage issues for which a courtroom forum may be more appropriate.

What are Appropriate Qualities of an ADR Advisor or Facilitator?

An ADR advisor or facilitator should be impartial, possess managerial skills, personal discretion, listening ability, ability to understand complex issues, patience, creativity, ability to explain issues, persuasiveness, and, in construction disputes, possess some design and/or construction experience, have personal prestige and legal expertise. All of these qualities make for a good advisor.

What is the Success Rate of ADR?

The ABA survey reflected that when using ADR, the parties reached a full settlement in 57.4% of the cases and a partial settlement in 8.4% of the cases. It was reported that mediation was the most successful ADR technique while mini trials was the least successful. It was also discovered that more settlements occur where the parties agreed to ADR after the dispute arose rather than agreeing under a contract to submit a future dispute or when being forced to use ADR by a court. For those parties voluntarily proceeding to ADR after a dispute arose, 72.3% of those case were either totally or

partially settled. For those who were "pushed" into ADR by a contract or a court, only 54.3% of those cases were totally or partially settled. This clearly indicates that the parties' eagerness and cooperation to participate in ADR will greatly affect the results to be achieved.

For those cases where ADR failed to achieve a satisfactory result, attorneys reported that in fully 2/3 of those cases the problem was an unwillingness on the part of the opposing party to compromise. Only in 17% of the cases was an ineffective advisor blamed. This again indicates that ADR is most attractive to those who desire to use it and are willing to compromise.

Preventive ADR

Preventive ADR goes by many names, including:

1. Partnering
2. Step Negotiations; and
3. The Standing Neutral Concept:
    (a) Dispute Resolution Panels
    (b) Standing Arbitration Panels

Partnering – Most disputes that go to litigation involve breakdowns in communication. Recognizing this fact the U. S. Corps of Engineers and others in the private sector have developed a technique called "partnering" to prevent disputes from interfering with construction projects. The experience with partnering, particularly in sealed bid fixed price contracts has reduced disputes in litigation sharply, according to a number of commentators.

The idea of partnering is to build a team mentally among all those who have to work together on it. This includes contractors, subcontractors, engineers, architects, owners, representatives, lawyers and others.

Initially, the parties schedule a preconstruction conference or retreat that might last for an extended period of time at a neutral location. The parties appoint a facilitator who encourages that all significant parties be invited. The facilitator may schedule personality tests of the participants to share with each other, team building exercises conducted in smaller groups and a general session at which hard issues likely to arise on a project are discussed.

While meeting together, the parties who are going to engage in partnering may design dispute resolution techniques or procedures that can be invoked in the future in the event of disagreements. The parties try to formulate and sign a partnership agreement indicating what their goals and aspirations are for the project.

Step Negotiations – Another technique is called step negotiations. In this case, representatives of each party who are intimately involved in the problem and who are not able to resolve it at their level, pass the problem on to their immediate superiors who are asked to confer and try to resolve the problem. Failing their ability to solve the problem, the problem is then passed on to the next higher management level in both organizations. The thought is that because intermediate managers have an incentive to keep difficult problems from bothering higher management, and also to demonstrate their dispute resolution skills, there is an incentive for those parties to resolve disputes before they go to a higher level.

The Standing Neutral Concept – The standing neutral concept involves the selection of a neutral to serve as a dispute resolver throughout the project. This independent neutral or neutrals are called a "Dispute Review Board" or a "Standing Arbitrator". The parties may select one or more industry experts to serve and be available as a standing board or panel throughout the project. The concept is that they are available to act immediately to resolve any dispute that the parties cannot resolve themselves. There are several steps to the procedure.

1. At the beginning of the project the parties make the selection of persons they trust and have confidence in to serve on the panel.

2. The selection of the panel may be patterned after American Arbitration Association procedures.

3. The neutral can be given authority to act on disputes by rendering either a non-binding evaluation or recommendation or a binding decision, whatever the parties decide.

4. The neutral may be given a basic introduction to the project, its nature, extent, scope and even may be favored with a basic set of contract documents for review before any problem arises.

5. The neutral may meet periodically at the project site with key personnel for review of progress even without disputes having arisen.

6. When a dispute does arise, it is referred to the neutral for prompt decision.

7. If the neutral only makes a recommendation and not a binding decision, then the parties can determine what to do with the recommendation and whether to proceed on to a later binding resolution.

8. The expenses of the neutral are generally absorbed equally by the parties who engage in securing one.

Dispute Review Board – The dispute review board consists of one member

selected by the owner and approved by the contractor and one member selected by the contractor and approved by the owner. The first two members select and agree on a third member and the third member usually acts as the chairperson.

The board makes its own rules of operation and the members are kept informed of the construction project progress by receiving weekly reports, making regular visits, visiting representatives, etc. Disputes are resolved as quickly as possible between the parties without involving the board. However, if the parties cannot resolve it, an appeal is then submitted to the board within a set period of time. The parties are given an opportunity to present evidence to the board and it is very informal. They may have representatives at the proceeding. The board is then allowed to ask questions of the witnesses but should not during the hearing express opinions concerning the merits of any facet of the case. After the hearing is conducted, the board meets to deliberate and reach a conclusion and a decision is rendered. The parties can then either accept or reject the decision and move on to other methods of alternative dispute resolution like binding arbitration or litigation if they conclude to reject the result.

Standing Arbitration Panel – The selection and function of the standing arbitrator or panel is similar to the dispute review board or adjudicator except that the neutral acts as an arbitrator who makes decisions that are final and binding on the parties just as in conventional arbitration.

While ADR and preventive ADR certainly are not the answer to all problems, they are an avenue to be considered on every project or, at the very least, when any dispute arises. Given the expense of litigation, the time involved and the uncertainty of

the ultimate result, ADR provides some increased measure of certainty in a very uncertain world.

Delay And Disruption In Construction

Prepared and Presented by:

G. Steven Ruprecht, Esq.
Brown & Dunn, P.C.

DELAY AND DISRUPTION IN CONSTRUCTION

I. The Elements of Delay and Disruption Claims

A delay is a period of time during which the construction project has been extended, postponed, slowed down, shut down, or otherwise has taken longer than it would have taken.

A disruption, on the other hand, is not a delay, although the terms are often confused with one another. A disruption does not necessarily result in a delay. Instead, a disruption is a type of change in the method of production or efficiency of contract performance that may prevent the contractor from actually performing the work as originally planned. A disruption can result in the project taking more time or less time to perform than it would have taken if the contractor had proceeded as originally planned. Whether or not the disruption causes the contractor to spend more or less time in performing the construction, the disruption will cause the contractor to spend more money than it would have otherwise have spent in performing the work functions. Disruption damages are the measure of the resulting increase in difficulty and loss of efficiency in performance of the project work. *See generally* Havens Steel Co. v. Randolph Engineering Co., 613 F.Supp. 514 (W.D. Mo. 1985).

A delay claim asserts that the contract performance time as originally contemplated was extended and that correspondingly the completion date was affected. Morrison Knudsen Corp. v. Fireman's Fund Ins. Co., 175 F.3d 1221

(10th Cir. 1999). A disruption claim, on the other hand, asserts that the contractor's performance of the work suffered a loss in efficiency or productivity. In a disruption claim, the completion date may or may not be affected, but efficiency and performance will be affected.

II. Two Types of Delays

A. Excusable and Nonexcusable Delays

Delays in the performance of construction contracts are generally one of two mutually exclusive types: (1) excusable and (2) nonexcusable.

Excusable delays justify the contractor in receiving an extension of contract performance time. They excuse the contractor from being assessed delays for impacts on the project's schedule. The theory is that the delay is beyond the control and without the fault or negligence of the contractor and, therefore, not properly chargeable to the contractor. Fru-Con Construction v. US, 44 Fed.Cl. 298 (1999); and Central Coast Construction v. Lincoln Way Corp., 404 F.2d 1039 (10th Cir. 1968). Nonexcusable delays, on the other hand, are the responsibility of the contractor and generally result in the assessment of liquidated damages by the owner if the contractor is unable to escape the impact of the delays. Brinderson Corp. v. Hampton Roads Sanitation Dist., 825 F.2d 41 (4th Cir. 1987).

As a general rule, delays caused by the actions or inactions of the owner or the owner's agents are excusable delays. Typical owner-caused excusable delays are defective plans and specifications, restricted access to the jobsite and other forms of owner interference, differing site conditions or changed conditions,

untimely review of contract submittals including shop drawings, failure of the owner to schedule and coordinate the work, suspensions of the work for reasons unrelated to the contractor, and owner-caused delays to the original scope of the work. *See gen.* Artcraft Cabinet, Inc. v. Watajo, Inc., 540 S.W.2d 918 (Mo. App. 1976); and Ark Construction Co. v. City of Florissant, Missouri, 558 S.W.2d 418 (Mo. App. 1977).

Other excusable delays may not be caused by anyone; but, instead, are the result of causes beyond the owner's control and without the fault of the contractor. These may include: unusually severe weather, other acts of God, labor disputes and strikes. These types of causes often are referred to as "force majeure" events. Excusable delays will entitle the contractor to an extension of time if the contractor can prove that it caused a delay to the completion date. However, if the completion date is not extended, then no extension of time is mandated.

Nonexcusable delays, on the other hand, are delays that the contractor may not be able to foresee or control including delays caused by lower tier subcontractors. *See gen.* Dicon, Inc. v. Marben Corp., 618 F.2d 40 (8th Cir. 1980) (Missouri law); Werner v. Ashcraft & Bloomquist, Inc., 10 S.W.3d 575 (Mo. App. 2000). The contractor cannot claim time or money for delays caused by normal weather conditions, defective and nonconforming work, the acts or omissions of subcontractors and suppliers of the contractor, or the impact of these delays on the work not otherwise affected by excusable delays. Generally, only excusable delays are compensable.

B. Excusable Delays

1. Compensable and Noncompensable Excusable Delays

Excusable delays will entitle a contractor to a time extension, but they will not necessarily entitle the contractor to compensation for economic loss. Excusable delays may be either compensable or noncompensable. By definition, a compensable delay results in compensation for the cost of the delay. A noncompensable delay only results in entitlement to a time extension and no money. Generally, a delay is not compensable unless it has been caused by the owner. Not all excusable delays are compensable delays. For example, delays due to acts of God, strikes, etc. may be excusable and result in a time extension, but are not compensable because they are not the direct fault of the owner.

As a general proposition, a contractor will be entitled to a time extension for an excusable delay if the delay affects a critical activity of the contractor in the performance of his work that extends the overall completion date. However, not all delays result in delays to overall project completion. Many delays may only impact activities that are not on the critical path of the project schedule and, therefore, they are only noncritical delays. Noncritical activities on a network schedule have what is called "float" or available time between the date designated as the early start and the late start date and the early finish and late finish dates. This cushion in the schedule, a float, is generally recognized by courts as an asset that may be available to all parties to the contract. The party that uses the float first gets the benefit of the float up to the point when the float is used up and the

project is then delayed. Therefore, for example, if there is a delay in approval of shop drawings, the owner may be able to utilize the cushion in the schedule for late return of the drawings until such point that the late return begins to impact completion. Likewise, the contractor's delay in submission of the shop drawings could be viewed the same way.

2. Critical and Noncritical Delays

Delays that impact the critical path of the project and, therefore, result in a delay to the overall project are called critical delays. *See* Morrison Knudsen Corp. v. Fireman's Fund, 175 F.3d 1221 (10th Cir. 1999). Many delays, however, impact activities that have available float time as noted above and the delaying event merely uses up that time without impacting the project completion date. These delays are considered to be noncritical and, therefore, do not result in time extensions or additional money.

C. Disruptions

1. Compensable and Noncompensable Disruptions

Like a delay, a disruption is classified as either compensable or noncompensable to the contractor suffering the disruption. Disruptions that occur to the contractor's planned performance of the work do not automatically entitle the contractor to a time extension or to money. As a general proposition, the same principles of compensability that apply to delay claims apply to disruption claims. If a disruption is not foreseeable or could not have been avoided by a reasonable contractor, it may be deemed compensable. However, if the disruption was foreseeable and could have been avoided by reasonable actions taken by the contractor, the disruption typically would not be compensable.

Similar to the issue regarding delays, owner-caused disruptions typically are compensable whereas disruptions caused by weather, strikes and other events that are not the fault of the owner or the contractor are typically not compensable.

Compensable disruptions may include defective plans and specifications, unavailable or late owner furnished materials, architectural failures, restricted site access, untimely responses to RFI's, suspensions of the work or resequencing of work, and a large number of changes to the original scope.

D. Concurrent Delays

Concurrent delays arise when two or more delaying events occur during the same period of time. The two delays may affect a claim if one event is excusable and the other event is not excusable or, if one event is compensable and the other event is not compensable. Concurrency issues arise when one delay is the responsibility of the owner and the other delay is the responsibility of the contractor. When this occurs, the delays are said to be concurrent and many courts have ruled that neither party may recover compensation for the delay unless it can be allocated. *See gen.* Havens Steel Co. v. Randolph Engineering Co., 613 F.Supp. 514 (W.D. Mo. 1985); US v. United Engineering & Construction Co., 234 US 236 (1914); and Southwest Engineering Co. v. US, 341 F.2d 998 (8th Cir. 1965).

Typically, a contractor is entitled to a time extension and corresponding delay damages for an owner-caused delay to the construction schedule. However, if the owner-caused delay is concurrent with a delay caused by the contractor, then the contractor is entitled to a time extension but not to damages.

Similarly, the owner cannot assess delay damages or liquidated damages against the contractor if the delays leading to the late completion of the project are concurrent and partially caused by the owner. *See gen.* Southwest Engineering v. US, 341 F.2d 998 (8th Cir. 1965); and Stewart v. Cunningham, 219 Kan. 374, 548 P.2d 740 (1976).

In order for a contractor or owner to recoup damages for delay, it is up to the party seeking the damages to show that the delay was not concurrent. If concurrent delay cannot be disproved, then the courts may not be able to separate the delay and likely will not be able to award delay damages. *See gen.* Havens Steel Co. v. Randolph Engineering Co., 613 F.Supp. 574 (W.D. Mo. 1985).

E. Contractual Limits on Recovery

1. No Damages for Delay Clause

An often utilized limitation on recovery of delay is the "No Damages for Delay" clause found in many contracts. This clause, by its terms, appears to preclude contractors from recovering damages for any delay, regardless of fault, to the contract performance. In the State of Missouri, in the private construction setting, no damages for delay clauses have been ruled enforceable. Roy A. Elam Masonry, Inc. v. Fru-Con Construction Corp., 922 S.W.2d 783 (Mo. App. 1996); *but see* Section 34.054, R.S.Mo. (2000), declaring that no damages for delay clauses are void and against public policy in the public setting; and *see* Peter Kewit & Sons Co. v. State Highway Commission, 184 Kan. 737, 339 P.2d 267 (1959), implying that Kansas courts would strictly construe such a clause.

2. Notice Provisions

Another potential limitation on a contractor's ability to recover delay and disruption damages are the notice provisions contained in the contract that may require the contractor to follow specific guidelines at the time of a potential source of injury if the contractor is to recover later for any delay or disruption arising

from the triggering event. *See* Southwest Engineering Co. v. Reorganized School District R-9, 434 S.W.2d 743 (Mo. App. 1968).

Failure on the part of the claimant to follow notice provisions may very well result in a waiver of any claim for delay. The contractor's failure to give an owner timely notice of a triggering event, could prejudice the owner's ability to protect its position and potential exposure because, without notice, the owner cannot mitigate its loss by taking steps reasonably necessary to avoid greater injury.

II. Factually Supporting a Delay/Disruption Claim

As indicated above, in order to prove entitlement to a time extension, a contractor must show that the delay in question was a critical delay and that it was an excusable delay. Also, it must be shown that the delay was not concurrent with other delays and that it was, therefore, compensable. In order to prove these facts, project documentation is important.

A. Project Documentation

Project documentation is the primary factual support used by contractors and subcontractors to develop claims for extension of time and disruption regardless of the claim theory or method.

Contractors, subcontractors and owner representatives should all maintain accurate and complete documentary records of the project conditions kept contemporaneous with project performance. Project records that are important to analysis of delay and disruption claims might include the bid package, the actual

bid, plans, specifications, schedules, and scope of work. Accurate jobsite records should also reflect daily conditions including the number of men on the job, equipment, material deliveries, weather, machinery breakdowns and other problems that day in and day out impact performance on the project and may delay or disrupt it from either the owner or contractor's standpoint. The entries into the books and records should discuss and record conversations on the project, minutes and notes of meetings held, oral notices, if any, objections and waivers to contract formalities.

Clearly, project records should be contemporaneous with the performance of the work and maintained by people with personal knowledge of the events that are recorded so that they might testify later. These records should be kept in the ordinary course of business and should be detailed enough to reconstruct the project history without resort to certain witnesses who might have left the contractor or owner's employment before the claim is heard. Records that routinely are important to this analysis are:

1. Pre-award documentation

   In order to establish the contractor's plan for the performance of the work as a baseline to compare later performance, records such as the bid package including drawings, specifications, pre-bid meeting minute notes, logs of telephone calls, requests for information, discussions regarding proposed schedules, as-bid schedules, manpower loading documentation, bid calculations, quantity takeoffs, subcontractor and supplier bids, vendor quotes, site investigation reports, geotechnical investigation reports, photographs, schedules, etc. are needed.

2. Contract documents

   These should include the original contract, amendments, plans, addendums, specifications, any changes to the bid package, post-award contract negotiation meeting minute notes, general and supplementary conditions, audited overhead rates, subcontract documents, schedules, architect's documents, records and instructions, replies to questions, construction management agreements, site condition reports, borings, pre-construction reports, jobsite inspection reports, notes and photos, walk-through reports, etc.

3. Contemporaneous records

   These might include such things as correspondence, meeting minute notes, notes of oral communications and conversations, interoffice communications, e-mails, permit applications, permits, jobsite diaries, jobsite reports including labor and equipment information, delivery tickets, testing and safety reports, requests for information, all notices to the owner, changes, drawings, specifications, shop drawing logs, change order proposals, change order logs, photographs, videos, weather reports, punch lists, certificates of substantial and final completion, and all letters, memos and other documents regarding reservation of rights by either party.

4. Schedule information

   This information should include original as-planned schedules, schedule updates, as-built schedules, progress

reports, short term look-ahead schedules, any as-planned and as-built manpower and equipment loading information, meeting minutes, fragnets, time extension proposals, requests relating to change orders or contractor change order proposals, notice of time-related impacts, and, again, all reservation of rights information.

5. Cost data

Cost data that should be retained includes all original budgets, as-planned cost information, takeoffs, labor distribution reports, labor time records, overtime records, certified payroll reports, equipment cost records, rental agreements, purchase orders, delivery tickets, invoices, project cost reports, subcontractors' cost reports, progress and payment reports, periodic payment requests with all backup, actual payment documents, bank loan and interest data, bond rates, audited overhead rates, indirect cost breakdowns, company revenue and profit history, etc.

B. Supplementary Project Information

Since construction projects are never built as originally planned and conceived, a contractor must continually update as-built project schedules to reflect progress, changes in sequence and logic, calendaring any unanticipated changes and events, and identifying impacts on project scheduling and performance.

Periodic schedule updates form the basis of an as-built record of the project. Accurate as-built information is a powerful tool for proving a delay and a disruption claim. It may help establish the cause and effect of the damages incurred by the contractor on the project and thereby establish entitlement to time extensions and compensation and establish defenses to any assessments of liquidated damages.

III. Establishing Causation and Entitlement – Delay Claims

Construction projects historically have been scheduled and managed using bar chart schedules. Bar charts are fairly useful tools for scheduling jobs. However, they do not demonstrate relationships among various scheduled activities. Therefore, they are very limited and generally helpful for smaller and less complicated jobs. Bar charts alone are generally incapable of meeting the necessary standards of proof for establishing a contractor's entitlement to, or quantum of, a delay or disruption claim.

Generally, a contractor will need a network-based scheduling technique such as Critical Path Method scheduling to properly reflect delay and disruption on a project. Critical Path Method (CPM) for scheduling is a computerized graphical presentation of the resourcing, sequencing, timing and interrelationships of the various activities that comprise a construction project. Time is allotted to each activity performed in sequence. Delay and disruption claims are proven through a combination of schedule analysis and costs quantification. Schedule analysis is the combination of CPM scheduling techniques with contemporaneous project records for establishing the effect or impact of delays and disruptions on the project schedule. Several methods of schedule analysis are utilized with varying degrees of success and acceptance. *See gen.* Sterling Millwrights Inc. v. US, 26 Ct.Cl. 49 (1992), for an explanation of CPM analysis.

A. Impacted As-Planned Analysis

One method is to take the original schedule and extend it out for events that occur. In this method, the contractor's as-planned schedule, or baseline schedule, is modified to include any delays by the owner, for example, through the insertion of those delays into the schedule. The schedule is then recalculated to determine a new completion date. The difference then between the old completion date and the new completion date is the amount of delay impact.

This is a very simple and quick method of analysis. However, approaching delay in this fashion ignores what may have actually happened on the project including delays which may have been the fault of the contractor or which may be concurrent with owner delays. Extended or impacted as-planned schedules are often used but one needs to be aware of the weaknesses in the approach.

B. Collapsed As-Built Analysis

This is somewhat the reverse of the impacted as-planned. This analysis looks at the project when completed based on job records and schedule updates. Owner-caused delays are then removed from the schedule and the schedule is recalculated or reduced back to show when the project should have finished absent or "but for" the owner's delays.

Again, this is a rather simple approach but relies heavily on the judgment of the person making up the schedule to identify and remove the appropriate impacts. It can be subjective.

C. Contemporaneous Schedule Analysis

There are two methods of schedule analysis that are considered contemporaneous in their approach. One is the "Time Impact Analysis" and the other is the "Windows Analysis".

The time impact analysis is an analysis typically used at the time the delaying event occurs and looks forward projecting the delay impact based on the contractor's planned schedule. The second method, the windows analysis, is retrospective, after the fact.

1. Time Impact Analysis (TIA)

Under this method, the contractor prepares a fragnet of the delaying event when it is first encountered. The fragnet is then inserted into the latest updated schedule when the delaying event occurs. The schedule is then recalculated, with the fragnet inserted, to determine the change, if any, to the completion date. The advantages to this method are that it allows for the timely and contemporaneous settlement of a particular issue. Also, the triers of fact may look favorably upon analyses completed at the same time as the occurrence of the delaying event. And, by using the latest update, the past performance and history of the project are taken into account in the analysis. The accuracy of the projection is directly linked to the accuracy of the fragnet and the accuracy of the baseline schedule.

2. The Windows Analysis

In a windows analysis, the project is broken down into time frames or "windows" of time. The as-built critical path is determined during each window and the status of the project is evaluated at the beginning and the end of each

window. The method for evaluating the status of the project at any point in time is to review the as-built schedule or contemporaneous update in effect at that point in time with the as-planned schedule and determine if the project is ahead or behind schedule and by how much. The analysis moves sequentially from the beginning to the end of the project.

There are several steps involved in performing a windows analysis but these are beyond the scope of this summary.

IV. Establishing Causation – Disruption Claims

As noted above, disruptions in the performance of the work can have a serious effect on the progress of the project. When continual, repetitive progress is made on a project, workers become skilled and efficient and, therefore, the contractor is able to reduce the number of workers and hours to perform a particular task. When a disruption occurs, the continuous flow is interrupted, reducing or halting the progress and causing the learning curve effect to diminish or disappear. The resulting loss of efficiency may be accompanied by a decline in the morale of the workers. Proving that a disruption has resulted in a loss of efficiency typically requires the contractor to demonstrate something more than the presence of anecdotal testimony about events that have occurred. Ordinarily the contractor must make comparisons to a standard to determine differences.

A. The Measured Mile Method

This comparison method compares an actual unit of productivity of performing certain work during periods of disruption to a selected baseline period

when such disruptions did not occur. Typically, these comparison of time frames are on the same project. The difference in productivity between the impacted period and the unimpacted period is theoretically the result of the disruptions to the performance.

This approach is valid if the nature of the work is repeatable, predictable and similar, the baseline period itself did not contain impacts which effect the analysis, the makeup and skill of the work force remains approximately the same, the inefficiencies due to contractor-caused problems were not concurrent with owner problems or have been removed, comparisons are not made between dissimilar crafts, and the periods of comparison were not impacted by excusable or noncompensable delays such as adverse weather and strikes. *See gen.* U.S. Industries, Inc. v. Blake Construction Co., 671 F.2d 539 (D.C. Cir. 1982).

B. Comparison with Other Projects

When an unimpacted period does not exist on the specific project to use as a baseline to measure a loss or productivity (for example, where a contractor has been impacted throughout the project), another method for demonstrating and quantifying the disruption is a comparison of the productivity experienced by the contractor for a specific type of work on another project. All of the same issues discussed above apply equally to a comparison with other projects. *See e.g.* Clark Baridon, Inc. v. Merritt Chapman & Scott Corp., 311 F.2d 389 (4th Cir. 1962).

C. Comparison of Schedules

This method simply compares the original schedule and the sequencing of activities in the original schedule to broken or disjointed sequencing and progression of the work actually experienced on the project.

D. Industry Estimating Guidelines

In utilizing this method, estimating guidelines published by national trade organizations, such as the National Electrical Contractors Association and the Mechanical Contractors Association of America, as well as industry estimating standards such as R.S. Means and The Richardson Rapid Construction Cost Estimating System can be used as baselines. However, these become very generalized and may not be job-specific and, therefore, not as reliable.

E. Industry Studies

There also exist certain industry studies to be used for estimating guidelines, such as those published by the Business Roundtable or the U.S. Army Corps of Engineers, to determine inefficiency experienced due to certain types of disruptions. Again, these are not job-specific and tend to be generalized in nature.

F. Time and Motion Studies

These can be fairly effective if executed properly. The time and motion study may measure labor and equipment inefficiencies by comparing an unimpacted segment of work to an impacted segment of work; the difference being the impact translated to dollars. *See e.g.* Peter Kiewit & Sons v. Summit Construction Co., 422 F.2d 242 (8th Cir. 1969).

V. Quantifying Damages

A. Types of Damages

Unless otherwise provided for in the contract, all reasonably foreseeable damages are recoverable in a compensable delay claim. *See* Kansas City Bridge Co. v. K.C. Structural Steel Co., 317 S.W.2d 370 (Mo. 1958).

A disrupted or delayed project typically may suffer three different types of damages.

1. Direct impact costs which include:

    (a) Incremental costs that would not have occurred but for the disruption; i.e. labor and equipment demobilization and remobilization;

(b) Lost efficiency costs; i.e., additional labor and equipment costs incurred because of decreased productivity; and

(c) Premium wages for working overtime or multiple shifts.

2. Extended overhead costs which include:

(a) Field overhead; and

(b) Home office overhead.

3. The owner's delay damages which are either:

(a) Contractually imposed liquidated damages; or

(b) Actual damages.

B. Calculating Damages

There are a number of methods used in the industry for calculating damages. These include, among others,

1. The total cost approach;

2. The A/B estimates approach;

3. The delta estimates approach;

4. The jury verdict approach; and

5. The modified total cost approach.

1. Disruption Damages

(a) Impact Costs

(1) The Total Cost Method –

Under this method, the actual cost of the project is compared to the estimated or bid price. The contractor then seeks the difference as compensation for the inefficiencies and disruptions encountered on the project. This method is not very well favored by the courts. It is allowed when there is no better method for determining damages. *See* Servidone Construction Corp. v. US, 931 F.2d 860 (Fed. Cir. 1991); and J.D. Hedin Construction Co. v. US, 374 F.2d 235 (Fed.Cl. 1965). In order for this method to be credible, the party using the method may have to prove three important things: (1) that his bid was accurate or reasonable to eliminate that issue as a cost factor, (2) that the actual costs incurred in the performance of the work were reasonable, and (3) that the contractor was not responsible for any increased costs. Moorehead Construction Co. v. City of Grand Forks, 508 F.2d 1008 (8th Cir. 1974).

There are two other variations of the total cost method. One is the modified total cost method which allows the court to adjust the total cost for inaccuracies in bids, costs which are not the responsibility of the owner, etc. Second, in the jury verdict method, the contractor may prove fair and reasonable approximations of his damages where no other means are available so long as the proof rises beyond mere speculation. *See e.g.* Azure v. US, 129 F.3d 136 (Fed. Cir. 1997); Municipality of Anchorage v. Frank Coluccio Construction Co., 826 P.2d 315 (Alaska 1992); and WRB Corp. v. US, 183 Ct.Cl. 409 (1968). Kansas seems to support this method. *See e.g.* Uhrich Millwork v. J.W.

Brester Co., 124 Kan. 579, 261 Pac. 561 (1927); and Horsch v. Terminix Intern. Co., Ltd. Partnership, 19 Kan.App.2d 134, 865 P.2d 1044 (1993).

2. The Measured Mile Method

Under this method, the claimant establishes a baseline production rate during an unimpacted period and compares this with the production rate during the impacted period. It is widely accepted. Generally it must be shown that the comparison is between similar work on the same project with similar complexity and crews. The comparison also must provide for periods which occurred close in time and that the periods were not impacted by excusable or noncompensable factors such as weather, etc. *See* P. J. Dick, Inc, ASBCA No. 5597, 01-2 BCA 3164 (2001).

3. Time and Motion Method

As noted above, a time and motion study can be done. Conditions on the jobsite are recreated, specific tasks are performed, and the production rates measured.

4. Estimating Guides and Industry Studies

As noted above, they can be compared to actual work and dollars established.

2. Delay Damages

(a) Extended Overhead

Delay damages result from a contractor's extended time on the project. If the delays are compensable, then the claimant may collect the delay costs from the owner. These delay damages include extended jobsite or field overhead costs as well as extended home office overhead.

The extended jobsite or field overhead is a time related cost incurred at the project site suffered due to extended time spent on the project. The most common types of extended job overhead costs are labor and material escalation costs, extended supervision costs, extended jobsite costs such as tools, utilities, equipment, trailer rentals, and other items that remain on the project during the delay period generally referred to as "general conditions".

(b) Extended Home Office Overhead

General and administrative overhead costs (G&A) incurred by a contractor's home office generally are borne by the contractor's active projects. In order to attribute some portion of that cost to a particular delay, courts have recognized a formula calculation commonly known as the *Eichleay* formula to do that. Eickleay Corp., ASBCA No. 5183, 60-2 BCA 2688 (1960). The *Eichleay* formula calculates a percentage of home office overhead attributable to a particular delay on a project as follows:

Contract Billings	x	Total Overhead incurred	=	Overhead allocable
Total Billings for a project		during the contract		to the contract

Allocable Overhead Actual days of contract performance	=	Overhead allocable to the contract on a per diem basis		
Daily Overhead	x	Number of days delay	=	Extended Overhead

See gen. Kansas City Bridge Co. v. K.C. Structural Steel Co., *supra*; Havens Steel Co. v. Randolph Engineering, *supra*; Capital Electric Co. v. US, 729 F.2d 743 (Fed. Cir. 1984); and Del Rio Drilling Programs, Inc. v. US, 146 F.3d 1358 (Fed. Cir. 1998), discussing elements and evidence necessary to prove an *Eichleay* claim.

VI. Impact, Escalation, Acceleration

There are two additional concepts related to delay and disruption. These are escalation and acceleration. Where a contractor seeks to recapture lost time due to delays or disruptions, he may incur extra costs due to higher wages, premium time, overtime, lost productivity, increased material and equipment costs, etc.

Escalation is the increased cost for performing work at a later date than planned. For example, a planned raise in union rates occurs during a delay phase in a project. The project may not be delayed overall (after taking into account excusable delays), but it may finish later than planned from a calendar standpoint. Increased costs (material increases in price, etc.) may be recoverable from the party causing the delay. Havens Steel Co. v. Randolph Engineering Co., 613 F.Supp. 514 (W.D. Mo. 1985).

Acceleration, on the other hand, is where the contractor applies additional resources to complete the project on schedule. The need for additional resources may be an owner-caused delay. These costs likewise may be recoverable. For example, loss of productivity (due to increased crew size) does not require that the end completion date be extended. US Indus., Inc. v. Blake Constr. Co., 671 F.2d 539 (D.C. Cir. 1982). Such a claim may also succeed in the face of a No Damages for Delay clause. John Green Plbg. & Htg. Co. v. Turner Constr. Co., 742 F.2d 965 (6th Cir. 1984).

Acceleration may result from direct orders of the owner or "constructively". If an owner insists that a project be completed on schedule in face of excusable delays, or where the owner presses for more crew and equipment than the contractor's original plans required, acceleration may be found. Azure v. US, 129 F.3d 136 (Fed.Cir. 1997); Titan Pacific Constr. Corp. v. US, 17 Ct.Cl. 630 (1989). Excusable delay, however, must be demonstrated. Granite Constr. Co. v. US, 24 Ct.Cl. 735 (1992). An owner's insistence that a schedule be met or the contractor accelerate to meet it when the owner has no fault in causing delay or disruption may be a cost to be absorbed by the contractor.

VI. Common Problems

There are any number of common problems that occur with respect to attempting to prove delay and disruption damages on a project. These include inadequate records kept by the contractor, noncritical path delays, work site overcrowding, failure to recognize or reconcile contractor-caused delays, miscalculations of lost productivity, miscalculations of overhead, and the extrapolation of productivity impacts. All of these can work against a contractor's claim.

In sum, it is important to know your contract and what it provides in terms of requests for extension of time for delays and disruptions; it is important to collect the documentation and review schedules; and understand what has occurred on the project. But, more than anything, it is important to simplify these rather complicated concepts so that they will be understood by the trier of fact.

G. Steven Ruprecht
Brown & Dunn, P.C.

CLAIMS FOR DELAY, ACCERLATION/INEFFICIENCIES, AND CHANGES ON CONSTRUCTION PROJECTS IN KANSAS & MISSOURI

Lorman Educational Services

Heber Gonzalez, Esq.
Shughart, Thomson, & Kilroy, P.C.
120 West 12th Street, Suite 1600
Kansas City, MO 64105
Phone: 816-395-0634
hgonzalez@stklaw.com

DELAY CLAIMS

- Excusable vs. Nonexcusable Delays
- Compensable Delays
- Concurrent Delays
- Float and Critical Path
- Contractual Provisions
- Liquidated Damages

Excusable/Nonexcusable Delay

- Excusable delays, also called "compensable" delays, are justified delays which preclude liquidated damages, serve as a basis for an extension of the contract time, and depending on contract terms as a basis for recovery of the resulting damages
- Nonexcusable delays are the responsibility of the contractor and generally result in the assessment of liquidated damages by the owner if the contractor is unable to escape the impact of the delays

Excusable Delay - Examples

- Design Errors/Omissions
- Owner-Initiated Changes or Owner Delay
- Unanticipated Weather Conditions
- Labor Disputes
- Force Majeure/Acts of God
- Differing Site Conditions
- Others allowed by contract

Nonexcusable Delay – Examples

- Foreseeable delays
- Normal Weather Conditions
- Correcting Defective Work
- Delays caused by subcontractors or suppliers
- Contractually allocated risks of delay

Float and Critical Path

- Critical path in schedule is the sequence of tasks that control the project schedule.
- Float is time that tasks may be delayed without impacting the critical path.
- Who owns the float?

Concurrent Delays

- Concurrent Delays are when two or more independent causes of the delay.
- Must be critical to project completion
  - Not concurrent- One delay affecting float and one affecting critical path task
- Must be independent

ACCELERATION

- Directed vs. Constructive Acceleration
- Owner may direct acceleration when project has suffered excusable delay.
- Constructive delay when acceleration due to excusable delay and refusal of any time extension

ACCELERATION

- "Acceleration" is the process by which the contractor simply throws more resources, specifically labor, at the project to complete on schedule.
- Notice
- Evidence of Acceleration
- Updated Schedules
- No Damages for Delay Provisions and Acceleration Claims

Acceleration

- Caused by other contractors, owner's material suppliers, or other hindrances
- Result in shifting work sequence, shifting work areas; stacking of trades; congested work areas; lack of site access
- Contractor tries to reclaim lost time resulting in: loss of productivity/overtime; increased material/labor costs; or increased costs for finding new subcontractor
- Increased costs in acceleration are generally recoverable. *See* Havens Steel Co. v. Randolph Eng'g Co., 613 F. Supp. 514 (W.D. Mo. 1985).

INEFFICIENCIES

- Lost Productivity in the Field
- Owner caused inefficiencies
- 3rd Party Contractors Causing Delays and Inefficiencies

Damages for Delay

- General Conditions
- Extended Overhead and Home Office Overhead (*Eichleay* Formula)
- Equipment Costs
- Interest
- Owner- Liquidated Damages or Actual Damages

Calculating Delay Claims

- **Unless otherwise provided for in the contract, all reasonably foreseeable damages caused by a compensable delay are recoverable. *Kansas City Bridge Co. v. Kansas City Structural Steel Co.*, 317 S.W.2d 370 (Mo. 1958).**
- **Total Cost Method**
- **Modified Total Cost Method**
- **Jury Verdict Method**
- **Estimates**
- **Actual Damages**

Liquidated Damages

- A contractual stipulation as to the damages that will be accessed against the party breaching the contract, typically expressed in terms of dollars per day that project is late.
- As long as the liquidated damages clause is a reasonable calculation of actual damages, the provision is upheld. *National Cooperative Refinery Ass'n v. Northern Ordnance, Inc*., 238 F.2d 803, 805 (10th Cir.1956) (applying Kansas law); *Unified School District No. 315 v. DeWerff*, 6 Kan.App.2d 77, 81, 626 P.2d 1206, 1210 (1981).

MO -No Damages for Delay

- Permissible in private contracts in Missouri. *See* Roy A. Elam Masonry, Inc. v. Fru-Con Const. Corp., 922 S.W.2d 783 (Mo.App. 1996).
- Not permitted in public contracts in Missouri. *See* RS Mo § 34.058.

KS -No Damages for Delay

- No statute regarding no "damages for delay" clauses
- Courts have upheld clauses
- Kansas Supreme Court upheld no damages for delay clause. *See* Kansas City Structural Steel Co. v. L.G. Barcus & Sons, Inc., 535 P.2d 419 (Kan. 1975)).
- Public cases: Edward Kraemer & Sons, Inc. v. City of Kansas City, Kansas, No. 94-2215-GTV, 1995 WL 405098 (D. Kan. June 19, 1995) & Kewit & Sons Co. v. State Highway Commission, 339 P.2d 267 (Kan. 1959)(strictly construed).

CHANGES
Differing Site Conditions

- Contractual Provisions
- Reasonable inspection of site
- Environmental concerns
- Notice
- Different site conditions from that indicated on plans or unknown/unforeseen conditions

Differing Site Conditions- Contract Provision

- **§ 4.3.4** Claims for Concealed or Unknown Conditions. If conditions are encountered at the site which are (1) subsurface or otherwise concealed physical conditions which differ materially from those indicated in the Contract Documents or (2) unknown physical conditions of an unusual nature, which differ materially from those ordinarily found to exist and generally recognized as inherent in construction activities of the character provided for in the Contract Documents, then notice by the observing party shall be given to the other party promptly before conditions are disturbed and in no event later than 21 days after first observance of the conditions….

AIA General Conditions of the Contract for Construction A201 (1997 edition)

MO-Differing Site Conditions

- Breach of warranty claim by a contractor against a governmental entity premised on a positive representation of a material fact:
  - (1) A positive representation by a governmental entity,
  - (2) Of a material fact,
  - (3) Which is false or incorrect,
  - (4) Lack of knowledge by a contractor that the positive representation of the material fact is false or incorrect,
  - (5) Reliance by a contractor on the positive representation of a material fact made by the governmental entity, and
  - (6) Damages sustained by a contractor as a direct result of the positive representation of a material fact made by the governmental entity.

  See Ideker, Inc. v. Missouri State Highway Commission, 654 S.W.2d 617 (Mo.App. 1983).

KS-Differing Site Conditions

- "It is established that 'when the contract contains no change conditions clause and imposes a site inspection requirement on the contractor, the risk of uncertainty of subsurface conditions is placed on the contractor.'
  Green Const. Co. v. Kansas Power & Light Co., 717 F.Supp. 738, 742 (D.Kan. 1989); *But see* Saddlewood Downs, L.L.C. v. Holland Corp., Inc., 33 Kan.App.2d 185, *192, 99 P.3d 640 (Kan.App. 2004)(factually distinguished to avoid harsh result on contractor).

CHANGES
Errors and Omissions

- Patent Errors
- Latent Errors
- Notice and Requests for Clarification
- Documentation of Costs
- Spearin Doctrine

CHANGES
Owner Actions

- Change in Scope
- Change in Schedule
- Owner's Other Contractors
- Construction Change Directive

CHANGES
Constructive Changes

- Constructive Change is equitable remedy for changes that should have resulted in change order
- Construction Change has been applied in the following situations:
  - Contract Interpretation Disputes
  - Government Interference or Failure to Cooperate
  - Defective Specifications
  - Misrepresentation or nondisclosure of superior knowledge
  - Acceleration, subject to limitation of materiality parameters in scope of contract

See Bruner & O'Conner on Construction Law, 4:25 (2002)

Constructive Changes

- When the public or authorized officials direct performance of work which is, in fact, beyond contract requirements, the direction to perform such work has been defined in some jurisdictions as a breach of contract, and in other jurisdictions as a constructive change.

See Global Const., Inc. v. Missouri Highway and Transp. Com'n, 963 S.W.2d 340, 343 (Mo.App. 1997)

- Three general categories of constructive change/breach of contract by public officials.
  - Defective specifications resulting in extra work
  - Public officials misinterpret contract & erroneously rejecting work or require a standard of performance higher than terms of contract
  - Public officials deny contractor justifiable time extension

See Global Const., Inc. v. Missouri Highway and Transp. Com'n, 963 S.W.2d 340, 343 (Mo.App. 1997)

Constructive Changes

- Generally, a contractor may recover for additional work necessitated by a material change in specifications. … However, there can be no recovery for extra work if the work is covered by the terms of the contract. .. "The extra work doctrine" allows additional compensation only "for work that was not within the scope of the contract, such that the parties could not have established a contract price of their own."
  Green Const. Co. v. Kansas Power & Light Co., 1 F.3d 1005, 1009 -1010 (10th Cir. 1993).

MISSOURI KANSAS FEDERAL

LIEN CLAIMS
BOND CLAIMS
PROMPT PAYMENT ACTS
RETAINAGE STATUTES

G. Steven Ruprecht
Brown & Dunn, P.C.
911 Main Street, Suite 2300
Kansas City, Missouri 64105
(816) 292-7000
(816) 292-7050 FAX
sruprecht@browndunn.com

*(*2007)

THE INFORMATION CONTAINED IN THIS MANUAL IS NOT LEGAL ADVICE, BUT IS PROVIDED FOR GENERAL INFORMATION ONLY. THE READER SHOULD CONSULT LEGAL COUNSEL BEFORE APPLYING THE INFORMATION PROVIDED TO ANY SPECIFIC SITUATION.

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I. MISSOURI CONSTRUCTION PROJECTS

A. PRIVATE CONSTRUCTION PROJECTS IN MISSOURI

1. Missouri Mechanic's Liens: Prime Contractor

a. Who Can Claim a Lien?

"Any person who shall do or perform any work or labor upon, rent any machinery or equipment, or furnish any material, fixtures, engine, boiler or machinery for any building, erection or improvements upon land, or for repairing, grading, excavating or filling of the same, or furnish and plant trees, shrubs, bushes or other plants or provide any type of landscaping goods or services or who installs outdoor irrigation systems, under or by virtue of any contract with the owner or proprietor thereof, or his or her agent, trustee, contractor or subcontractor. . . ." (§429.010, R.S.Mo. (2005))

***Note**: Land survey, landscaping suppliers and subcontractors (§429.010), and architects/engineers (§429.015) are also provided lien rights.*

b. Extent of the Lien

(1) The lien shall be upon such building, erection or improvements, and upon the **land** belonging to such owner or proprietor on which the same are situated, to the extent of **three acres**; or

(2) If such building, erection or improvements be upon any lot of land in any **town, city or village**, or if such building, erection or improvements be for **manufacturing, industrial or commercial purposes** and not within any city, town or village, then such lien shall be upon such building, erection or improvements, and the lot, tract or parcel of land upon which the same are situated, and not limited to the extent of three acres; except

(3) If such building, erection or improvements are **not** within the limits of any city, town or village, then such lien shall be also upon the land to the extent necessary to provide a roadway for **ingress** to and **egress** from the lot, tract or parcel of land upon which such building, erection or improvements are situated, not to exceed forty feet in width, to the nearest public road or highway.

***Note**: Liens for tenant-ordered work extend only to tenant's leasehold interest, unless the tenant can be considered the landlord's agent, or unless the landlord requires the tenant to make permanent alterations at the time of the lease.*

(4) Special rules for rental of machinery or equipment provide that (a) the lien shall be for reasonable rental value during the period of actual use and any periods of non-use taken into account into the rental contract while the equipment is on the property; but that (b) there is no lien unless there are improvements made on the property, the amount of the claim exceeds $5,000 and the claimant provides written notice within five (5) days of the commencement of use identifying the rental entity, equipment rented and the rental rate.

(5) Special rules for streets, curbs, sewer, sidewalks, sewer lines, waterlines or other pipelines in front of, adjacent to or along adjoining real estate – a lien may be granted if the work is performed for the owner or his agent, trustee, contractor or subcontractor. (*See* §429.020, R.S.Mo. for specifics.)

c. Notice requirements

(1) Warning Statement to Owner

* Every "original contractor" must give the owner a **statutory warning statement**, in **ten point bold type**, warning the owner to obtain lien waivers from everyone furnishing labor and/or materials. (§429.012, R.S.Mo.) Failure to include warning statement results in failure of the lien.

[SEE FORM M(1)]

(2) Who is an "original contractor"?

* An original contractor is one who makes a **contract** to perform labor or furnish materials with the then owner of the property.

(3) When must the warning statement be given?

* The warning statement must be given at **one of the following four events**, provided the warning statement is given **prior** to the original contractor's receipt of any payment of any kind from the owner:

(a) When the contract is executed;

(b) When the materials are first delivered;

(c) When the work is commenced; or

(d) When the first invoice is delivered.

d. The Lien Statement

Any person claiming a lien on real property and the improvements thereon must file a **lien statement**. (§429.080, R.S.Mo.)

(1) When must the lien statement be filed?

* Within **six (6) months** after the indebtedness shall have accrued (the indebtedness accrues on the last day the claimant furnishes labor and/or materials on the project).

NOTE: *A running account is usually deemed an entire contract.*

(2) Special rule for rental equipment or machinery

* Within **sixty (60) days** after the date the last of the rental equipment or machinery was last removed from the property.

(2) Where must the lien statement be filed?

* With the **clerk of the circuit court** of the county where the project is located.

(3) What must the lien statement contain?

* The lien statement must contain a **verified** statement showing:

(a) The name of the owner;

(b) The name of the claimant/contractor;

(c) The legal description of the real property; and

(d) A **just and true account** of the claim, after all just credits have been given (an itemized statement of the claim, with supporting documentation such as unpaid invoices or pay requests, unpaid supply invoices, records of unpaid materials delivered to the site, records showing hours and type of work performed by each worker, etc.).

An original contractor who has a lump sum contract with the

owner can state his account in lump sum and is not required to itemize it except for extra work.

A "just and true" account may contain mistakes, errors, omissions or inaccuracies so long as they were honest and unintentional.

[SEE FORM M(2)]

e. Suit to Enforce the Lien

An action to enforce a lien must be filed within **six (6) months** after the lien statement is filed. (§429.170, R.S.Mo.) [If defendant files bankruptcy prior to filing of suit, time frame is tolled.] Failure to commence suit results in loss of lien. Suit must be brought against all those with a legal or equitable interest in the land including all lien claimants of record.

f. What Items Are Lienable?

Items of labor and materials used, consumed or made an integral part of the improvement, including such items as labor, materials entering into, used in or consumed in the construction of the improvement, and transportation charges.

g. Lien Fraud

Any contractor which fails to pay a subcontractor or supplier for work or labor for which the contractor has been paid by the owner, with the intent to defraud, is subject to a charge of lien fraud, a Class C felony.

h. Priority of Lien

Lien attaches **to improvements** (but not land) in preference to any prior lien or encumbrance or mortgage upon the land upon which the improvements were made. Execution upon improvements made may be had and improvements removed and sold.

Lien attaches and is preferred to all other liens and encumbrances attaching subsequent to contractor's commencement of work (First Spade Rule).

i. Assignment of rights

Lien rights may be assigned and enforced by assignees.

j. Sale of Property

Property may be sold by order of court and proceeds of sale distributed to satisfy lien.

2. Missouri Mechanic's Liens: Subcontractor/Supplier

a. Who Can Claim a Lien?

Any person who shall do or perform any work or labor upon, or furnish any material, fixtures, engine, boiler or machinery for any building, erection or improvements upon land, or for repairing the same, under or by virtue of any contract with the owner or proprietor thereof, or his agent, trustee, contractor or subcontractor. (§429.010, R.S.Mo.)

**NOTE: Landscaping suppliers and subcontractors (§429.010), and architect/engineers (§429.015) are also provided lien rights.*

**NOTE: Some older Missouri court decisions raise the question of whether the claimant must have a direct contractual relationship with the prime contractor or a subcontractor in order to file a lien.*

b. Extent of the Lien

(1) The lien shall be upon such building, erection or improvements, and upon the **land** belonging to such owner or proprietor on which the same are situated, to the extent of **three acres**; or

(2) If such building, erection or improvements be upon any lot of land in any **town, city or village**, or if such building, erection or improvements be for **manufacturing, industrial or commercial purposes** and not within any city, town or village, then such lien shall be upon such building, erection or improvements, and the lot, tract or parcel of land upon which the same are situated, and not limited to the extent of three acres; except

(3) If such building, erection or improvements are **not** within the limits of any city, town or village, then such lien shall be also upon the land to the extent necessary to provide a roadway for **ingress** to and **egress** from the lot, tract or parcel of land upon which such building, erection or improvements are situated, not to exceed forty feet in width, to the nearest public road or highway.

***Note**: Liens for tenant-ordered work extend only to tenant's*

leasehold interest, or tenant's personalty, unless the tenant can be considered the landlord's agent, or unless the landlord requires the tenant to make permanent alterations at the time of the lease.

c. Notice Requirements

Every person except the original contractor claiming a lien must give the owner at least **ten (10) days advance notice** of his intent to file a lien statement.

[SEE FORM M(3)]

(1) How must notice be given?

* The notice should be **personally served** on the owner in the manner provided for service of process generally (authorized officers or any competent witness to be verified by affidavit).

d. The Lien Statement

Any person claiming a lien on real property and the improvements thereon must file a **lien statement**. (§429.080, R.S.Mo.)

(1) When must the lien statement be filed?

* Within **six (6) months** after the indebtedness shall have accrued (the indebtedness accrues on the last day the claimant furnishes labor and/or materials on the project).

* Within **sixty (60) days** for rental equipment and machinery.

NOTE: *A running account is usually deemed an entire contract.*

(2) Where must the lien statement be filed?

* With the **clerk of the circuit court** of the county where the project is located.

(3) What must the lien statement contain?

* The lien statement must contain a **verified** statement showing:

(a) The name of the owner and contractor;

(b) The name of the claimant;

(c) The legal description of the real property; and

(d) A **just and true account** of the claim, after all just credits have been given (an itemized statement of the claim, with supporting documentation such as unpaid invoices or pay requests, unpaid supply invoices, records of unpaid materials delivered to the site, records showing hours and type of work performed by each worker, etc.).

[SEE FORM M(4)]

e. Suit to Enforce the Lien

An action to enforce a lien must be filed within **six (6) months** after the lien statement is filed. (§429.170, R.S.Mo.).

f. What Items Are Lienable?

Items of labor and materials used, consumed or made an integral part of the improvement, including such items as labor, materials entering into, used in or consumed in the construction of the improvement, and transportation charges.

g. Special Rules: Repair/Remodeling of Residential Property

No person, other than an original contractor, who furnishes any labor and/or materials for the **repair or remodeling of or addition to owner-occupied residential property** of four units or less shall have a lien on such building or structure **unless** and owner of the building or structure, pursuant to a written contract, has consented and agreed to be liable for such costs in the event that such costs are not paid.

(1) Definitions

* "**Owner**" means the owner of record at the time any contractor, laborer or materialman agrees or is requested to furnish any labor and/or materials.

* "**Owner-occupied**" means property which the owner currently occupies, or intends to occupy and does occupy as a residence within a reasonable time after the completion of the repair, remodeling or addition.

* "**Residential property**" means property consisting of four or less existing units.

(2) Form of Consent

* The consent form must be printed in **ten point bold type** and contain the required statutory language.

[SEE FORM M(5)]

(3) Inclusion in Lien Statement

* A copy of the **consent form**, signed by the owner, must be attached to the lien statement.

** **NOTE**: The prime contractor must retain a copy of the consent form, signed by the owner, and must furnish a copy to any person performing work or furnishing labor and/or materials upon request.*

Table 1: Summary of General Rules - Missouri Mechanic's Liens

	Provide Warning Statement[1] to Owner	Obtain Consent of Owner[1]	Serve Notice of Intent to File Lien on Owner[3]	File Lien Statement[4]	File Suit to Enforce Mechanic's Lien
Prime Contractor	Provide Warning Statement to Owner[2]	None Required	None Required	File within 6 months after last day labor/ materials furnished by lien claimant	File within 6 months of filing lien statement
Supplier of Materials to Owner	Provide Warning Statement to Owner[2]	None Required	None Required	File within 6 months after last day labor/ materials furnished by lien claimant	File within 6 months of filing lien statement
Supplier of Rental Equipment	Provide Warning Statement[5]	None Required	Serve upon Owner 10 days before filing lien statement	File within 60 days after the last rental equipment or materials were removed from project	File within 6 months of filing lien statement
Subcontractor or Supplier (other than Supplier to Owner)	None Required	None Required	Serve upon Owner at least 10 days before filing lien statement	File within 6 months after last day labor/ materials furnished by lien claimant	File within 6 months of filing lien statement
Subcontractor/Supplier (other than Supplier to Owner): Repair/Remodel Residential Property	None Required	Must be contained in Owner's contract	Serve upon Owner at least 10 days before filing lien statement	File within 6 months after last day labor/ materials furnished by lien claimant	File within 6 months of filing lien statement

- - - - - - - - - - -

1. Must be in ten point bold type.

2. May be given at any one of 4 specified events (provided it is given prior to receipt of any payment): (a) at execution of contract; (b) when materials first delivered; (c) when work is commenced; or (d) when first invoice delivered.

3. Notice should be personally served on Owner.

4. File with Clerk of Circuit Court of county where project is located.

5. Written notice to Owner within 5 days of the commencement of use. Identify the rental entity, equipment rented and rental rate.

3. Private Payment Bonds

a. Introduction

On private construction projects, owners sometimes require general contractors to provide **payment bonds**, guaranteeing payment to subcontractors/suppliers, to protect the owner from mechanic's liens.

b. Who Can Make a Claim?

Most private payment bonds **specifically define** who will be entitled to make a claim against the bond (e.g., payment bonds typically limit the class of "claimants" to those who furnish labor and/or materials directly to the prime contractor or directly to one of his "first tier" subcontractors).

* ***NOTE:*** Occasionally, *prime contractors will require those subcontractors performing major portions of the work to likewise furnish payment bonds.*

c. Notice Requirements

Private payment bonds typically require a claimant who did not contract directly with the prime contractor to furnish notice, usually within ninety days, to the prime contractor, the owner and the surety in order to preserve a bond claim.

d. Suit on the Bond

Many private payment bonds contain a "private" statute of limitations, indicating a limited period in which suit may be filed against the bond (e.g., within one year following the date on which the prime contractor ceased its work on the contract). If the payment bond is controlled by **Missouri law**, any such "private" statute of limitations is void and unenforceable under Missouri statute, and the general contract statute of limitations of five (5) years controls. (§431.030, R.S.Mo.).

e. Recommendations

Recovery under a private payment bond usually depends upon the specific language of the payment bond. Accordingly, subcontractors and suppliers can protect themselves by taking the following steps:

(1) Determine as soon as possible, even prior to the time that there is any payment problem, whether a private payment bond exists on the project; and

(2) If a private payment bond does exist, obtain a copy of the bond as soon as possible to determine (a) who is entitled to make a claim, and (b) what needs to be done and what procedures need to be followed in order to make a claim.

** **NOTE**: A copy of the private payment bond, if any, can usually be obtained from the project architect/engineer.*

4. Missouri Private Prompt Payment Act

a. Introduction

In 1995, Missouri enacted private prompt payment act legislation requiring that "all persons who enter into contracts for private design or construction work after August 28th, 1995, shall make all scheduled payments pursuant to the terms of the contract. (§431.180.1,R.S.Mo.).

b. Failure to make scheduled payments pursuant to the contract subjects the violator to an award of interest on the scheduled payment of 1-1/2% per month from the date the payment was due under the contract, and a reasonable attorneys' fees to the prevailing party.

c. The act does not apply to owner occupied residential property of four (4) units or less.

d. The act does include contracts for design, construction, demolition, excavation, surveying, planning and management services.

5. Missouri Private Retainage Statute

a. Introduction

All private construction contracts except those concerning residential construction consisting of four or fewer units (including contracts for reconstruction, maintenance, alteration or repair) entered into after July 11, 2002, and controlled by Missouri law are subject to Missouri's retainage statutes. (§§436.300-436.336, R.S.Mo.).

Contract terms inconsistent with the statutes are unenforceable.

b. Failure to Comply

Penalties for non-compliance with statutes are an award of interest at the rate

of 1-1/2% per month from the date of improper withholding of retainage plus reasonable attorneys' fees. (§436.333, R.S.Mo.). [Unlike the Public Prompt Payment Act (see below), a claimant need not show lack of good faith by the withholding party.]

c. Amount of Retainage

The maximum amount of retainage that can be withheld from a progress payment is 10% unless performance is not in accordance with the terms of the contract. (§436.303, R.S.Mo.). This applies to both owners and general contractors. (§436.315, R.S.Mo.).

d. Trust Funds

Retainage funds are held as trust funds for the benefit of downstream contractors. (§436.303, R.S.Mo.). Owners, general contractors and subcontractors all must comply. (§436.330, R.S.Mo.).

e. Release of Retainage

Within thirty (30) days of substantial completion, an owner must release all retainage, except for an amount equal to 150% of the costs to complete any remaining contract items.

f. Substantial Completion

Substantial completion is defined as the "occurrence of the earlier of the architect or engineer issuing a certificate of substantial completion in accordance with the terms of the contract documents or the owner accepting the performance of the full contract." (§436.327, R.S.Mo.).

g. Early Completion

Prior to substantial completion, an owner may be obligated to release retainage for "early completion" subcontractors. A subcontractor (through the prime contractor) may request payment from the owner of the pro rata share of retainage prior to substantial completion of the entire project "if it is determined that the subcontractor's performance has been satisfactorily completed and the subcontractor can be released prior to substantial completion of the entire project without risk to the owner involving the subcontractor's work." The payment is to be made as part of the next billing cycle. (§436.321, R.S.Mo.).

h. Ratable Share of Retainage

Prime contractors must pay to each subcontractor the subcontractor's ratable share of retainage as released by the owner. (§436.318, R.S.Mo.). The same is true for subcontractors as to their lower tier subcontractors. (§426.330, R.S.Mo.).

i. Substitute Security

Subcontractors and contractors may each tender "acceptable substitute security" to be held in lieu of retainage. (§436.306 and §436.309, R.S.Mo.). A prime contractor must tender a subcontractor's substitute security to the owner. No retainage may be withheld if substitute security is tendered. Acceptable substitute security can be:

(1) A certificate of deposit in the amount of the retainage held.

(2) A retainage bond.

(3) An irrevocable letter of credit.

B. PUBLIC CONSTRUCTION PROJECTS IN MISSOURI

1. Missouri Public Works Bonds

a. Introduction

Missouri law does not permit the filing of mechanic's liens against public works projects. Instead, Missouri law requires the prime contractor and its surety to provide **payment bonds**, guaranteeing payment to subcontractors, suppliers and materialmen who have furnished labor and/or materials on the project.

b. Applicable Projects

All contracts for public works of any kind to be performed for the State, or for any county, city, town, township, school or road district in the State.

c. Who Can Make a Claim?

Any person furnishing labor, equipment, materials or supplies, used or consumed in connection with the construction of the public work, **under an agreement with the prime contractor or a subcontractor**. [Missouri law is unclear whether this includes lower tier subcontractors as well.]

d. Notice Requirements

The Missouri statutes do not set forth any notice requirements for claims against public works bonds. Therefore, the **specific language of the bond will control**. Missouri public works bonds typically require a claimant who did not contract directly with the prime contractor to furnish notice, usually within ninety days, to the prime contractor, the owner and the surety in order to preserve a bond claim. Missouri courts enforce such notice provisions.

e. Suit on the Bond

Missouri law prohibits a "private" statute of limitations contained in a bond which attempts to limit the time period in which suit may be filed against the bond to a period less than that for contracts generally. (§431.030, R.S.Mo.). Instead, the general contract statute of limitations (**five years**) applies, and suit must be brought within five years of the accrual of the claimant's right of action against the bond.

**NOTE: §522.300, R.S.Mo. requires the claimant to file a copy of the bond, certified by the party in charge of the bond, with the action filed to recover on the bond.*

2. Missouri Public Prompt Payment Act

a. Introduction

In 1990, Missouri enacted public prompt payment legislation, setting forth **time limits for payment and penalties for late payment** on contracts for all public works projects. (§34.057, R.S.Mo.). All such contracts are required to provide for prompt payment by the public owner to the contractor, and prompt payment by the contractor to its subcontractors and material suppliers.

b. Applicable Projects

All public works projects of the State, or any county, city or other political subdivision of the State, **except** the Missouri Highway and Transportation Department.

c. Payments from Owner to Prime Contractor

* Except in the case of a lump sum prime contract, a public owner is required to make progress payments to the prime contractor at least **once a month**

based on the progress of the work.

* If payment is not made within thirty days, the owner shall pay the prime contractor **interest** at the rate of 1½% per month from the expiration of the thirty-day period until payment in full is made, unless such payments are withheld in good faith for reasonable cause.

d. Payments from Prime Contractor to Subcontractor

* Subcontractors and material suppliers are entitled to be paid by the prime contractor within **fifteen days** after the prime contractor receives payment from the public owner.

* Payments which are late without reasonable cause shall bear **interest** at the rate of 1½% per month, calculated from the expiration of the fifteen-day period, until fully paid.

e. Payment from Subcontractor to Sub-Subcontractor

* A subcontractor is likewise required to pay its sub-subcontractors and material suppliers within **fifteen days** after the subcontractor is paid by the general contractor.

* Payments which are late without reasonable cause shall bear **interest** at the rate of 1½% per month, calculated from the expiration of the fifteen-day period, until fully paid.

f. Limits on Retention

For contracts which provide for payments to the prime contractor based on its applications for payment, retainage shall not exceed 5% of the value of the contract (or subcontract) unless the public owner and the architect/engineer determine that a higher rate of retainage is required to ensure performance, but in no event shall retainage exceed 10% of the value of the contract (or subcontract).

**__NOTE__: A subcontractor whose work is entirely completed may be paid all of his retainage without having to wait for the completion of the entire project.*

**__NOTE__: A prime contractor cannot withhold more retainage from his subcontractors than the owner is withholding from the prime contractor.*

NOTICE TO OWNER

FAILURE OF THIS CONTRACTOR TO PAY THOSE PERSONS SUPPLYING MATERIALS OR SERVICES TO COMPLETE THIS CONTRACT CAN RESULT IN THE FILING OF A MECHANIC'S LIEN ON THE PROPERTY WHICH IS THE SUBJECT OF THIS CONTRACT PURSUANT TO CHAPTER 429, R.S.MO. TO AVOID THIS RESULT YOU MAY ASK THIS CONTRACTOR FOR "LIEN WAIVERS" FROM ALL PERSONS SUPPLYING MATERIAL OR SERVICES FOR THE WORK DESCRIBED IN THIS CONTRACT. FAILURE TO SECURE LIEN WAIVERS MAY RESULT IN YOUR PAYING FOR LABOR AND MATERIAL TWICE.

FORM M(1)

CONTRACTOR'S STATEMENT OF MECHANIC'S LIEN

NOW on this _____ day of _____, 20____, comes [**Name of Contractor/Claimant**] (hereinafter "Claimant"), and with a view to avail itself of the benefits of the Missouri statutes relating to liens for labor and materials, files this Statement of Mechanic's Lien and the account set forth below for the work, labor, equipment, materials and supplies furnished, performed and rendered by Claimant at the instance and request and under one certain contract with **[Name of Owner]**, for the construction of **[description of construction project]** and other improvements related thereto upon and in connection with the real property situated in the County of _____, State of Missouri, and described as follows:

[Legal Description of Real Property]

All for the immediate use, enjoyment and benefit of the aforesaid owner of said real property.

Claimant, as original contractor, files this claim and the account set forth below in order that it may constitute a lien upon said real property and materials, fixtures, trade fixtures, engines, boilers, pumps, belting, pullies, shafting, machinery, improvements and every other right, title and interest in said property. Such account and claim, after all proper deductions and setoffs, is in the total sum of $_____, all as more particularly itemized in detail in the statement attached hereto as Exhibit "A" and made a part hereof as if fully set forth.

The date of the furnishing of the first item of labor, equipment, materials, supplies, services, machinery and tools by Claimant was _____, 20_____, and the date that the last item thereof was furnished and performed by Claimant was _____, 20____.

[Name of Claimant]

By:_____

Its:_____

VERIFICATION

STATE OF _____)
) ss.
COUNTY OF _____)

[**Name of Person Signing**], of lawful age, being first duly sworn, states on his oath that he is the [**Title**] of [**Name of Claimant**] and is duly authorized to make this verification on its behalf, and that the above and foregoing Statement of Mechanic's Lien is true and correct and is a just and true account of the demand and the amount due it for labor, materials, equipment, supplies, services, machinery and tools furnished and performed by [**Name of Claimant**] for improvements upon and to the above-described real property pursuant to its contract with, and at the instance and request of [**Name of Owner**], for itself and as agent for and on behalf of, and for the immediate use, enjoyment and benefit of, the aforesaid owner thereof.

_____

Subscribed and sworn to before me this _____ day of _____, 20____.

_____
Notary Public

My Commission Expires:

_____

FORM M(2)

NOTICE OF CLAIM OF MECHANIC'S LIEN

TO: **[Name and Address of Owner(s)]**

TAKE NOTICE AND BE ADVISED that [**Name and Address of Claimant**] holds a claim against the fee simple and/or leasehold estates, buildings, appurtenances, improvements, machinery and equipment located and situated upon real property in the County of _____, State of Missouri, commonly known and described as [**common name and street address of project**], and particularly described as follows:

[**LEGAL DESCRIPTION OF REAL PROPERTY**]

for work performed and labor done, and materials furnished on and to the same by [**Name of Claimant**] under its contract with [**Name of person to whom labor/materials furnished**], the owner's contractor and agent, for making the improvements on the above-described premises. Said total claim amounts to $_____ and the same is due and owing to [**Name of Claimant**] from said [**Name of person to whom labor/materials furnished**], and accrued within six (6) months prior to the giving of this notice.

TAKE FURTHER NOTICE that, unless you pay the same within ten (10) days from the date of service of this notice upon you, [**Name of Claimant**] will file its mechanic's lien in the amount of the aforesaid claim against the fee simple and/or leasehold estates and the other interests and estates owned by you in the above-described premises and said buildings, appurtenances, improvements, machinery and equipment, and will proceed with such lien or liens according to law.

Dated at _____ County, State of Missouri, this _____ day of _____, 20___.

[Name of Claimant]

By:_____

Its:_____

FORM M(3)

RETURN OF SERVICE

I, _____, hereby certify that on the _____ day of _____, 20____, I served the within notice of claim of mechanic's lien on [**Name of Owner**] by delivering a true and correct copy thereof to _____.

_____

Subscribed and sworn to before me this _____ day of _____, 20_____.

_____
Notary Public

My Commission Expires:

SUBCONTRACTOR'S STATEMENT OF MECHANIC'S LIEN

NOW on this _____ day of _____, 20____, comes [**Name of Claimant**] (hereinafter "Claimant"), and with a view to avail itself of the benefits of the Missouri statutes relating to liens for labor and materials, files this Statement of Mechanic's Lien and the account set forth below for the work, labor, equipment, materials and supplies furnished, performed and rendered by Claimant at the instance and request and under one certain contract with **[Name of Person to whom labor/materials furnished]**, for itself as and/or as agent for the original contractor, and as agent for and on behalf of **[Name of Owner],** as Owner, for the construction of **[description of construction project]** and other improvements related thereto upon and in connection with the real property situated in the County of _____, State of Missouri, and described as follows:

[Legal Description of Real Property]

All for the immediate use, enjoyment and benefit of the aforesaid owner of said real property.

Claimant, as subcontractor, files this claim and the account set forth below in order that it may constitute a lien upon said real property and materials, fixtures, trade fixtures, engines, boilers, pumps, belting, pullies, shafting, machinery, improvements and every other right, title and interest in said property. Such account and claim, after all proper deductions and setoffs, is in the total sum of $_____, all as more particularly itemized in detail in the statement attached hereto as Exhibit "A" and made a part hereof as if fully set forth.

The date of the furnishing of the first item of labor, equipment, materials, supplies, services, machinery and tools by Claimant was _____, 20_____, and the date that the last item thereof was furnished and performed by Claimant was _____, 20____.

[Name of Claimant]

By:_____

Its:_____

VERIFICATION

STATE OF _____)
) ss.
COUNTY OF _____)

[**Name of Person signing**], of lawful age, being first duly sworn, states on his oath that he is the [**Title**] of [**Name of Claimant**] and is duly authorized to make this verification on its behalf, and that the above and foregoing Statement of Mechanic's Lien is true and correct and is a just and true account of the demand and the amount due it for labor, materials, equipment, supplies, services, machinery and tools furnished and performed by [**Name of Claimant**] for improvements upon and to the above-described real property pursuant to its contract with, and at the instance and request of [**Name of Person to whom Labor/Materials furnished**], for itself and as agent for the original contractor, and as agent for and on behalf of, and for the immediate use, enjoyment and benefit of, the aforesaid owner thereof.

_____

Subscribed and sworn to before me this _____ day of _____, 20____.

_____
Notary Public

My Commission Expires:

_____

FORM M(4)

CONSENT OF OWNER

CONSENT IS HEREBY GIVEN FOR FILING OF MECHANIC'S LIENS BY ANY PERSON WHO SUPPLIES MATERIALS OR SERVICES FOR THE WORK DESCRIBED IN THIS CONTRACT ON THE PROPERTY ON WHICH IT IS LOCATED IF HE IS NOT PAID.

II. KANSAS CONSTRUCTION PROJECTS

A. PRIVATE CONSTRUCTION PROJECTS IN KANSAS

1. Kansas Mechanic's Liens: Prime Contractor

a. Who Can Claim a Lien?

Any person furnishing labor, equipment, material, or supplies used or consumed for the improvement of real property, and for the cost of transporting the same, under a contract with the owner or with the trustee, agent or spouse of the owner. (K.S.A. §60-1101).

(1) Improvement of Real Property

Improvement means a valuable addition or amelioration in its condition, amounting to more than mere repairs or replacement, costing, labor or capital, and intended to enhance its value, beauty, or utility to adapt it for new or further purposes.

(2) Furnished at the Site

The improvement must be "visibly" furnished at the site.

(3) Earliest Unsatisfied Lien

If there are multiple liens filed, all liens are preferred to the earliest unsatisfied lien of any of them. If an earlier unsatisfied lien is paid in full or otherwise discharged, the commencement date of all claimants shall be the date of the next earliest unsatisfied lien. (2005)

(4) Signs or Stakes

Placement of signs or survey stakes shall not constitute visible furnishing.

b. The Lien Statement

Any person claiming a lien on real property as a prime contractor must file a **lien statement**. (K.S.A. §60-1102).

(1) When must the lien statement be filed?

* Within **four (4) months** after the date material, equipment or supplies, used or consumed, was last furnished or last performed

under the contract. The date cannot be extended by gratuitous services that are beyond the scope of the original contract.

(a) Effective July 1, 2003, a general contractor can extend the period to **five (5) months** providing a notice of extension is filed within four (4) months of last work. (K.S.A. §1102(c)).

[SEE FORM K(1)

(2) Where must the lien statement be filed?

* With the **clerk of the district court** of the county in which the property is located.

(3) What must the lien statement contain?

* The lien statement must contain a **verified** statement showing:

(a) The name of the owner;

(b) The name of the claimant;

(c) The legal description of the real property; and

(d) A reasonably **itemized statement** and the **amount** of the claim (but if the amount of the claim is evidenced by a written instrument, or if a promissory note has been given for the same, a copy thereof may be attached in lieu of the itemized statement). The statement must be sufficient to allow the owner to ascertain whether the labor and material was furnished and the charges fair from the four corners of the lien itself.

**NOTE: Supporting documents, such as unpaid invoices or pay requests, records of unpaid materials delivered to the site and labor records, should be attached to itemized statement.*

(e) A mechanic's lien statement may be amended by leave of court and in the furtherance of justice as long as the lien amount is not increased. (K.S.A. §60-1105(b)).

[SEE FORM K(2)]

c. Suit to Foreclose the Lien

An action to foreclose a lien shall be brought within **one (1) year** from the time of filing the lien statement.

All other lien claimants and those with encumbrances of record are to be joined into the lawsuit except for encumbrances that have priority over the lien. (2005)

* ***Note****: If a promissory note has been attached to the lien statement in lieu of an itemized statement, the action must be commenced within one year from the maturity of the note.*

2. Kansas Mechanic's Liens: Subcontractor/Supplier

a. Who Can Claim a Lien?

Any supplier, subcontractor or other person furnishing labor, equipment, material or supplies, used or consumed at the site of the property subject to the lien, under an agreement with the contractor, subcontractor or owner-contractor. (K.S.A. §60-1103(a)) [Only those contracting with a first tier subcontractor may claim a lien.]

* ***Note****: "Owner-Contractor" is defined as the fee title owner of the subject real estate, who enters into contracts with more than one person, firm or corporation for labor, equipment, material or supplies used or consumed for the improvement of such real property.*

* ***Note****: Claimant must have direct contractual relationship with the contractor or a subcontractor (e.g., a supplier to a supplier to a subcontractor cannot assert a mechanic's lien).*

b. The Lien Statement

Any person claiming a lien on real property as a subcontractor/supplier must file a **lien statement**.

(1) When must lien statement be filed?

*Within **three (3) months** after the date the labor and/or materials were last furnished by claimant.

(a) Effective July 1, 2003, a subcontractor can extend the period to **five (5) months** providing a notice of extension is filed within three (3) months of last work. (K.S.A. §60-1103(e)).

[**SEE FORM K(3)]**

(2) Where must lien statement be filed?

*With the **clerk of the district court** of the county in which the property is located.

(3) What must the lien statement contain?

*The lien statement must contain a **verified** statement showing:

(a) The name of the owner;

(b) The name of the prime contractor;

(c) The name of the claimant;

(d) The legal description of the real property; and

(e) A reasonably **itemized statement** and the **amount** of the claim (but if the amount of the claim is evidenced by a written instrument, or if a promissory note has been given for the same, a copy thereof may be attached in lieu of the itemized statement).

**NOTE: Supporting documents, such as unpaid invoices or pay requests, records of unpaid materials delivered to the site and labor records, should be attached to itemized statement.*

[SEE FORM K(4)]

c. Notice Requirements

The claimant must:

(1) Cause a copy of the lien statement to be **served personally** upon any one owner and any party obligated to pay the lien in the manner provided for service of process generally, **or**

(2) Mail a copy of the lien statement to any one owner of the property and to any party obligated to pay the same by **restricted** mail, **or**

(3) If the address of any one owner or such party is unknown and cannot be ascertained with reasonable diligence, **post a copy** of the lien statement in a conspicuous place on the premises.

d. Suit to Foreclose the Lien

An action to foreclose a lien must be brought within **one (1) year** from the time of filing the lien statement.

* ***Note****: If a promissory note has been attached to the lien statement in lieu of an itemized statement, the action shall be commenced within one year from the maturity of the note.*

e. Special Rules: Improvement of Residential Property

A lien for the furnishing of labor, equipment, materials or supplies for the **improvement of residential property** may be claimed by a subcontractor/supplier **only** if the subcontractor/supplier has (1) mailed to any one of the owners of the property a **warning statement**, or (2) in its possession a copy of a **statement** signed and dated by any one owner of the property stating that the prime contractor or the claimant had given the warning statement to one such owner of the property.

(1) What constitutes "improvement of residential property"?

*Improvement of a pre-existing structure in which the owner resides at the time the claimant first furnishes labor, equipment, materials or supplies and which is not used or intended for use as a residence for more than two families or for commercial purposes, or improvement or construction of any addition, garage, fence, swimming pool, out building or other improvement appurtenant to such a structure; **or**

*Any construction upon real property which is owned or acquired by an individual at the time the claimant first furnishes labor, equipment, material or supplies, and which is intended to become and does become the principal personal residence of that individual upon completion, and which is not used or intended for use as a residence for more than two families or for commercial purposes.

(2) When must the warning statement be given?

* Prior to the filing of the claimant's lien statement.

(3) What must the warning statement contain?

[SEE FORM K(5)]

(4) Inclusion in the lien statement

* There must be attached to the lien statement the **affidavit** of the subcontractor/supplier that the warning statement was properly given.

f. Special Rules: New Residential Property

A lien for the furnishing of labor, equipment, materials or supplies for the construction of new residential property may be claimed by the subcontractor/supplier after the passage of title to such new residential property to a good faith purchaser for value only if the claimant has filed a **notice of intent to perform** prior to the recording of the deed passing title to such new residential property. (K.S.A. §60-1103(b))

(1) What constitutes "new residential property"?

* A new structure which is constructed for use as a residence and which is not used or intended for use as a residence for more than two families or for commercial purposes ("new residential property" does **not** include any improvement of a pre-existing structure or construction of any addition, garage or out building appurtenant to a pre-existing structure).

(2) When must the notice be filed?

* As soon as possible, but in any event prior to the filing of the lien statement.

(3) Where must the notice be filed?

* In the office of the clerk of the district court of the county where the property is located.

(4) What must the notice contain?

[SEE FORM K(6)]

(5) Service

The lien shall be served personally upon any one owner any holder of a recorded equitable interest and any party obligated to pay the lien.

g. Special Rules – Leased Property

If a lien arises due to work for a lessee, the lien can attach only to the leasehold interest, not the real estate or fee interest.

An exception to the rule exists where the lease allows improvements to be made on the property and that the expenses of the improvements are deducted from the rentals.

A tenant cannot charge a landlord's estate with a lien absent the landlord's authority or consent or the tenant acting as the landlord's agent or trustee or the landlord's acquiescence in the improvements. The landlord's knowledge that improvements are being made is not sufficient to charge a lien nor is the landlord's agreement to permit the improvements.

h. Fraudulent Liens

Any owner or debtor who believes that a fraudulent lien statement has been filed may file with the court a motion for judicial review of the status of the documentation purporting to create the lien. The motion shall be filed by the movant or its attorney and supported by an affidavit setting forth a concise statement of the facts upon which the claim of fraud is made. (2005)

i. Assignment

Lien claims and rights of action upon liens are assignable in Kansas.

j. Amendment of Lien

A lien statement may be amended by leave of court in furtherance of justice except to increase the amount claimed.

3. Mechanic's Lien Discharge Bond

Under K.S.A. §60-1110, a contractor or owner may execute a bond **to the State of Kansas** for the use of all persons in whose favor liens might accrue by virtue of the Kansas Mechanic's Lien Law.

The bond shall be conditioned upon payment of all claims which might be the basis of a lien.

The amount of the bond penalty shall be not less than the contract price.

In the alternative, Kansas amended its law in 2005 to provide also that a bond may be executed to any person claiming a lien which is disputed by the owner or contractor, conditioned for the payment of such claim in the amount thereof. (2005)

[SEE FORMS K(7), K(8),K(9) AND K(10)]

Table 2: Summary of General Rules - Kansas Mechanic's Liens

	Provide Warning Statement to Owner	File Notice of Intent to Perform	File Lien Statement[1,2]	File Suit to Foreclose Lien
Prime Contractor	None Required	None Required	File within 4 months after last day labor/ materials furnished by claimant (unless extended to 5 months)	File within 1 year of filing lien statement
Subcontractor/Supplier: Non-residential Construction	None Required	None Required	File within 3 months after last day labor/materials furnished by claimant (unless extended to 5 months)	File within 1 year of filing lien statement
Subcontractor/Supplier: Improvement of Residential Property	Mail to Property Owner as soon as possible, and prior to filing lien statement	None Required	File within 3 months after last day labor/ materials furnished by claimant[3]	File within 1 year of filing lien statement
Subcontractor/Supplier: New Residential Property	None Required	File as soon as possible, and prior to filing lien state-ment[2]	File within 3 months after last day labor/ materials furnished by claimant	File within 1 year of filing lien statement

- - - - - - - - - - -

1. Subcontractors/Suppliers must also serve copy of lien statement upon Owner, Prime Contractor and upon person to whom labor/materials were furnished.

2. File with clerk of District Court for county in which property located.

3. Lien statement must also include affidavit of subcontractor/supplier that warning statement was properly given.

3. Private Payment Bonds

a. Introduction

On private construction projects, owners sometimes require general contractors to provide **payment bonds**, guaranteeing payment to subcontractors/suppliers, to protect the owner from mechanic's liens.

b. Who Can Make a claim?

Most private payment bonds **specifically define** who will be entitled to make a claim against the bond (e.g., payment bonds typically limit the class of "claimants" to those who furnish labor and/or materials directly to the prime contractor or directly to one of his "first tier" subcontractors).

**Note: Occasionally, prime contractors will require those subcontractors performing major portions of the work to likewise furnish payment bonds.*

c. Notice Requirements

Private payment bonds typically require a claimant who did not contract directly with the prime contractor to furnish notice, usually within ninety days, to the prime contractor, the owner and the surety in order to preserve a bond claim.

d. Suit on the Bond

Many private payment bonds contain a "private" statute of limitations, indicating a limited period in which suit may be filed against the bond (e.g., within one year following the date on which the prime contractor ceased its work on the contract). Kansas courts may uphold such "private" statutes of limitations.

**Note: Many private payment bonds also include a forum selection provision, which specifies where the suit on the bond must be filed.*

e. Recommendations

Recovery under a private payment bond usually depends upon the specific language of the payment bond. Accordingly, subcontractors and suppliers can protect themselves by taking the following steps:

(1) Determine as soon as possible, even prior to the time that there is any payment problem, whether a private payment bond exists on the

project; and

(2) If a private payment bond does exist, obtain a copy of the bond as soon as possible to determine (a) who is entitled to make a claim, and (b) what needs to be done and what procedures need to be followed in order to make a claim.

**__Note__: A copy of the private payment bond, if any, can usually be obtained from the project architect/engineer.*

4. Kansas Fairness in "Private" Construction Contract Act

Effective July 1, 2005, Kansas enacted the following requirements (which do not apply to single family residential housing and multi-family residential housing of 4 units or less or to public works projects). (K.S.A. §16-1801, *et seq.*).

a. Payments

All payments must be made pursuant to the terms of the contract.

b. Contingent Payment Clauses

Contingent payment clauses do not provide a defense to the filing of a mechanic's lien.

c. When Payments Made to Contractor

Owners must make payments to a contractor (except retainage) within thirty (30) days after receipt of a timely, properly completed, undisputed request for payment. Interest at the rate of 18% per annum shall accrue for non-payment beginning on the 31st day after receipt of request.

d. When Payments Made to Subcontractor

Contractors shall pay subcontractors within seven (7) days after receipt of payment form the owner (including retainage, if released by the owner) upon receipt of a timely, properly completed undisputed request for payment. Interest at the rate of 18% per annum shall accrue for non-payment beginning on the 8th day after receipt of request

e. Retainage

Ten per cent (10%) of payment amount is the maximum retainage that may be withheld.

f. Interest

Interest at the rate of 18% per annum shall be paid for all retainage not paid when due.

g. What if non-payment occurs?

Contractors and subcontractors who are not paid undisputed payments within seven (7) days form date due may suspend performance upon seven (7) days notice and contract performance time shall be extended and payments made for reasonable costs of demobilization, delay, and remobilization.

h. Costs to enforce the law

In any action to enforce the law, costs and reasonable attorneys' fees may be awarded.

i. Waiver

The provisions of the Act cannot be waived.

j. Right to litigate

The right to litigate claims cannot be waived.

k. Right to file mechanic's lien

The right to file a mechanic's lien cannot be waived.

l. Subrogation rights

Subrogation rights cannot be waived.

B. PUBLIC CONSTRUCTION PROJECTS IN KANSAS

1. Kansas Public Works Bonds

a. Introduction

Kansas law does not permit the filing of mechanic's liens against public works projects. Instead, Kansas law requires the prime contractor and its surety to provide payment bonds, guaranteeing payment to subcontractors,

suppliers and materialmen who have furnished labor and/or materials on the project where the prime contract sum exceeds $100,000.

b. Applicable Projects

K.S.A. §60-1111 requires the prime contractor to provide a **payment bond** on any Kansas public works project where:

(1) The prime contract exceeds the sum of **$100,000** in amount; and

(2) The prime contract is for the purpose of making any **public improvements**, or constructing any **public building** or making **repairs** on the same.

c. Who Can Make a Claim?

Any person furnishing labor, equipment, material or supplies, used or consumed in connection with or in or about the construction of the public building or in making the public improvements, **under an agreement with the prime contractor or a subcontractor**.

* ***NOTE****: Claimant must have direct contractual relationship with the contractor or a subcontractor (e.g., a supplier to a supplier to a subcontractor cannot assert a bond claim).*

d. Suit on the Bond

Any person to whom there is due any sum for labor and material furnished may bring an action on the bond for recovery of such indebtedness, but no action shall be brought on the bond after **six (6) months** from the completion of the public improvements or public buildings.

e. Capital Improvement Projects

A Certificate of Deposit is authorized for state capital improvement projects in lieu of a surety bond. (K.S.A. §60-1112)

NOTICE OF EXTENSION TO FILE CONTRACTOR LIEN

(K.S.A. §60-1102(c))

Name of Contractor: _____

Address of Contractor: _____

Telephone Number of Contractor: _____

Name and/or Number of Job: _____

Address of Job Site: _____

The last day upon which said work, labor and materials were performed or supplied was _____, 20___.

Filing of such notice extends the time for filing a lien to five (5) months for the above contractor providing materials or labor on property owned by:

Owner's Name (if known): _____

Owner's Address (if known): _____

_____

DATED this _____ day of _____, 20___.

[Name of Contractor]

By:_____

Its:_____

STATEMENT OF CONTRACTOR FOR MECHANIC'S LIEN

(K.S.A. §60-1102)

AMOUNT OF CLAIM: [Dollar Amount of Claim]

NAME OF OWNER: [Name and Address of Owner]

NAME OF CONTRACTOR/CLAIMANT: [Name and Address of Claimant]

DESCRIPTION OF REAL PROPERTY: [Legal Description of Property]

The undersigned, [Name of Claimant], as original contractor, claims a lien upon the above-described real property on account of furnishing [Description of Labor/Materials Furnished], all as more fully and particularly itemized in detail in the statement attached hereto as Exhibit "A" and made a part hereof as if fully set forth, which was by said contractor performed and furnished for and was applied to, used and consumed in the construction of [Description of Improvements] on said real property, pursuant to a contract with [Name of Owner], acting in its own right and as the agent for and on behalf of the Owner of said real property.

The aforesaid claim, a reasonably itemized statement of which is attached hereto as Exhibit "A", is filed in order that it may constitute a lien upon the above-described real property, and every other right, title and interest in said real property.

The date upon which the aforesaid labor and/or materials were last furnished and performed by Claimant was _____, 20__.

WITNESS the hand of said Claimant this ___ day of _____, 20__.

[Name of Claimant]

By: _____

Its: _____

VERIFICATION

STATE OF _____)
) ss.
COUNTY OF _____)

[Name of Person Signing], of lawful age, being first duly sworn, states upon his [her] oath that he [she] is the [Title] of [Name of Claimant], and is duly authorized to make this verification on its behalf; and that the above and foregoing statement is true and correct and is a just and true account of the demand of and the amount due Claimant.

_____

Subscribed and sworn to before me, a Notary Public, this ___ day of _____, 20__.

_____
Notary Public

My Commission Expires:

_____

FORM K(2)

NOTICE OF EXTENSION TO FILE SUBCONTRACTOR LIEN

(K.S.A. §60-1103(e))

Name of Subcontractor or Supplier:
_____

Address of Subcontractor or Supplier:
_____

Telephone Number of Subcontractor or Supplier:
_____

Name of Contractor:
_____

Address of Contractor:
_____

Telephone Number of Contractor:
_____

Name and/or Number of Job:
_____

Address of Job Site:
_____

The last day upon which said work, labor and materials were performed or supplied was _____, 20___.

Filing of such notice extends the time for filing a lien to five (5) months for the above contractor providing materials or labor on property owned by:

Owner's Name (if known):
_____

Owner's Address (if known):
_____

_____

DATED this _____ day of _____, 20___.

[Name of Subcontractor or Supplier]

By:____

Its:____

FORM K(3)

STATEMENT OF SUBCONTRACTOR/MATERIALMAN FOR MECHANIC'S LIEN

(K.S.A. §60-1103)

AMOUNT OF CLAIM: [Dollar Amount of Claim]

NAME OF OWNER: [Name and Address of Owner]

NAME OF CONTRACTOR: [Name and Address of Prime Contractor]

NAME OF CLAIMANT: [Name and Address of Claimant]

DESCRIPTION OF REAL PROPERTY: [Legal Description of Property]

The undersigned, [Name of Claimant], as subcontractor/materialman, claims a lien upon the above-described real property on account of furnishing [Description of Labor/Materials Furnished], all as more fully and particularly itemized in detail in the statement attached hereto as Exhibit "A" and made a part hereof as if fully set forth, which was by said subcontractor/materialman performed and furnished for and was applied to, used and consumed in the construction of [Description of Improvements] on said real property, pursuant to a contract with [Name of Person to Whom Labor/Materials Furnished], acting in its own right and as the agent for and on behalf of the original contractor.

The aforesaid claim, a reasonably itemized statement of which is attached hereto as Exhibit "A", is filed in order that it may constitute a lien upon the above-described real property, and every other right, title and interest in said real property.

The date upon which the aforesaid labor and/or materials were last furnished and performed by Claimant was _____, 20__.

WITNESS the hand of said Claimant this ___ day of _____, 20__.

[Name of Claimant]

By: _____

Its: _____

VERIFICATION

STATE OF _____)
) ss.
COUNTY OF _____)

[Name of Person Signing], of lawful age, being first duly sworn, states upon his [her] oath that he [she] is the [Title] of [Name of Claimant], and is duly authorized to make this verification on its behalf; and that the above and foregoing statement is true and correct and is a just and true account of the demand of and the amount due Claimant.

_____

Subscribed and sworn to before me, a Notary Public, this __ day of _____, 20__.

_____
Notary Public

My Commission Expires:

_____

FORM K(4)

WARNING STATEMENT

NOTICE TO OWNER: **[Name of Supplier or Subcontractor]** is a supplier or subcontractor providing materials or labor on Job No. _____ at **[Residence Address]** under an agreement with **[Name of Prime Contractor]**. Kansas law will allow this supplier or subcontractor to file a lien against your property for materials or labor not paid for by your contractor unless you have a waiver of lien signed by this supplier or subcontractor. If you receive a notice of filing of a lien statement by this supplier or subcontractor, you may withhold from your contract the amount claimed until the dispute is settled.

[Name of Party Furnishing Labor and/or Materials]
Subcontractor/Supplier

By: _____

[Address of Subcontractor/Supplier]

FORM K(5)

NOTICE OF INTENT TO PERFORM

The undersigned, **[Name and Address of Subcontractor/Supplier]**, do hereby give public notice that I am a supplier, subcontractor or contractor or other person providing materials and/or labor on the property owned by **[Name of Property Owner]** and having the legal description as follows: **[Insert Legal Description of Real Property]**.

[Name of Party Furnishing Labor and/or Materials]
Subcontractor/Supplier

By: _____

[Address of Subcontractor/Supplier]

FORM K(6)

IN THE DISTRICT COURT OF _____ COUNTY, KANSAS
CIVIL COURT DEPARTMENT

[Name of Subcontractor], Subcontractor,	)	
Plaintiff,	)	Mechanic's Lien Statement and Case No. [Lien Number]
vs.	)	
[Name of Owner], Owner	)	
[Name of General Contractor], General Contractor,	)	
Defendants.	)	

MOTION TO APPROVE THE STATUTORY BOND, TO DISCHARGE LIEN, AND TRANSFER OF LIEN CLAIM TO THE BOND

COMES NOW Defendant,_____ ("_____"), and hereby moves this Court, pursuant to K.S.A. §60-1110, to: (a) approve Statutory Mechanic's Lien Release Bond # _____ ("Bond") in the penal sum of $_____, (b) to order that the Bond be filed with the Clerk of the District Court, (c) to discharge Mechanic's Lien No. _____ ("Lien"), and (d) to transfer the lien claim to the Bond.

WHEREFORE, Defendant _____ prays this Court for its Order to: (a) approve the Statutory Mechanic's Lien Release Bond in the penal sum of $_____, (b) to order that the Bond be filed with the Clerk of the District Court, (c) to discharge Mechanic's Lien No. _____, and (d) to transfer the lien claim to the Bond.

FORM K(7)

Respectfully submitted**,**

BROWN & DUNN, P.C.

By_____
G. Steven Ruprecht Bar #_____
sruprecht@browndunn.com
911 Main Street, Suite 2300
Kansas City, MO 64105
(816) 292-7000 Telephone
(816) 292-7050 Facsimile

ATTORNEYS FOR DEFENDANT
[Name of Defendant Contractor]

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was mailed via first-class mail, postage prepaid, this _____ day of _____, 20___, to:

[Name of Plaintiff's Attorney]
[Address of Plaintiff's Attorney]

Attorneys for Plaintiff

_____
ATTORNEY FOR DEFENDANT
[Name of Defendant Contractor]

IN THE DISTRICT COURT OF _____ COUNTY, KANSAS
CIVIL COURT DEPARTMENT

[Name of Subcontractor], Subcontractor,	)	
Plaintiff,	)	Mechanic's Lien Statement and Case No. [Lien Number]
vs.	)	
[Name of Owner], Owner	)	
[Name of General Contractor], General Contractor,	)	
Defendants.	)	

SUGGESTIONS IN SUPPORT OF MOTION TO APPROVE THE BOND, TO DISCHARGE LIEN, AND TO TRANSFER THE CLAIM TO THE BOND

COMES NOW Defendant, _____ ("_____"), and for its Suggestions in Support of its Motion to Approve the Statutory Mechanic's Lien Release Bond, to Discharge Lien and Transfer of Lien Claim to the Bond, states as follows:

1. This cause of action concerns real property and improvements, commonly referred to as the "[Name of Project]," with a legal description attached as Exhibit A and incorporated herein by reference.

2. _____ ("_____") is the owner of the Property.

3. On or about _____, 20__, [Owner] and [Contractor] entered into a contract, titled _____ (the "Contract").

FORM K(8)

4. On or about _____, 20__, [Contractor] and

[Subcontractor] ("") entered into a subcontract, pursuant to which [Subcontractor] was to perform [type of work] work in connection with the construction and improvements to the Property (the "Subcontract"). In exchange and consideration for this work, [Contractor] agreed to pay [Subcontractor] $.

5. On , 20, [Subcontractor] filed a Mechanic's Lien Statement No. against the Property for $.

6. Pursuant to [Article number] of the General Conditions to the Contract between [Owner] and [Contractor], if a mechanic's lien is filed against the Property by [Contractor]'s subcontractors, [Contractor] is required to immediately furnish and file a statutory bond in accordance with K.S.A. §60-1110 to discharge any such mechanic's lien.

7. Pursuant to its Contract with the Owner, defendant has executed a Statutory Mechanic's Lien Release Bond in the penal amount of $ representing the Lien claim ($) and 18 months of interest at 10% per annum. Pursuant to K.S.A. §60-1110, [Contractor]'s Bond should be approved and filed by the Court, and the Mechanic's Lien should be discharged. See Statutory Bond No. ; attached as Exhibit B and incorporated herein by reference. If the Lien is discharged, the claim should be transferred to the Bond.

WHEREFORE, Defendant prays this Court for its Order to: (a) approve the Statutory Mechanic's Lien Release Bond No. , (b) to order that the Bond be filed with the Clerk of the District Court, (c) to discharge Mechanic's Lien No. of record, and (d) to transfer the lien claim to the Bond.

Respectfully submitted,

BROWN & DUNN, P.C.

By_____
G. Steven Ruprecht Bar # _____
sruprecht@browndunn.com
911 Main Street, Suite 2300
Kansas City, MO 64105
(816) 292-7000 Telephone
(816) 292-7050 Facsimile

ATTORNEYS FOR DEFENDANT
[Name of Defendant Contractor]

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was mailed via first-class mail, postage prepaid, this _____ day of _____, 20___, to:

[Name of Plaintiff's Attorney]
[Address of Plaintiff's Attorney]

Attorneys for Plaintiff

_____
ATTORNEY FOR DEFENDANT
[Name of Defendant Contractor]

Bond No. _____ Lien No. _____

BOND TO DISCHARGE MECHANIC'S LIEN

CONTRACTOR:

[Name and Address of Contractor]

SURETY:

[Name and Address of Surety]

OWNER:

[Name and Address of Owner]

CLAIMANT:

[Name and Address of Claimant]

KNOW ALL MEN BY THESE PRESENTS, that [Contractor], as Contractor/Principal and [Surety], as Surety, a corporation duly authorized and existing under the laws of the State of _____, are hereby held firmly bound unto the State of Kansas, as Obligee, in the penal sum _____ Dollars and ____ Cents ($_____), lawful money of the United States of America, for the use and benefit of [Claimant], as Claimant. We hereby bind ourselves, our successors, heirs, executors and administrators jointly and severally and firmly by these presents.

WHEREAS, the said above bounden Contractor/Principal has entered into a written contract with the _____ dated _____, 20__ for the [Name of Project], according to its contract documents; and

WHEREAS, in the District Court of _____ County, Kansas, Claimant, _____, filed a Mechanic's Lien Statement No. _____ on _____, 20__, for labor, equipment, materials and supplies for the improvement of the real property legally described as set forth in attached Exhibit A.

WHEREAS, said notice of lien purports to have been made and filed as prescribed in the Lien Law of the State of Kansas pursuant to K.S.A. 60-1103, wherein such Lienor claims a Lien against the above described property, and improvements thereon, for and on account of labor, equipment, materials and supplies furnished for the construction and/or improvement of such property.

FORM K(9)

NOW THEREFORE, with respect to the Owner, State of Kansas and [Claimant], this obligation shall be null and void if [Contractor] makes payment, directly or indirectly, of all sums which [Claimant] is entitled to recover as a mechanic's lien in the above described case within ten (10) days after entry of a final judgment, after all appeals, in favor of [Claimant]. This Bond is intended to serve as a Bond to discharge mechanic's lien pursuant to K.S.A. § 60-1110 and shall be construed consistent with that purpose. Any provision required to conform this Bond for that purpose and Kansas law shall be deemed incorporated herein and Claimant shall not be entitled to recover any sums through this Bond except to the extent Claimant has a right to a mechanic's lien against the fee or the leasehold interest in the property and such lien could have been perfected and enforced if this Bond had not been given.

Witnessed our hands and seals this _____ day of _____, 20____.

_____

_____

CONTRACTOR/PRINCIPAL SURETY

By: _____ By:

_____

Its: _____ Its:

_____

Approved By:

_____

Judge, District Court of _____ County, KS

IN THE DISTRICT COURT OF _____ COUNTY, KANSAS
CIVIL COURT DEPARTMENT

[Name of Subcontractor], Subcontractor,	)	
Plaintiff,	)	Mechanic's Lien Statement and Case No. [Lien Number]
vs.	)	
[Name of Owner], Owner	)	
[Name of General Contractor], General Contractor,	)	
Defendants.	)	

ORDER TO APPROVE THE BOND AND DISCHARGE LIEN

Now on this ___ day of _____, 20__, _____[Defendant Contractor]__ ("____"), by counsel, moved the Court for its Order, pursuant to K.S.A. §60-1110, to approve Statutory Mechanic's Lien Release Bond No. _____ ("Bond"), to order that the Bond be filed with the Clerk of the District Court, to discharge Mechanic's Lien No. _____ ("Lien") filed on _____, 20___, and to transfer the lien claim to the Bond.

The Court, after review of the Bond and statements of counsel, finds that the Bond is duly executed and issued by a good and sufficient surety, that the Clerk of the District Court is ordered to file the Bond, and that Mechanic's Lien No. _____ should be discharged forthwith, and the Court further finds that the lien claim should be transferred to the Bond.

ACCORDINGLY, IT IS SO ORDERED that Statutory Mechanic's Lien Release Bond No. _____ is approved by the Court; that the Clerk of the District Court shall file

FORM K(10)

the Bond of record in the Clerk's office; that Mechanic's Lien No. _____ is discharged of

record; and that plaintiff's lien claim is transferred to the Bond.

IT IS SO ORDERED.

_____ _____

DATE District Court Judge, _____ County, KS

Submitted and Approved By:

BROWN & DUNN, P.C.

_____

G. Steven Ruprecht Bar #_____
sruprecht@browndunn.com
911 Main Street, Suite 2300
Kansas City, MO 64105
(816) 292-7000 Telephone
(816) 292-7050 Facsimile

ATTORNEYS FOR DEFENDANT
[Name of Defendant Contractor]_____

III. FEDERAL CONSTRUCTION PROJECTS

A. Introduction

Public policy does not permit the filing of mechanic's liens against federal construction projects. Accordingly, Congress has adopted the **Miller Act** (40 U.S.C. §270a-d, amended 40 U.S.C. §3131 (2002)), which requires the prime contractor and its surety to provide payment bonds, guaranteeing payment to some -- but not all -- subcontractors, suppliers and materialmen who have furnished labor and/or materials on federal construction projects where the prime contract sum exceeds $100,000.

The amount of the payment bond shall equal the total amount payable by the terms of the contract unless the officer awarding the contract determines that a payment bond in that amount is impractical in which case he shall set the amount of the bond which shall not be less than the amount of the performance bond.

B. Applicable Projects

The Miller Act requires the prime contractor to provide a **payment bond** on any federal construction project where:

1. The prime contract exceeds the sum of **$100,000** in amount; and

2. The prime contract is for the **construction, alteration or repair of any public building or public work**. (40 U.S.C. §270(a); 40 U.S.C. 3131(b))

C. Who Can Make a Payment Bond Claim?

1. Every person who has furnished labor and/or materials in the prosecution of the work provided for in the prime contract, who has not been paid in full before the expiration of the period of **ninety days** after the day on which the last labor and/or materials were furnished or supplied. (40 U.S.C. §270(b) and 40 U.S.C. §3133(b)(1)).

2. Only **two categories** of subcontractors, suppliers and materialmen **can make a claim** on the Miller Act payment bond:

   (a) Those who furnish labor and/or materials **directly to the prime contractor**; and

   (b) Those who furnish labor and/or materials directly **to a subcontractor or supplier that itself has a direct contract** with the prime contractor.

   ***NOTE:** Those who furnish labor and/or materials to one who does **not** have a direct contract with the prime contractor **cannot** make a claim on*

the Miller Act payment bond.

D. <u>Notice Requirements</u>

1. <u>Who Must Give Notice</u>?

   (a) Those who have a **direct contract with the prime contractor** need **not** give a notice of claim on the payment bond.

   (b) Those who do **not** have a direct contractual relationship with the prime contractor, **but** who furnish labor and/or materials under a direct contractual relationship with a subcontractor or supplier who itself has a direct contract with the prime contractor **must** give a notice of claim on the payment bond. (40 U.S.C. §3131(b)(2)).

2. <u>To Whom Must Notice Be Given</u>?

   * Notice of claim must be given to the **prime contractor**.

   **** NOTE:*** *Although not required, the claimant should also give notice of claim to the **surety** who issued the payment bond and to the **subcontractor/supplier** to whom the labor and/or materials were furnished.*

3. <u>When Must Notice Be Given</u>?

   * Within **<u>ninety (90) days</u>** from the date upon which the last labor and/or materials were furnished or supplied by the claimant. (40 U.S.C. §3131(b)(2)).

4. <u>How Must Notice Be Given</u>?

   (a) Notice of claim must be given **in writing**; and

   (b) Notice of claim must be served on the prime contractor by **registered or certified mail**, postage prepaid, addressed to the prime contractor at any place he maintains an office or conducts his business.

5. <u>What Must the Notice Contain</u>?

   (a) Notice of claim must state, with substantial accuracy, **the amount claimed**; and

   (b) By any means that provides written third party verification of delivery to

the contractor at any place the contractor maintains an office or conducts business or at the contractor's residence; and

(c) In any manner in which the United States Marshal of the district in which the public improvement is situated by law may serve summons. (40 U.S.C. §3133(b)(2)(A)and (B)).

[SEE FORM F(1)]

E. Suit on the Bond

1. When Must Suit Be Filed?

* Suit on the payment bond must be filed **within one (1) year** from the date on which the claimant last furnished or supplied labor and/or materials. (40 U.S.C. §3133(b)(4)).

2. Where Must Suit Be Filed?

* Suit on the payment bond must be filed in the **federal district court** in the district **where the prime contract was performed**. (40 U.S.C. §3133(b)(3)(B)).

3. How Must Suit Be Filed?

- Suit on the payment bond must be brought in the name of the United States for the use of the person suing. (40 U.S.C. §3133(b)(3)(A)).

Table 3: Summary of General Rules - Miller Act Payment Bond Claims [1]

	Provide Written Notice of Claim[2]	File Suit on Payment Bond[4]
Subcontractor/Supplier having direct contract with Prime Contractor	None required	File within 1 year from last date on which Claimant furnished labor/materials
Supplier/Materialman, having no direct contract with Prime Contractor, but furnishing labor/materials to Subcontractor who has direct contract with Prime Contractor	Must be served[3] on Prime Contractor within 90 days from last date on which Claimant furnished labor/materials	File within 1 year from last date on which Claimant furnished labor/materials

- - - - - - - - - - -

1. Federal construction projects; prime contract amount exceeds $100,000

2. Stating amount claimed, and name and address of party to whom labor/materials furnished.

3. By registered/certified mail, postage prepaid.

4. In U.S. District Court, in district where prime contract was performed.

F. Federal Prompt Payment Act

1. Introduction

The Federal Prompt Payment Act can be found at 31 U.S.C. §3901, *et seq.*

The Act provides for timely payment of billings (31 U.S.C. §3901); interest and penalties for failure to timely pay (31 U.S.C. §3902); (at rates established by the Secretary of the Treasury); and requirements for the inclusion of prompt payment terms by prime contractors in subcontracts (31 U.S.C. §3905).

[DATE]

To: **[Name and Address of Prime Contractor]**

CERTIFIED MAIL
RETURN RECEIPT REQUESTED

Re: **[Description of Construction Project, Project Number, if known, and Address or Legal Description for Project]**

Gentlemen:

On or about _____, 20__, you entered into Contract No. _____ with **[Name of Federal Contracting Party]** in connection with the above-referenced project, together with Payment Bond No. _____ in the principal amount of _____ Dollars ($_____) with **[Name of Surety]** as surety, pursuant to the requirements of The Miller Act, 40 U.S.C. §270a, amended 40 U.S.C. §3131.

On or about _____, 20__, you entered into a written subcontract with **[Name and Address of party to whom materials and/or labor were furnished]**, to furnish a portion of the labor and/or materials provided for in said prime contract. On or after _____, 20__, the undersigned, having a direct contractual relationship with said subcontractor but having no contractual relationship express or implied with you, furnished labor and/or materials under written contract with **[or at the request of]** said subcontractor for **[specify labor and/or materials]** in the prosecution of the work provided for in said prime contract. Said subcontractor agreed to pay the undersigned for such labor and/or materials _____ Dollars ($ _____), being the reasonable value thereof, of which only _____ Dollars ($_____) has been paid, leaving a balance of _____ Dollars ($_____) due and owing the undersigned, the amount being stated with substantial accuracy and being the amount claimed by the undersigned. The last of the labor done or performed by the undersigned and/or material furnished or supplied by the undersigned was on or about _____, 20__.

This notice of claim against you and the surety on your payment bond is given pursuant to the provisions of the Miller Act, 40 U.S.C. §270b.

Dated this ___ day of _____, 20__.

[Name of Party who furnished labor and/or materials, e.g. Home Depot]]
Claimant

_____
[Name of person signing on behalf of Claimant]

Its:_____

[Address of Claimant]

carbon copy: **[Name and Address of Surety]**
Certified Mail
Return Receipt Requested

carbon copy: **[Name and Address of Party to whom materials and/or labor were furnished]**
Certified Mail
Return Receipt Requested

FORM F(1)

This concludes the American Institute of Architects
Continuing Education Systems program.

Feel free to approach today's speakers if you have additional questions or would like clarification on a topic covered in today's program.

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