Construction Law Newsletter

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Recent Cases In Construction Law

Wheeler v. Bucksteel Co., 73 Or App 495,698, P.2d 995 (1985.) A contract to perform engineering services is invalid and unenforceable by a person who is not a registered engineer at the time he made the contract or performed the services. ORS 672.020(1).

Sacher v. Bohemia, Inc., 74 Or App 685,704 P.2d 528 (1985). The plaintiff was injured while operating a table saw for his employer which was located on defendant's premises. Plaintiff claimed against defendant under the Employer Liability Act (ELA), ORS 654.305. The Court held that although defendant and plaintiffs employer were engaged in a common enterprise, defendant was not liable under the ELA because it did not have sufficient control over the risk-producing instrumentality.

As stated in 74 Or App 690-691:

"Plaintiff has not shown that defendant was in direct control of Cascade's saw to a degree sufficient to subject it to liability under the ELA. Defendant did not own.tke saw, nor did the activities of any of its employees contribute to the risk or danger. Defendant had no obligation to inspect the saw or undertake to see to its safe operation. The fact that defendant had an economic interest in Cascade's operation or that it might have required Cascade to remove its entire operation from its sawmill, does not show the type of control over the work activity or the injury-producing instrumentality that is necessary to establish liability under the ELA."

Medford School District No. 549C, ex rel. North Coast Electric Company et al v. Peterson and Jones Commercial Construction, Inc., 76 Or App 99,708P.2d 623 (1985); review denied, 300 OR 545, 715 p.2d 92 (1986).

Plaintiff supplied an electrical subcontractor (Martt) of the defendant general contractor. Martt went bankrupt. Plaintiff then sued to recover the value of materials it sold to Martt, claiming it had not been fully paid. The trial court held that plaintiffs receipt of defendant's joint checks to plaintiff and Martt was greater than the value of goods sold by plaintiff to Martt. Plaintiff appealed, and the Court of Appeals reversed for plaintiff.

The facts should be noted, because they involve facts that commonly occur when joint general contractors pay subcontractors with joint checks.

Defendant paid Martt with joint checks which plaintiff then cashed. Plaintiff retained the full amount due as of the latest date covered by each check and then paid back Martt the balance. Although this procedure was a customary practice, defendant did not know this procedure was being used. Defendant made its last progress payment to Martt on March 4, 1983, covering work through February 25, 1983. Plaintiff was not fully paid for materials furnished to Martt after that date. It therefore sought recovery of the balance from defendant and defendant's surety.

The Court held that Post ***Brothers Construction Company v. Yoder,*** 20 Cal. 3d 1, 141 Cal. Rep. 28, 569 P.2d 133(1977), upon which defendant relied, did not hold the plaintiff was deemed to receive the full amount of each check. The fact that defendant did not know of the procedure used by plaintiff and Martt was also of no avail. The Court wrote at 76 Or App 102:

"In this case, each check constituted payment for materials supplied through approximately the 25th of the previous month which was when Martt submitted its statement to defendant. There was no reason for defendant to expect those progress payments to cover future advances to Martt from plaintiff or from anyone else."

The lesson to be learned from this case is that joint check payments do not necessarily protect the payor from subsequent claims by the payee on the joint check. If the party making payment seeks protection to the full extent of the joint check, it should require an acknowledgment from the joint payee that the full amount has been received, or some other type of written acknowledgment to that effect.

Bruce Lee Schafer

Shop Drawings: New Court Ruling Casts Doubt on Architects' Stamped Disclaimers as Effective Protection From Liability For Their Content

Over the past 25 years, design professionals have been increasingly exposed to liability for both the content of their plans and their administration of projects.[1] One area of special interest has been architects' liability for the *content* of shop drawings submitted for review by contractors and subcontractors.[2] Traditionally, architects have attempted to limit their liability in this regard by stamping shop drawings with a disclaimer.[3] These stamps typically state that the architect has only reviewed the shop drawings for their general conformity with the overall plans. Further, the stamps disclaim any responsibility for the actual content of the drawings. For many years, this has been an effective technique to insulate design professionals from liability. A recent court decision, however, has cast doubt about the usefulness of this method not accompanied by specific language in the architect's contract with the owner stating that the architect has no duty with respect to the actual content of shop drawings.[4]

Continued On Page 2

Continued From Page 1

This article examines three facets of this new shop drawing problem. First, the development of stamped disclaimers is briefly reviewed. Second, the recent case law casting doubt on the effectiveness of these stamps is reviewed. Finally, the topics by which an architect can best minimize exposure in this area is discussed.

The Development of Stamped Disclaimers

A particular area which design professionals have faced increasing liability in recent years is in the duty to administer the construction projects for which they have developed plans and specifications. Courts have held architects liable to both injured construction workers and building occupants based on their failure to exercise the reasonable care expected of a professional in the design field in administering projects.[5] The key question in these cases has usually focused on whether the architects involved had a duty to administer the particular aspects of the construction which caused the plaintiffs injuries.[6] In answering this question, the courts have looked primarily to the architects' contracts with the owners.' If those contracts charged the architects with a duty beyond merely ensuring general compliance with the plans and specifications, courts have frequently found architects liable to foreseeable individuals who were injured as a result of the architects' negligence.[8]

In response to this expanding liability, architects develop the practice of stamping shop drawings submitted for their review with a disclaimer. The intent of these disclaimers was to make plain that the architects were not undertaking responsibility for any errors in the shop drawings. Rather, the architects were only vouching for the general conformity of the shop drawings to the overall design concept. For a time, this practice worked extremely well in protecting architects from liability for errors in the content of these drawings. Yet, as will be discussed below, a recent court decision has now cast doubt on the use of a simple disclaimer stamp as a way to minimize liability.

Recent Case Law Casting Doubt on Stamped Disclaimers

Recently, the United States Court of Appeals for the Eighth Circuit issued a particularly troubling opinion on shop drawing liability in ***Jaeger v. Henningson, Durham & Richardson, Inc.,*** 714 F2d 773 (8th Cir 1983).[9]

The ***Jaeger*** case involved a suit by two construction workers who were injured at a building site against the architectural firm which designed the building. By way of background, Midland National Insurance Company of Sioux Falls, South Dakota, engaged Henningson, Durham & Richardson ("HDR) to design an office building. Midland National Life also selected Swift Brothers Construction Company as the general contractor. Swift Brothers, in turn subcontracted with Egger Steel Company to do the steel fabrication work. Finally, Egger Steel hired L. H. Sowles Construction Company for steel erection. The two injured workers were employees of Sowles.

Midland National Life's contract with HDR required HDR to both prepare the overall plans and specifications for the building and also to review shop drawings submitted by the contractor. In this regard, their agreement provided that HDR was only to review shop drawings "for conformance with the design concept of the Project and for compliance with the information given in the Contract Documents."[10]

In the course of the project, Egger Steel submitted some shop drawings to HDR concerning a steel staircase. Although HDRs specifications for the stairs required 10-gauge steel for the landing pans, Egger Steel's shop drawings inadvertently called for only 14-gauge steel. HDR reviewed the shop drawings for their general conformity, and approved them. When doing so, HDR stamped "furnish as noted" on the drawings.[11] along with the following disclaimer:

"This *review* is for general conformance with design concept only. Any deuiation from plans or specifications not clearly noted by the contract has not been reuiewed. *Review* shall not *constitute* a complete check of all detailed dimensions or count or serue to *relieve* the contractor of contractual responsibility for any error or deuiation from contract *requirements.*"[12]

The stairs were indeed built with landing pans that used only 14-gauge steel. When the stairs were being installed, two workmen walked out onto one of the landing pans. It collapsed, and the workers were seriously injured. The two workers then sued HDR, contending that HDR was negligent in reviewing the content of the shop drawings for the stairs. A jury awarded the two men a combined $285,000 in damages.

Although HDR appealed on several grounds, the Eighth Circuit upheld the award. In doing so, it specifically recognized HDRs negligence in failing to review the content of the shop drawings.[13] The court ruled that HDR's duty to the workers in this regard stemmed from its responsibilities under its contract with Midland National Life." Moreover, the stamped disclaimer was apparently insufficient to block the liability that arose under the contract.[15]

How Architects Can Best Minimize Their Liability for the Content of Shop Drawings

Obviously, in light of the ***Jaeger*** case, serious rethinking is necessary in the area of stamped disclaimers. Architects can no longer rely solely on stamped disclaimers for protection against liability for the content of shop drawings.

Continued On Next Page

Three courses of action appear prudent to minimize the liability of design professionals in this area. First, the stamped disclaimers should continue to be used. Their use adds evidentiary strength to any case which actually goes to litigation. Second, the same disclaimer of liability for content found on the stamp should be incorporated into the architect's contract with the owner. This will make clear that the architect is not contractually assuming a duty for the content of shop drawings. Finally, for maximum protection, the construction contract with the owner should indicate that it is the general contractor's responsibility to both compare any shop drawings submitted with the architect's specifications and to review them for content. By delineating the respective roles of the architect and the general contractor in this way, responsibility for the content of shop drawings will be placed where they can most efficiently by evaluated.[16]

Richard E. Alexander

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[1]*See generally Miller,* Architect *Engineer Liability: A Growth* Period (1984).

[2]*See generally* Clark, *Focus on Shop Drawings* (1985).

[3]*See generally* Clark. *Focus on Shop Drawings, supra,* at 5-8.

[4]*See Jaeger v. Henningson, Durham* & Richardson, *Inc.,* 714 F2d 773. 775.76 (8th Cir 1983).

[5]*See generally* Annot, 59 ALR3d 869 (1974 & Supp Aug 1985) (and the cases discussed therein).

[6]*Id.* at 877-83; see *also* Arness, "Architects and Engineers: A consideration of Basic Liability Principles and Legal Trends in Foundation Engineering," 34 Ins Counsel J 334, 340-41 (1967) (and the cases discussed therein).

[7]*See generally* Annot, 59 ALR3d 869, *supra,* at 877 (and the cases discussed therein).

[8]*Id.* at 882-83 (and the cases discussed therein).

[9]*See also Henningson, Durham & Richardson v. Swift Bros.,* 739 F2d 1341 (8th Cir 1984) (a related case in which the architects unsuccessfully sought indemnification from the general contractor).

[10]*Jaeger v. Henningson,* Durham &Richardson *Inc.,* supra. 714 F2d at 775.

[11]*Henningson,* Durham &Richardson *u. Swift Bros.,* supra, 739 F2d at 1344.

[12]*Id.*

[13]*Jaeger v. Henningson,* Durham *& Richardson, Inc.,* supra, 714 F2d at 776.

[14]*Id.*

[15]This particular facet was not specifically addressed in the court's opinion in *Jaeger.* However, the tenor of the decision clearly indicates that the court was not persuaded by the disclaimer.

[16]The steps suggested herein were incorporated into a contract which the Oklahoma Supreme Court held protected the architect from liability for the content of shop drawings in the factual content very similar to *Jaeger. See Waggoner v. W&W Steel* Co., 657 P2d 147 (Okla 1982). In the *Waggoner* case. the contract between the architect and the property owner rend, in relevant part, as follows:

"SUPERVISION AND CONSTRUCTION PROCEDURES

"4.3.1 The Contractor shall supervise and direct the work. using his best skill and attention. He shall be solely responsible for all construction means, methods, techniques, and sequences and procedures and for coordinating all portions of the Work under Contract.

* * *

"4.13.1 By approving and submitting Shop Drawings and Samples, the Contractor thereby represents that he has determined and verified all field measures, field construction criteria, materials. catalog numbers and similar data, or will do so, and that he has checked and coordinated each Shop Drawing and Sample with the requirements of the Work and of the Contract Documents.

* * *

"4.13.5 The Architect will review and approve Shop Drawings and Samples with reasonable promptness so as to cause no delay, hut only for conformance with the design concept of the Project and with the information *(Footnote Continued)*

Ensuring Financial Solvency of Sureties on Public Contracting Bonds

Under Oregon's Little Miller Act, the successful bidder on a public contract must execute and deliver to the public contracting agency a "good and sufficient bond." ORS 279.029(2)(b). Failure to require the contractor to execute that bond makes the State of Oregon and the officers authorizing the contract jointly liable for unpaid labor and materials if the contract was entered into with the State of Oregon. If the contract was entered into on behalf of a public body other than the state, the public body and the officers authorizing the contract shall be jointly liable for labor and materials used in the prosecution of the work. ORS 279.542.

What is a public body in Oregon required to do to ensure that the sureties on the bonds it accepts on public projects are financially sound? There are no Oregon cases considering this issue. Therefore, one must look to the policies underlying the statutes.

That issue creates a tension between two public policies. One purpose of statutes which require payment bonds on public projects is to protect those who provide labor and materials to the project. ***E.g., Housing Authority of Franklin County for Use and Benefit of Smith-Alsop Paint & Varnish Co. v. Holtzman,*** 120 Ill. App. 2d 226, 256 N.E. 2d 873 (1970). That policy would appear to require the public agency to take affirmative steps to ensure that the surety or sureties on the bonds are financially sound at the time the public agency accepts the bond.

Continued *On Page 4*

Continued From Page 3

On the other hand, the sufficiency of the surety or sureties on the bond is a matter solely for the determination of the public officials in the exercise of their discretion. ***E.g., Marquette Gravel & Construction Co. v. Bengtson,*** 127 Kan. 492,274, P. 253 (1929). That policy protects public agencies from being second-guessed. However, it gives the public agencies little incentive to investigate the financial condition of the surety or sureties they accept.

This issue arose in a recent case before the Multnomah County Circuit Court, ***Metropolitan Service District for the Use and Benefit of Thomas P. Reeves and James G. Stark, Co-Partners, dba Krypton Mineral Industries v. Roberto A. Robles Assoc., Inc., et al.,*** Case No. A8408-04807. In that case, the Metropolitan Service District had contracted to construct the Alaska Tundra Exhibit at the Washington Park Zoo. Before the job was completed, the general contractor defaulted and several subcontractors, including Krypton Mineral Industries, filed suit against the general contractor and against the sureties on the statutory payment bond. The general contractor did not defend.

There were three sureties on the payment bond for that project Surety Insurance Company of California, Allied Fidelity Insurance Company and American Centennial Insurance Company. Those three sureties claimed that they had divided up their responsibility on the bond as follows: Surety Insurance Company of California was responsible for the first $400,000; Allied Fidelity Insurance Company was responsible for the next $1,000,000; and American Centennial Insurance Company was responsible for the final approximately $82,000 of liability on the payment bond.

Before the subcontractors initiated their lawsuits, Surety Insurance Company of California was placed in receivership. Thus, if the sureties' position was accepted, the first $400,000 in claims for unpaid labor and materials would not be paid.

After filing its initial complaint, Krypton Mineral Industries learned that there was some question as to whether the Metropolitan Service District either knew, or had reason to know, that Surety Insurance Company of California was not in sould financial condition at the time the Metropolitan Service District accepted the statutory payment bond for this project. Krypton Mineral Industries amended its complaint to add a claim against the Metropolitan Service District and its councilors under ORS 279.542. Krypton Mineral Industries alleged that the bond offered by the general contractor was not "good and sufficient" as required by ORS 279.029(2)(b) because the Metropolitan Service District knew, or had reason to know, that Surety Insurance Company of California was not in sound financial condition at the time it accepted the bond.

The Metropolitan Service District filed a ORCP 21 motion to dismiss Krypton Mineral Industries' claim under ORS 279.542. The Metropolitan Service District contended that (1) it fulfilled its statutory obligation by requiring that a bond beexecuted, and (2) Krypton Mineral Industries must allege that the Metropolitan Service District was arbitrary, capricious or fraudulent in accepting this bond.

In granting the Metropolitan Service District's motion to dismiss, the court stated that a public contracting agency must exercise some discretion in determining whether a particular bond satisfied the requirements of ORS 279.029(2)(b). This determination will necessarily involve some examination of who will act as surety. On the other hand, the contracting agency is not required to exercise any greater degree of care in using its discretion in this matter than would be the case when performing other governmental functions. The court held that Krypton Mineral Industries' allegations that Metropolitan Service District new, or had reason to know at the time it accepted the bond, that Surety Insurance Company of California was not in sound financial condition do not state a claim that Metropolitan Service District had failed to discharge its statutory duty.

That ruling by the court raises a couple of questions. First, it appears to be inconsistent with the public policy that statutes requiring payment bonds on public projects are to protect those who provide labor and materials. Generally, that policy would mandate that such statutes be interpreted in the light most favorable to the bond claimant. Second, that ruling gives public agencies little incentive to ensure that the bonds which they accept will in fact protect those providing labor and materials to public projects. Courts should not substitute their judgment for that of the public agency in determining whether a public agency accepted a good and sufficient bond. However, it would seem unfair to those providing labor and materials that a public agency should be able to escape liability under ORS 279.542 where it knew, or had reason to know, that the surety or sureties on the bonds it was accepting could not protect the providers of labor and materials because the surety or sureties were not in sound financial condition.

David T. Douthwaite

Attorney Fees are Available in Litigation with the Federal Government – Sometimes.

Historically the "American *rule"* has been the guide on recovery of attorney fees in litigation with the federal government. In short a private litigant could only recover attorney fees when the particular cause of action was under a statute that expressly made provision for the fees.

Continued On Next Page

The Equal Access to Justice Act (EAJA) which initially became effective October 1, 1981 changed this. The amendments to the Act, on August 5, 1985 made substantive changes which broaden its application and may allow recovery in many instances not previously available.

The EAJA, Pub. L. No. 96-481, and amended Pub. L. No. 99-80 amends 5 U.S.C. 5504, Costs and Fees of Parties (in agency action) and 28 U.S.C. §412 Costs and Fees (awarded by courts). It applies to other matters, but the focus of this note is construction contracts with the federal government, and litigation of claims and disputes before the agency contract appeal boards, or before the U.S. Claims Court. This may have application in matters before the U.S. District Court, when dealing with one of the classes of actions that the legislation allows.

Eligibility

Applicants for attorney fees must meet several criteria:

1. A natural person with net worth of not more than $2 million. (Prior to October 1, 1984, not more than $1 million)., or

2. An owner of unincorporated business with a net worth of not more than $7 million, ($5 million prior to Oct. 1, 1984) and not over 500 employees, or

3. Any partnership or corporation with a net worth of not more than $7 million, ($5 million prior to Oct. 1, 1984) and not over 500 employees.

The applicant must have prevailed in a decision rendered (or favorably settled in a case in litigation) on or after Oct. 1, 1981. Fees incurred prior to that date can be recovered, where the court action was pending on that date.

The EAJA applies only to "civil actions", and "adversary adjudications". This clearly includes federal contract disputes before the U.S. Claims Court, or the Board of Contract Appeals.

Standards for Award

An agency, or court shall award fees and other expenses to a "prevailing party" unless the position of the United States is substantially justified. §504(a)(1); §2412(d)(1)(A).

1. Prevailing Party:

A plaintiff may be a prevailing party if they have succeeded on some significant issue in litigation which achieves some of the benefit the plaintiffs sought in the case. ***Austin v. Dept. of Commerce,*** 742 F.2d 1417 (Fed. Cir. 1894) Where a party prevailed on a particular phase of the litigation, but not on all aspects they can still be awarded fees for that phase of the litigation. ***Ellis v. United States,*** 711 F.2d 1571 (Fed. Cir. 1983); ***Rawlins v. United States,*** 8 Cl. Ct. 355 (1985); ***Euerett Plywood Corp. V. United States, 3*** Cl. Ct. 705 (1983). Even a successful settlement of the case may satisfy the requirement of "prevailing" ***Deuine v. Sutermeister,*** 733 F.2d 892 (Fed. Cir. 1984).

2. Substantially justified position of United States:

Piror to the 1985 Amendments the trend was to view only the posture in the litigation process, and to consider lack of justification only when the conduct of the United States was "reprehensible." ***Estate of Berg v. United States,*** 687 F.2d 377 (Ct. Cl 1982). This was toned down a little by the CAFC in concluding that the behavior of the United States did not have to be reprehensible, only reasonable under the circustances. ***Kay Mfg. Co. v. Untied States,*** 699 F.2d 1376 (Fed. Cir. 1983) This has been clarified with the 1985 amendments. In the House discussion, the intent was to have the test be one where the government action is more than just reasonable. The 1985 amendments also extended the scope of government action to include a review of the agency level action before commencement of litigation. The CAFC, en banc, has said that substantial justification is a case by case matter to be reviewed on the whole record. It requires the government to show that it was "clearly reasonable" in asserting its position, including its position at the agency level, in view of the law and facts. It is not enough to be able to show a mere existence of a colorable legal basis for the governments case. ***Gavette v. Office of Personnel Management,*** CAFC No 84-1286, (slip op., Feb. 28, 1986) (en banc). This more stringent burden on the government was also adopted in ***Schuenemeyer v. United States,*** 776 F.2d 329 (Fed. Cir. 1985). The Armed Services Board of Contract Appeals has recently cited ***Schuenemeyer*** in saying that the statutory standard of "substantially justified" is a standard slightly more stringent than reasonably justified, and requires more than mere reasonableness. ***Roberts Construction Company,*** ASBCA No. 31033, 86-1 BCA para. 18,846 (1986).

However, a party seeking to enjoin award of a bid solicitation was determined not to be entitled to attorney fees when the court found the government carried its burden of substantially justified in that the solicitation was cancelled for reasons other than the suit. ***J.H. McQuiston v. John O. Marsh, Jr.*** 790 F.2d 798, 33 CCF para. 74,390, (Ninth Cir. 1986) (9th Cir. No. 84-6500, decided May 30, 1986). The Armed Services Board has declined attorney fees in a case where it concluded that action of the government was taken in response to legal uncertainties about the application of the Debt Collection Act, and were substantially justified. ***Pat's Janitorial Service, Inc.*** ASBCA No. 29129, 86-2 BCA para. 18,995 (1986). The Engineers board concluded that prevailing on a theory not raised until the last stages of the proceeding did not afford the government any basis to have acted differently in the litigation, and the government was substantially justified. ***Great Western Utility Corporation,*** ENG BCA Nos. 4866-F, 4899F, 4934-F, 4935-F. 86-3 BCA para. 19011.

Continued On Page 6

Continued *From Page 5*

Amounts of Fees, Procedure

The Act places a limit on the hourly rate of attorney fees of $75 per hour, with a few narrow exceptions. Pre-litigation expenses are not allowed, ***Bailey v. United States,*** 721 F.2d 357 (Fed. Cir. 1983), but post litigation costs and expenses incurred in applying for attorney fees are compensable. ***Schuenemeyer*** u. ***United States,*** supra. Allowable expenses include the reasonable expense of expert witnesses, reasonable costs of any study, analyses, engineering report, etc. found by the tribunal to be necessary for the preparation of the parties case. §5504(b)(1)(A); §2412(d)(2)(B). Items of cost traditionally not considered within the attorney hourly fee such as postage, photo copying, travel cost, meals away from home office, are not allowed. The cost of paralegals, and computer researchers are allowed. ***Hirschey v.*** FERC, 760 F.2d 760 (D.C. Cir. 1982).

The application requires the submission under oath of a statement that specifies the nature of each service rendered, the amount of time expended for each service, and the customary charge for each service. ***Gauette,*** supra.

The time for filing is within thirty (30) days of final judgement. §504(a)(2); §2412(d)(1)(B). A judgment is final when it is no longer appealable. Under the Contract Disputes Act, a decision of a Board of Contract Appeals becomes final if not appealed within 120 days after receipt of the decision. In other forums, such as U.S. District Court, the time for appeal is 60 days when the United States is a party, and if not appealed would then become a final judgment. 28 USC $2107. In some forums the time for appeal is as little as 30 days.

J. William *Bennet with* specific acknowledgement to the Don Kinlin article entitled: "Equal Access to Justice Act" *16* Public Contract **Law** Journal *266-286* **(1986).**

Wrap-ups, Controversial Insurance Consolidations

Consolidating the coverages, controlling the construction insurance program, and paying the premium are the elemets of the much praised (but often maligned) device known as "wrap-up" used in construction insurance. The consolidation of coverages may include public liability, workers' compensation, and builders' risk insurance written under one policy which, in effect, "wraps-up" the exposures of the several interests involved in a construction .project. The interests may include the construction project owner, the general contractor, the sub-contractors, the architects and engineers. Wrap'ups usually are created by the construction project owner, although they may be instigated by general contractors to include sub-contractors and others.

A wrap-up formulated by a construction project owner sets forth the details of the coverage to be provided by the owner and usually stipulates that contractor-bidders submit construction project bids on an ex-insurance basis. An owner also may require the bids to be submitted on both ex-insurance and with the cost of insurance included, permitting the owner to choose the most cost-effective method of insuring particular segments of the construction project. If an ex-insurance basis is used, the owner's insurance arrangements prevail and the contractor-bidders agree to suspend their relevant insurance coverages for the project, which would be redundant given the owner-provided insurance program. Through the process of bidding ex-insurance, the contractor-bidders are implicitly agreeing to participate and cooperate in the wrap-up when it is implemented.

It sould be noted that wrap-ups are not necessarily universal coverage "umbrellas." They bundle coverages which the project owner chosses to include, and those included generally provide protection at the job site and for necessary and incidental operations relating to the specific construction project. Certain coverages are not included; for example automobile liability coverage is excluded, although the auto liability exposure exists in construction projects. This exclusion occurs because the mobility of autos and trucks makes it impossible to assign premium charges equitably when they are used at multiple sites.

Wrap-ups are not totally legal. In some jurisdictions, they are prohibited; in other jurisdictions, the state insurance regulatory officials have not issued regulations concerning wrap-ups. In come jurisdictions, serious obstacles to the use of this device have been promulgated, such as the required dollar size of the construction project, before it is eligible for a wrap-up.

Few insurance concepts have caused as much controversy or generated the verbal blasts as the wrap-up concept engendered from wrap-up proponents and opponents. This has tended to obscure an objective consideration of the merits and disadvantages of this unusual insurance consolidation device. Unfortunately, many of the stated reasons for and against wrapups are so closely allied with the self-interest of the proponents and opponents that it is difficult to sort out the true worth, if any, of wrap-ups. A review of those contentions is in order.

An advantage claimed for construction project owner-controlled insurance is that it enables an owner to effect a comprehensive, more uniform construction insurance program. It is said that purchasing the insurance in one lot from one insurer (or, at least, from fewer insurers than if all

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project participants purchased their own coverage) will allow the owner to obtain higher policy limits and' eliminate the cost and necessity of securing certificates of insurance from the many entities involved in the construction project. Also, coverage gaps and coverage duplications that arise when multiple policies and multiple insurers provide protection are avoided.

Wrap-up opponents would respond that effective and efficient insurance agents and brokers have devised comprehensive insurance programs for their contractor clients which have stood the test of time and are specifically tailored to the special needs of those clients. They would contend that these programs, at least for their clients, are superior to the centralization of coverage under a wrap-up, and that the intrusion of the project owner into a contractor's insurance affiars is disruptive especially to the continued relationships of the contractor, broker. and insurer. Unquestionably, the stated advantage of more uniform, broader coverage has much merit. The opponents' contention of superior individual insurance programs is valid in specific situations; however, there is no substantial evidence available that constructin project owners are not capable of devising and administering a wrap-up that will adequately meet the coverage needs of contractors and other project participants, especially if the owner uses an efficient, knowledgeable broker to effect the wrap-up. The disruptive effect on existing contractor, broker, insurer relationships is a trade-off for the contractor against participating in the construction project involving a wrap-up. It would seem that occasional participation in wrap-ups requiring suspension of a contractor's coverage, while bothersome, might be worth the profit to be gained from the project.

A related specific issue is the disposition of the completed operations exposure. The wrap-up liability coverage may expire at the completion of the construction project or may continue only for several years beyond that date. In any event, if completed operations coverage is provided by the wrap-up, the coverage will expire when the wrap-up liability coverage expires, or shortly after, and on some projects and in some jurisdictions, that arrangement may not he sufficient. The contractor will need to arrange continuing completed operations coverage with his own liability insurer. This may cause some difficulty because the contractor's insurer was not involved in the basic liability coverage on the construction project operatons and may not look favorably on providing completed operations coverage. It would appear that this issue might be negotiated with the contractor's insurer, and the additional premium required for the coverage included as a part of the contractor's project bid.

Insurance cost reduction has been one of the major arguments advanced by proponents for the use of wrap-ups. Premium savings are obtained, usually through increased premium discounts, the elimination of coverage duplications, lesser agent/broker costs because of possibly using a fee approach as opposed to straight commission, the aggregation of dividends by the project owners rather than by the individual project participants, and the reduction of losses because of better centralized loss control and claim control. It should be noted that these savings are not obtained without some additional expense being incurred by the project owner to establish and master a wrap-up. Opponents would contend that net savings in costs under a wrap-up are illusory when all cost aspects are considered. In addition to the project owner's additional administrative expenses, the individual participants must maintain additional and different records, which can be costly. For example the general contractor may be required to oversee the reporting and premium forwarding by sub-contractors. The cost of these activities must be absorbed by the contractor-participants in the wrap-up and, therefore, the contention by opponents that apparent wrap-up cost savings may redound only to the project owner's benefit, while increased administrative costs are incurred by other participants, has merit. Of the various savings techniques referred to above, the aggregation of dividends by the project owner probably is most controversial, because the dividends depend, in part, on the safety efforts of the wrap-up participants. Some contractors, through extensive safety and loss control efforts, may have been able to reduce rates or obtain better dividends in their respective construction insurance programs. A wrapup in which such contractors participate requires a suspension of their insurance program, at least for the wrap-up project, and this may prove harmful to their expected continuing favorable rating and dividend experience. Obviously, this is another trade-off of the operating profit gained by the contractor by participating in the construction project as opposed to any loss of favorable rating and dividend experience by participation in the wrap-up. It will have to be evaluated on that basis. Are wrap-up cost savings chimerical? It depends on the manner in which the wrap-up is established. If it is of the magnitude to generate considerable cost savings because of the economies of scale and it is built and implemented effectively and efficiently. project owners will relaize significant financial savings, making this an attractive insurance/risk management device. It should be noted that wrap-ups do not guarantee cost savings, but if properly used, they *can* make a significant dollar difference.

Wrap-up opponents would point to the fragmentation of coverages among insurers when participating in a wrap-up. As indicated above, automobile liability and continuing completed operations coverage normally are not included in a wrapup. This causes these coverages to be written by different insurers than the basic construction project liability wrap-up insurer. This can result in disputes among insurers as to who is teasonible for

Continued On Page 8

Continued From Page 7

incidents that might, for example, be covered under the wrap-up liability coverage or under the contractor's automobile liability coverage. Some of this controversy can be avoided by careful, prior coordination of coverage by the project owner, the participating contractor, and their brokers. The residual dispute problem makes for a good case to include hold-harmless clauses in the construction contract. The project owner, the general contractor, and the sub-contractors can use this device to offset some of the problems referred to and caused by not having one liability insurer.

One issue involving wrap-ups that seems to be loaded with much more emotion than logic is the centralization of safety and loss control. One seldom would quarrel with the contention that centralization and enforcement of a uniform safety and loss control program by the project owner, if properly designed and implemented, is more than likely superior to a variety of safety and loss control programs, some of real quality and some not, conducted by a large number of sub-contractors involved in a large construction project. Opponents would contend that the philosophy of shifting the safety and loss control program to the project owner is wrong, because it removes the incentive from the sub-contractors that was presentwhen the sub-contractors' insurance costs depend on their loss reduction prevention efforts in a nonwrap-up construction project. Opponents also would contend that a contractor's existing safety and loss control program may not mesh with the program proposed by the project owner, making for a less than optimum program. It is true that the sub-contractors are contractually required by the wrap-up to cooperate and participate in the project owner's safety efforts, but opponents point out cost savings (money) does more to focus the mind than contractual provisions. This contention cannot easily be dismissed. Possibly, one should observe that a contractor's attitude toward safety and loss prevention is not, or should not be, different, irrespective of who isresponsiblefor the loss reduction and control program. **A** contractor suffers losses other than increased insurance costs when key employees areinjured, and the reduction of such losses is not an on-again, off-again thing with most contractors, and certainly should not be dependent on whether a wrap-up is in existence. Nevertheless, the opponents' contention is of concern, and extra efforts must be made to make sure safety and loss control efforts with respect to construction projects does not deteriorate because some or all of the responsibility for such efforts has been centralized.

An intangible, but perhaps the most important, controversial aspect of wrap-ups is the simple proposition that those who gain by constructing and implementing a wrap-up (the project owner or general contractor, the broker, and insurers) are convinced, philosophically and pragmatically, that the wrap-up is the way to go. The contractors and other participants, their brokers and insurers who are "forced" into a wrap-up to their perceived detriment, resent the coercion involving the loss of control of their insurance affairs, as well as premium income, causing them to contend it is philosophically and pragmatically wrong. Unfortunately, in any such competitive game, there are winners and losers, and one should expect the losers to complain: however, the clamor generated tends to block an objective consideration of the wrapup device.

Is a wrap-up useful and worth considering for an eligible construction project? Yes. Is a wrap-up suitable for all eligible construction projects? No. Are all, or almost all, wrap-ups well done? No. The bottom line is that each must be condisered on its individual merits and not accepted or rejected categorically on the basis of the real or perceived advantages or disadvantages of the device.

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Miller Act Claims Can Be Made Against Irrevocable Letters of Credit

In ***United States of America, for the Use of Douglas G. Anderson v. Challinor,*** 620 F. Supp. 78 (D. Mont. 1985), the court held that the Miller Act provides a remedy and a forum for those cases where the law requires a bond and where the administrative officer accepts a letter of credit in lieu of a hond.

In that case, the Forest Service let a contract. Instead of requiring a bond, the contracting officer accepted a letter of credit. The contractor failed to pay its subcontractor. The subcontractor filed a Miller Act claim in U.S. District Court.

The express provisions of the Miller Act state that it applies only in instances where the contractor provides a bond. However, the federal government has amended its regulations to state that irrevocable letters of credit could be used as a substitute for Miller Act bonds. 41 C.F.K. §1-10.204-2 (1984). Apparently, there was some question as to whether the U.S. District Court had jurisdiction because the security was a letter ofcreditandnota Miller Act bond. The court concluded that it would frustrate the purposes of the Miller Act to hold either that there was no right for the subcontractor to sue, or there was no jurisdiction for the court to try to suit because the contracting officer had accepted a letter of credit in lieu of a performance bond.

Party Need Not Seek to Compel Arbitration Under ORS 33.230 If Arbitration Agreement Provides For Ex Parte Arbitration

In ***IFG Leasing Co. v. Snyder,*** 77 Or. App. 374, 713 P.2d 630 (1986), defendant defaulted on a lease agreement containing an arbitration clause. That clause provided that the rules of the arbitration Association would apply. Plaintiff made numerous requests for arbitration, all of which the defendant ignored. After giving the defendant notice of arbitration by certified mail, plaintiff initiated an ***ex parte*** arbitration proceeding pursuant to the rules of the American Arbitration Association. Plaintiff received **a** favorable award. Defendant was personally served with a petition to have the award entered as a judgment in the Circuit Court. Plaintiff moved for summary judgment. Defendant resisted, claiming that the award was void because plaintiff had not complied with ORS 33.230. The trial court granted plaintiffs motion for summary judgment. Defendant appealed.

ORS 33.230 provides that a party aggrieved by the failure, neglect, or refusal of another party to perform under a contract or submission providing for arbitration shall petition the Circuit Court that the arbitration proceed as provided in the contract. The court concluded that the procedure of ORS ***33.230*** was not mandatory if the parties had agreed to have their dispute governed by the rules of the American Arbitration Association. Those rules expressly provided for ***erparte*** arbitration, and the parties are bound by that agreement.

Provider of Rental Equipment Must Give Notices Required By ORS 87.021

In ***Brown u. Ruhl,*** 78 Or. App. 333, 717 P.2d 162(1986), the court held that rental equipment is "material or labor described in ORS 87.010(1) to (3), (5) and (6)." In that case, plaintiffs rented equipment to defendant Ruhl, who had contracted with McKenzie to paint McKenzie's barn. Ruhl did not pay plaintiffs. Plaintiffs filed a lien on McKenzie's barn and subsequently filed an action to foreclose the lien. Plaintiffs obtained a decree of foreclosure. McKenzie appealed from that decree, arguing that plaintiffs were required under ORS 87.021(1) to provide him with a notice of the right to claim the lien. Because they failed to do so, their lien should be unenforceable under ORS 87.021(3).

Plaintiffs argued that the terms "material or labor" as used in ORS 87.021 do not include rental equipment, and that a notice is required only if a person provides materials and labor. In the alternative, they argued that if "materials and labor" include rental equipment, then plaintiffs were exempted from giving notice by ORS 87.021(4) because McKenzie's barn was a commercial improvement,

The court held that the terms "material or labor described in ORS 87.020(1) to (3), (5), and (6)" includes rental equipment. In fact, subsection (2) principally concerns rental equipment and subsection *(3)* only concerns rental equipment. Thus, rental equipment is within the type of lien requiring a notice.

In an earlier opinion, ***Star Rentals, Inc. u. Seeberg Construction Co., Inc.,*** 66 Or. App. 822, 825-27, 677 P.2d 708, ***reu. den.,*** 297 Or. 124(1984), the Court of Appeals had concluded that the terms "materials or supplies" used in former ORS 87.021 did not include rental equipment. However, the court noted that ORS 87.021(1) had been amended since the filing of the lien in this case to apply to "a person furnishing any materials or lahor ***described in*** *ORS 87.010(1) to (3), (5)* **and** *(6)."*

As to the plaintiffs' second defense, the court relied upon a subsequent statutory amendment. In 1983, the legislature amended ORS 87.021(4), which provides exceptions to the notice requirements of subsection **(1)**. The 1983 legislature added an exception for person "who rents equipment used in the construction of a commercial improvement." If notice was not required under former ORS 87.021(4), it would have been unnecessary for the legislature to add a special exception from the notice requirement for rental equipment.

Notice of Right to Lien Must Be Delivered During the Progress of the Improvement

Contractors who supply materials to short-duration projects must make sure that they deliver their notice of right to lien during the progress of the improvement. **In *Sun Solutions, Inc. u. Brandt,*** 300 Or. 17, 709 P.2d 1079 (1985), homeowners contracted to have a solar waterheating system placed in their home. The general contractor, in turn, purchased materials from the plaintiff. Plaintiff delivered those materials to the general contractor at the defendant's home on December 27, 1982. The solar waterheating system was constructed and

Continued On Page 10

Continued From Page 9
installed on that same date. Subsequent to the completion of the improvement, but within ten days of delivery, plaintiff notified the homeowners of plaintiffs right to claim a lien for providing those materials. After the general contractor failed to pay the plaintiff for the materials, plaintiff filed a claim of lien and commenced a lawsuit to foreclose the lien.

The trail court dismissed the plaintiffs complaint because the plaintiff failed to plead that notice of the right to claim a lien **was** given to the defendants "during the progress of the improvement" as required by ORS 87021(1). The Court of Appeals reversed, and it in turn was reversed by the Oregon Supreme Court. The Supreme Court stated that the statutory language "during the progress of the improvement" established the absolute time limit within which the notice of the right to claim a lien must be given.

Professional Engineer's Stamp Does Not Protect Unregistered Designer

In ***Merrill u. Board of Architect Examiners,*** 300 Or. 34, 706 P.2d 556 (1985), the court affirmed a finding by the Board of Architects Examiners (BAE) that fined **the** designer of a building for the unlicensed practice of architecture. In that case, the Hamilton Creek School District No. 33C employed Merrill to design a classroom addition to a school. Because Memll was not an architect, he associated himself with Joseph Thaler, a registered professional engineer with whom he had **a** previous working relationship. Merrill prepared plans and specifications for the construction project. Thaler reviewed them, made some calculations, and put hs engineer's stamp on the documents. The BAE found that Merrill's preparation of the plans and specifications constituted practicing architecture without a license.

The practice of architecture is defined to mean the "planning, designing or supervision of the erection, enlargement or alteration of any building or of any appurtenance thereto other than exempted buildings." ORS 671.010(5). Contractors or their supervisors or foremen acting under the supervision of a registered architect or registered professional engineer are excluded. *Id.* ORS 671.030(1) also excludes from the practice of architecture the practice of engineering by **a** registered professional engineer or any person engaged in architecture or engineering work as an employee of an architect or registered professional engineer.

In this case, Merrill could not qualify for either exemption. **He** was not employed by the contractor on the job and therefore did not fall within the exemption in ORS 671.010(5). Nor was he employed by the engineer Thaler, and thus did not fit under the exemption in ORS 671.030.

No Particular Amount On-Site Labor Is Necessary to Avoid The Notice Requirement Of ORS 87.021

A subcontractor does not have to provide any particular amount of on-site labor in order to avoid the notice requirements of former ORS 87.031. ***Northwest Iron Works, Inc. u. Rippling River Development Corporation,*** 71 Or. App. 144, 691 p.2d 111 (1984), *rev. **den.,*** 398 Or. 597 (1985). In that case, plaintiff orally agreed with the general contractor to furnish and fabricate steel beams, trusses, and miscellaneous **steel** for a construction project. Some of the steel did not fit properly. The subcontractor sent one of its sub-subcontractors to the site for two days to do certain welding. It also sent two employees to the site for three days to do other welding and to replace certain materials. When the general contractor was unable to pay, the subcontractor filed a construction lien and **a** suit to foreclose it. The general contractor went bankrupt. The owner claimed that the subcontractor failed to provide the materialman's notice required by ORS 87.021. The owner argued that the subcontractor had not provided labor within the meaning of the statute.

The court disagreed. It reasoned that the statute does not expressly require any particular amount of labor and that the subcantractor's on-site labor was not ***de** minimis.* It also stated that it may attribute to the subcontractor the labor of both its employees and its sub-subcontractors. The court found that the subcontractor's labor in this case was within the statute, even if it was necessary to correct errors made by both the subcontractors and the general contractor.

David T. Douthwaite

Washington Law Update

As part of Washington's recent tort reform legislation, there are provisions which cast some doubt on the enforceability of certain indemnification provisions in construction contracts.

These provisions apply to any agreement signed after June 13, 1986.

Richard E. Alexander

The Basic Law of Construction:

*Cut it **large** and* kick it into ***place.***

NOTICE

TOPICS:
Bid Disputes, Project Coordination, Labor - DBE & MBE Issues, Breach of Contract, Damages, Project Records, Use of Experts, Surety Issues, Filing Construction Liens, Public Contract Issues.

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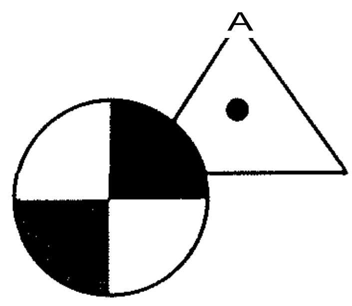
3. TIME: 8:45 A.M. - 4:45 P.M.



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OREGON STATE BAR
CONSTRUCTION SECTION

CONSTRUCTION
LITIGATION SEMINAR '86

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Why This Project Has No Schedule:

1. We had a schedule, but it was too big for the wall.
2. This job is too complicated to schedule.
3. This job is too small to need a schedule.
4. We don't have a schedule, but if we had one we would be on it.
5. They made one. but it is in the home office.
6. We don't make schedules so then the Owner can't complain when we don't follow it.
7. We don't want the subs to complain that the job is taking too long.
8. If we had a schedule, it would take too much time to keep it up to date.
9. We do have a schedule; it's that roll in the corner.
10. We're too busy building the project to have any time to schedule it.

OREGON STATE BAR CONSTRUCTION LAW CLE SCHEDULED

Co-editors Dick Alexander and Steve Schell state that the first comprehensive Oregon State Bar sponsored CLE on Construction Law is now scheduled for publication in 1988. Topics have been selected and authors are now being named.

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