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Businesses Providing Wi-Fi or Free Internet: Beware of Trolls!

Jason Alexander
Clifford Davidson
Sussman Shank

Recently, there has been a dramatic rise in so called "copyright trolling" litigation. These lawsuits, several of which have been filed in Oregon, Washington and California, pose a significant risk to any business that makes Wi-Fi or other Internet connections available for use by customers, guests, clients, employees, or the public.

In order to understand the risks that "copyright trolls" pose, it is necessary to know a bit about how they operate. The typical copyright troll is an LLC established for the purpose of enforcing the copyrights of one or more protected works, such as movies or songs. A plaintiff's attorney works in conjunction with that entity and files copyright infringement actions on the entity's behalf.

In order to find potential defendants, the attorney hires a company to search for illegal downloads of particular movies or songs. Such downloads may be traced to specific IP addresses -- unique numbers assigned by Internet Service Providers, such as Comcast, to each subscriber. Once the copyright troll determines the IP addresses used to download the copyrighted materials, the troll files a lawsuit against "unknown" defendants. For example, a case recently filed in Washington is captioned *R&D Film 1, LLC v. Does 1-45*, where "Does 1-45" are unknown defendants. The troll then subpoenas the Internet Service Provider, *e.g.*, Comcast, in order to learn the true identities of the defendants. The troll then substitutes the real names of the accused copyright infringers for the "Doe" defendants. In this way, copyright trolls are able to file lawsuits against thousands of businesses and individuals, and obtain settlements ranging from several-hundred to several-thousand dollars.

Though these lawsuits are problematic for a number of reasons, they are particularly troubling because they do not simply punish individuals who actually download copyrighted materials illegally. These suits also seek to exploit those who provide the network connections that downloaders use. This potentially implicates any business providing Wi-Fi as a perk or service to its customers, clients, or employees -- even though such businesses themselves did not actually perform any illegal downloads.

The reason trolls may plausibly claim that a business offering Wi-Fi is liable for infringement is that copyright liability can be both primary and secondary. If a person actually makes infringing copies, or other unauthorized use, of a copyrighted work, that person is a primary infringer. Further, a party may be held liable as a secondary infringer if that party either encourages infringement, or is aware (or should be aware) of such infringement but does not prevent it. Thus, for example, if a company has reason to believe that its customers use its Internet connection to download copyrighted content, but that company does nothing to prevent such downloads, that company might be liable as a secondary infringer.

Fortunately, several arguments have been successful in early efforts to dispose of such

lawsuits and to prevent Internet Service Providers from being compelled to provide the identities of their subscribers. In addition, there are several steps that might help prevent illegal downloads and, in the event of troll litigation, convince the plaintiff that its secondary infringement case will fail:

- Protect your Internet with a complex password that is changed often in order to prevent strangers from using your Internet connection. Keep a log of who has been given the password to your Internet connection.
- Require a click-through login screen with terms of use, including a promise by the user not to use BitTorrent or other file sharing programs that commonly are used to share infringing materials.
- Train employees to recognize BitTorrent and other pirating software, and establish a written policy that employees are to report immediately to supervisors any use of such software. Reports should be logged, and those using such software should be either disciplined (if employees) or denied access to the Internet connection (in the case of customers).

Difficult Issues in Contractual Defense & Indemnity

Seth Row
Parsons Farnell & Grein

Contractual defense-and-indemnity issues bedevil construction lawyers in every area of practice, whether representing developers, contractors, insurers, or policyholders. This article discusses some recent issues on the "defense" side of the defense-and-indemnity question.

Most standard construction contracts contain some form of defense and indemnity language. The language will generally provide something like the following:

> ["Downstream" party (usually a contractor, subcontractor, or supplier)] will defend, indemnify and save [the "upstream" party (usually the owner, developer, or general contractor)] harmless from all liability, loss, damage, causes of action, claims or judgments because of injury or damage to any person or property… that may occur or may be alleged to have occurred arising out of or connected with the performance of the work under this contract or as a result of the acts or omissions of the contractor, or its subcontractors…

This language is so common that most people drawing up construction contracts give it little thought.

Enforcement of these clauses, however, can be difficult. Most of the common objections to enforcement spring from the concept that the downstream party (indemnitor) is only obligated to indemnify the upstream party (indemnitee) to the extent only that the indemnitee is held liable for the fault or negligence of the indemnitor. This objection has its grounding in ORS 30.140, which provides that:

> …any provision in a construction agreement that requires a person or that person's surety or insurer to indemnify another against liability for damage arising out of death or bodily injury to persons or damage to property caused in whole or in part by the negligence of the indemnitee is void.

This statute is used by insurers, and other potential indemnitors, to limit not only their indemnity obligations, but to deny or limit the defense obligation.[1]

[1] In *Hays v. Centennial Foods, Inc.,* 33 Or App 689 (1995), the Court of Appeals held that, even if the indemnity language of a contract appears to be so broad

The argument sometimes goes something like this: we (indemnitor) don't know at this point to what extent the plaintiff is seeking to hold the indemnitee (upstream party) liable because of its *own* negligence, as opposed to *our* negligence. We only have to defend if there is an indemnity obligation – that is, if the plaintiff holds you liable for *our* negligence. Therefore there can be no defense until it is determined that that is in fact the situation. This argument turns the defense obligation into, at most, a reimbursement obligation (likely not what the indemnitee thought that it was getting).

Of course sometimes it is clear from the face of the pleadings that the plaintiff is seeking to hold the indemnitee liable for the negligence of the indemnitor.[2] The argument from the indemnitee in response to that situation sometimes goes like this: even if the allegations clearly implicate vicarious liability for our negligence, the plaintiff is also trying to hold you liable for your failure to supervise our work. We don't have to indemnify you for that liability. Therefore, we have to wait until the jury decides (if they do) how much of the damages are because of our fault, and how much of your fault, to apportion that defense (reimbursement) between what you pay for, and what we pay for.

And to make things worse, in most cases the "upstream" party is seeking defense and indemnity from *multiple* potential indemnitors, who *themselves* are named in the lawsuit. In that case, the arguments against providing a defense will include: 1) that apportionment between indemnitors has to wait until the jury's answer to special interrogatories about the relative allocation of fault, and 2) that because the indemnitor is *in* the case, they will pay for their own fault, which means that there will be no indemnity owed, or at least not any indemnity that is allowed by ORS 30.140, and therefore there is no defense obligation.

Some arbitrators and judges have accepted one or more of these arguments. A common resolution on a motion for summary judgment on the defense obligation is that while there is a duty to defend that is not foreclosed by ORS 30.140, the nature or extent of the defense obligation cannot be determined until there has been final resolution of the underlying case.

But some have taken a different approach. For example, in 2012, the Washington County Circuit Court held, on motions for summary judgment, that a subcontractor had a duty to defend a general contractor regardless of whether or not a jury found that the indemnitors were or were not at fault. In other words, the court rejected the idea that the duty to defend could wait until it was determined that the indemnitee would be held liable for the fault or negligence of the indemnitors. As the court put it: "[A] harsh reality is many people are sued every day in which ultimately they may not be at fault, yet, they have to pay to prove they were at fault… contractually the subcontractors agreed to contribute to those legal costs [of the general] regardless of fault."

This ruling was hailed by developers and general contractors because it disposed of the argument that the defense obligation is dependent on fault, and also (by extension) disposed of the argument that the *extent* of the duty to defend depends on ultimate liability. If the subcontractor has an immediate duty to defend, the subcontractor's contribution to defense costs cannot depend on its degree of contribution to the ultimate damages.

However, in a later ruling on damages for breach by a subcontractor of its defense obligation, the court adopted an approach that somewhat cheered the subcontractor community. The court held that the subcontractor's duty to defend began when the contractor filed a third-party action

as to provide indemnity beyond what is permissible under ORS 30.140, the clause is not necessarily void, but should simply be enforced only to the extent that indemnity is provided for by the negligence or fault of the indemnitor.

[2] Note that, if the plaintiff's allegations foreclose the plaintiff from offering evidence that the claimed damages arise from the fault of the subcontractor, the general contractor will have a hard time establishing an entitlement to a defense at all. *See Clarendon Nat. Ins. Co. v. Amer. States Ins. Co.,* 688 F. Supp. 2d 1186 (2010) (insurance carrier for subcontractor did not have obligation to defend general contractor under "additional insured" language where plaintiff's complaint alleged that damages were the "sole" fault of developer).

against the subcontractor, and ended when the owner and general contractor settled. The court also held that the subcontractor was only required to pay those defense costs for the "specific fees" "associated with [contractor] having to defend against allegations involving [the subcontractor's] work" and that the burden is on the *contractor* to identify what specific fees were incurred that "relate directly to defending against" those allegations. The court held that the general contractor had not met that burden and awarded no damages.

These combined rulings present a good news/bad news scenario for both general contractors and subcontractors. It will no doubt difficult for most lawyers defending an indemnitee to parse their time *after the fact*, as may have happened in the Washington County case. However, if the indemnitee's lawyers know from the beginning that they need to allocate their time, it may become clear that most if not all of the work in the defense of the contractor in the typical construction case is done because of the allegedly bad work of the subcontractors.

The court's approach may also prove to be unworkable or leave too many issues open for debate and argument between the indemnitor and indemnitee since bills are generated every month. Although the indemnitee's attorneys will no doubt be incentivized to delineate as much work as possible to dealing with the fault of one subcontractor or another, there is always defense work that cannot be tied neatly to one specific trade. A more efficient approach might be to presumptively allocate the defense of the indemnitee based on the number of indemnitors, and then attempt to reapportion defense costs at the end based on a review of bills for the entire case (if such matters are not simply resolved as part of a global settlement).

The Washington County court's decision is on appeal, and that appeal may resolve some of these issues. Absent further guidance from the appellate courts, construction lawyers (and the insurers for their clients) will continue to struggle with how to turn the expectations surrounding defense-indemnity clauses into reality.

Insurance Coverage and Construction Defect Claims

Tom Ped
Williams Kastner

Oregon law requires contractors to carry liability insurance, but that does not mean that coverage is always available for construction defect claims. In the recent case of *Parker v. American Family Insurance Company et al.*, 3:10-CV-1417-PK, 2013 U.S. Dist. LEXIS 9085 (Jan. 23, 2013), the Oregon district court held that the "owned-property" exclusion in a builder's liability policy excluded coverage for a homeowners' defect lawsuit.

ORS 701.073 states that licensed contractors shall have in effect public liability, personal property and property damage insurance covering the work of the contractor, including coverage for the contractor's completed operations, but subject to "applicable policy exclusions." A typical commercial general liability ("CGL") policy provides coverage for those sums an insured becomes legally obligated to pay as damages because of bodily injury or damage to the property of a third party.

CGL policies typically exclude coverage for property damage to property that "you own, rent or occupy." The "owned-property" exclusion prevents the policy from providing first party property insurance coverage. As the Washington Court of Appeals has noted:

> Third party insurance provides protection for the policyholder for liability it incurs to someone else, while first party insurance provides protection for losses to the policyholder's own property. An owned property exclusion prevents a CGL policy from providing first-party benefits to the insured. Thus, the exclusion bars coverage to the extent of losses to the insured's own property. There are no first party benefits under a policy with such an exclusion.
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> *State Farm Fire & Casualty Co. v. English Cove Associates, Inc.*, 121 Wn. App. 358, 368-69, 88 P.3d 986, (2004)

The *Parker* case is instructive for owners of commercial buildings and residential properties who may be contemplating bringing suit against a builder or developer for construction defects. In *Parker*, the defendant-builder had an insurance policy that was effective from June 1, 2004 to June 1, 2005. The evidence showed that the builder owned the property and the home that the builder constructed on it until the builder sold the home to the plaintiffs. The purchase and sale transaction closed on July 25, 2005, which was after the policy expired. United States District Judge Anna J. Brown held that the owned-property exclusion in the builder's policy applied and precluded coverage for the homeowners' construction defect claims.

Judge Brown's ruling was based on an earlier Oregon Court of Appeals decision finding that the owned-property exclusion was unambiguous and prohibited coverage for damage done to property owned by the named insured. *Baumann v. N. Pac. Ins. Co.,* 152 Or. App. 181, 187-89, 952 P.2d 1052 (1998). Thus, it appears unlikely that any further challenges to the application to the owned-property exclusion in Oregon (whether in state or federal court) will succeed.

In addition, in *Clarendon Am. Ins. Co. v. State Farm Fire & Cas. Co*., 3:11-CV-01344-BR, 2013 U.S. Dist. LEXIS 880 (Jan. 3, 2013), the court held that coverage was excluded even as to an insured property owner's construction manager. In that case, the court ruled that an insurer under an apartment insurance policy had no duty to defend claims alleged against the apartment owner's construction manager. Although the manager was not expressly named as an insured on the policy, it nonetheless qualified as an insured under the definition of "insured," which included "any person, other than your employee, or your organization while acting as your real estate manager."

The *Clarendon* case makes clear that even a party that never owned the subject property may be barred from obtaining a defense or indemnification for defect claims, under the owned-property exclusion. It is thus imperative for building owners' and their attorneys to carefully and thoroughly investigate the available insurance coverages to the greatest extent possible prior to filing suit.

In instances where the developer or builder ceased operations and went out of business shortly after completing a project, where no policies were procured subsequent to the coverage that was in place during the time of construction, and the owner or purchaser did not obtain the title to the property until after the policy expired, there may be no insurance coverage for any construction defect claims. This may be true even for individuals and entities who partnered in the development of a project and never held the title to the land or buildings.

Owner and Developer Licensing: A Trap for the Unwary

Tyler Storti & Kathryn Walter
Stewart, Sokol & Gray

General and specialty contractors directly involved with constructing or remodeling improvements to real property in the State of Oregon are generally aware that they are required to hold proper contractor licenses issued by the Oregon Construction Contractors Board ("CCB") in order to perform their work. Licensing requirements can sometimes be less clear for individuals and entities that own and/or are involved in developing real property. However, owners and developers failing to comply with licensing requirements may be exposed to the same consequences, which can include fines, CCB sanctions and the inability to file construction lien claims and pursue other legal remedies. This

article explains when owners and developers must be licensed (and when they may be exempted from licensure), and also summarizes the main penalties for their failure to do so.

1. When Are Owners and Developers Required to Maintain a CCB License?

Under the licensing statutes and regulations, the labels "owner" and "developer" are not determinative of the issue of whether a license is necessary. The term "Owner" is not specifically defined. Interestingly, a "Developer" is defined as "***a contractor*** that owns property or an interest in property and engages in the business of arranging for construction work or performing other activities associated with the improvement of real property, with the intent to sell the property." ORS 701.005(3) (emphasis added). The characterization of a "developer" as a subset of "contractor" implies that developers are likely required to be licensed, and the categories of license endorsements specifically designated for developers support that implication. ORS 701.021 (listing endorsements for "residential developer' and "commercial developer").

A. Activities Requiring Licensure

Rather than labels and definitions determining the issue, the statutory and regulatory scheme looks to the types of activities the particular person or entity is performing, regardless of label. Specifically, the main licensing statute provides that any person who "undertakes, offers to undertake or submits a bid to do work as a contractor" must have a CCB license. ORS 701.021(1). The term "contractor" is broadly defined to include a number of activities, including the following which are related to roles traditionally occupied by owners and developers:

> (a) A person that, for compensation or with the intent to sell, arranges or undertakes or offers to undertake or submits a bid to construct, alter, repair, add to, subtract from, improve, inspect, move, wreck or demolish, for another, a building, highway, road, railroad, excavation or other structure, project, development or improvement attached to real estate, or to do any part thereof.
>
> (b) A person that purchases or owns property and constructs or for compensation arranges for the construction of one or more residential structures or small commercial structures with the intent of selling the structures. ORS 701.005(5)(a)-(b).

ORS 701.031(1) provides that it is prima facie evidence of "doing business as a contractor" if a person, (a) for that person's own use, performs, employs others to perform or "for compensation and with the intent to sell the structure" arranges to have performed any work described in ORS 701.005(5) (which is the definition of "contractor"), and (b) within any 36-month period offers for sale two or more newly built structures.

The CCB has promulgated additional rules that further define what it means to do "work as a contractor." Relevant to the current discussion about owners and developers, OAR 812-002-0760(3) provides that "work as a contractor" includes "construction management" activities. "Construction management" is defined as "the coordinating of a construction project, including, but not limited to, selecting contractors to perform work on the project, obtaining permits, scheduling specialty contractors' work, and purchasing materials." OAR 812-002-0760. Thus, an owner or developer involved in managing and overseeing the progress of work is required to have a license. Also considered "work as a contractor" is the "[i]mprovement of lots with the intent of selling lots with structure(s)." OAR 812-002-0760(5). This "intent to sell" element commonly appears throughout the statutory scheme as an indicator that a license is required. *E.g.,* 701.031(1).

B. Exceptions to Licensure

ORS 701.010 lists several exemptions to the licensing requirement. The most relevant exemptions to the current discussion are the following three, which apply to certain activities often performed by owners and developers:

> (5) An owner who contracts for work to be performed by a licensed contractor. This subsection does not apply to a person who, in the pursuit of an independent

business, constructs, remodels, repairs or for compensation and with the intent to sell the structure, arranges to have constructed, remodeled or repaired a structure with the intent of offering the structure for sale before, upon or after completion. It is prima facie evidence that there was an intent of offering the structure for sale if the person who constructed, remodeled or repaired the structure or arranged to have the structure constructed, remodeled or repaired does not occupy the structure after its completion.

(6) An owner who contracts for one or more licensed contractors to perform work wholly or partially within the same calendar year on not more than three existing residential structures of the owner. This subsection does not apply to an owner contracting for work that requires a building permit unless the work that requires a permit is performed by, or under the direction of, a residential general contractor.

(7) A person performing work on a property that person owns or performing work as the owner's employee, whether the property is occupied by the owner or not, or a person performing work on that person's residence, whether or not that person owns the residence. This subsection does not apply to a person performing work on a structure owned by that person or the owner's employee, if the work is performed in the pursuit of an independent business with the intent of offering the structure for sale before, upon or after completion. ORS 701.010(5)-(7).

Subsection (5) exempts traditional property owners who contract with licensed contractors to perform the construction work, but carves out of that exemption property owners who are in the business of improving and selling residential real property. With respect to this subsection, the courts have drawn a fairly bright line that the carve-out is meant to "include residential developers . . . while excluding individual residential property owners who are not in the business of constructing and selling real property." *Tandem Properties, LLC v. Construction Contractors Board*, 184 Or App 28, 35 (2002).

In analyzing ORS 701.010(5), the Court found that owners or developers must be licensed if they do all of the following: "(1) arrange to have a building constructed, (2) in the pursuit of an independent business, (3) for compensation, and (4) with the intent to sell the structure before, upon or after completion." *Id.* at 33. The Court further elaborated on the meaning of "compensation," concluding that the only reasonable interpretation was "profit gained from a sale as well as payment or remuneration for work done." *Id.* at 34. The Court also noted that the "independent business" requirement is met if the owner is involved in "a commercial or industrial enterprise," and that the requirement "functions to include residential developers within the licensing scheme while excluding individual residential property owners who are not in the business of constructing and selling real property." *Id.* at 35.

The Court further explained:

> Under the statutory scheme, owners of property who arrange for work to be done on residences that they occupy with the intent of later offering the structure for sale are excluded from the licensing requirements because they are not in the "business" of developing and selling real property. *Id.*

Thus, where a property owner develops property with intent to sell, and does so in the course of its business, that owner qualifies as a contractor and must hold an appropriate license, but an individual owner of a single lot who hires a licensed contractor to build a residence for the owner to occupy does not (even if the owner may later sell the property).

The exemption in ORS 701.010(6) excludes from the licensing requirements those owners who contract with licensed contractors to perform work on their residences, so long as it is on not more than three such structures in one calendar year. On projects where a building permit is required, this exemption does not apply, unless the owner hires a general contractor to perform the permitted work.

The exemption (and limitation to that exemption) in ORS 701.010(7) also suggests that the distinction between whether a license is required or not depends on whether the owner is in the business of property development and whether the owner's intent for a specific project is to sell it for profit.

The Oregon Court of Appeals considered this provision in *Justice v. Builder's Board, Department of Commerce*, 47 Or App 487 (1980), and noted that the exemption "was not intended to exempt from the registration requirement persons engaged in the business of building homes for sale." 46 Or App at 490. The Court explained that the exemption "applies to 'persons' other than 'builders' doing work as an owner or tenant of residential property which is intended for sale." *Id.* at 491 (holding that the CCB had jurisdiction to hear a homeowner's complaint, where the homeowner had purchased his home from a builder who built the home on property formerly owned by the builder).

Another law that owners and developers looking to take advantage of the licensing exemptions should also be aware of is ORS 701.042, which provides that a developer 1"(1) [s]hall act ***only*** in association with ***licensed*** general contractors, one or a combination of whom must have ***sole*** responsibility for overseeing all phases of construction activity on a property; and (2) [m]ay not perform any construction work on a property." ORS 701.042. This section reaffirms that unlicensed property owners must not only refrain from performing construction work, but must only engage licensed contractors who must have sole responsibility for overseeing the construction and engaging in construction management.

2. What Are the Consequences for Failing to Maintain a License?

Owners and developers are incentivized to comply with the licensing requirements in various ways, including exposure to potential civil penalties, being precluded from filing liens, and from pursuing legal remedies in the courts or with the CCB. In enforcing such punishments, Oregon courts have warned that ORS Chapter 701 is "a remedial statute, made for the protection of the building business and of people dealing with builders who might be irresponsible. Therefore, it should be read as a whole and liberally construed to accomplish its purpose." *Robinson v. Builders Board of Oregon*, 20 Or App 340, 343 (1975).

A. Civil Penalty

The CCB has authority to revoke, suspend, or refuse to issue or reissue a license and to "assess a civil penalty as provided in ORS 701.992 if the board determines after notice and opportunity for hearing that any person has violated ORS 701.021," which is the main licensing statute. ORS 701.098(3). Pursuant to ORS 701.992(1), the penalties may be assessed "in an amount determined by the board of not more than $5,000 for each offense."

The CCB has promulgated various guidelines for the assessment of civil penalties. For example, violations of ORS 701.021 carry a penalty of $1,000 per offense "when the Board has no evidence that the person has worked previously without having a license and no consumer has suffered damages from the work." OAR 812-005-0800(3). That penalty may be reduced to $700 if a license is obtained within a specified time. *Id.* On the other hand, the penalty may be increased to $5,000 per violation of ORS 701.021 when a complaint has been filed for damages caused by performance of the unlicensed work. OAR 812-005-0800(4)(a).

In addition, violation of ORS 701.021 is classified as a Class A misdemeanor, ORS 701.990(1), and this potentially subjects the violator to another fine, not to exceed $6,250. ORS 161.635(1)(a). However, that penalty does not apply to corporations. ORS 161.635(4).

A failure to obtain the proper endorsement may also result in the assessment of civil penalties, but likely will not bar a contractor from filing a lien, commencing a lawsuit or pursuing its other legal remedies. In *Edwards v. Perry*, a contractor was licensed, but failed to obtain the proper endorsement. The court held that "[a] contractor's failure to register in a particular category as required by the Board's rules exposes the contractor to penalties . . . for violating the rule, but it does not trigger" the statute barring a

contractor from maintaining an action to recover compensation for the construction work performed. 130 Or App 165, 169 (1994).

B. Inability to Pursue Legal Remedies

Perhaps more catastrophic than potential civil penalties are the legal remedies unlicensed owners and developers may be precluded from pursuing. ORS 701.131(1) provides:

> [A] contractor may not perfect a construction lien, file a complaint with the [CCB] or commence an arbitration or a court action for compensation for the performance of any work or for the breach of any contract for work that is subject to this chapter, unless the contractor had a valid license issued by the board and properly endorsed for the work performed.

This bar has been rigorously enforced by the CCB and the courts. *See, e.g.*, *Tandem Properties*, 184 Or App at 35 (upholding CCB's dismissal of property owner's claims against a licensed contractor because the property owner was required to have a license before its claims could be heard). The claims bar applies to claims in both tort and contract. In *Bannister v. Longview Fibre Co.*, the Court construed an earlier version of ORS 701.131 (numbered ORS 701.065) and held that "persons subject to the statute 'cannot avoid the prohibition contained in ORS 701.065 by the labels or legal theories they employ.'" 134 Or App 332, 337 (1995) (quoting *Roelle v. Griffin*, 59 Or App 434, 437 (1982)). The claims bar will not apply to contracts that are not construction contracts covered by ORS Chapter 701. *MacLean & Associates, Inc. v. American Guaranty Life Ins. Co.*, 85 Or App 284 (1987) (holding that ORS 701.065 did not apply to a contractor's action against a resort owner for breach of a franchise agreement, which was not a contract covered by ORS Chapter 701).

ORS 701.131(2) sets forth several exceptions to the above-described bar. The first exception deals with awareness of the requirement to be licensed and the prompt remediation by obtaining a license, prior to pursuing its legal remedies. ORS 701.131(2)(a). For the claims bar not to be enforced in this circumstance, enforcement of the bar must "result in substantial injustice to the contractor." ORS 701.131(2)(a)(C).

This exception was considered in *Remington Ranch, LLC v. Hooker Creek Cos., LLC*, 2010 Bankr. LEXIS 3167 (Bankr. D. Or. Sept. 24 2010), where the Court found that the claimant obtained a license more than three months after filing a lien claim, and that "ORS 701.131(2)(a) requires a contractor to be licensed by the CCB at the time it perfects a lien . . . [or else] the lien is a nullity."

The second exception applies where a contractor was "licensed by the board for some but not all of the times required" and timely completed an application for license renewal upon notice of the lapse "to include the entire time period for which a license was required." ORS 701.131(2)(b). This exception has not been elaborated on by the courts.

The third exception will not bar a proceeding that:

(A) Is directed against a person or entity that:

> (i) Is subject to this chapter;
>
> (ii) Provides construction or design labor or services of any kind; or
>
> (iii) Manufactures, distributes, rents or otherwise provides materials, supplies, equipment, systems or products; and
>
> (B) Arises out of defects, deficiencies or inadequate performance in the construction, design, labor, services, materials, supplies, equipment, systems or products provided.

ORS 701.131(2)(c).

One Oregon appellate case offers meaningful insight into the purpose of this particular provision, *Pincetich v. Nolan*, 252 Or App 42 (2012). In this opinion, the Court of Appeals stated that "[c]onsistently with its text, context, and history, we conclude that ORS 701.131(2)(c) applies to construction-defect proceedings and, consequently, to claims involving

services whose inadequacy contributed to the defects that are the subject of the proceedings." 252 Or App at 49. The Court of Appeals also analyzed the legislative history for that subsection, noting that it was added "to further benefit consumers by providing authority for unlicensed contractors to pursue third-party claims in construction-defect cases.

The concern that motivated the proponents of the exception to ask the legislature to adopt it was that the claims bar in ORS 701.131(1) could prevent unlicensed contractors from pursuing third-party claims in cases in which consumers sued them for damages for construction defects" and that "[b]y lifting the bar to allow unlicensed contractors to bring third-party claims against others whose actions had caused or contributed to construction defects, the provision was intended to allow contractors to recover funds from other responsible parties and to thereby better ensure that affected consumers were made whole." 252 Or App at 47-48.

The U.S. District Court for the District of Oregon also interpreted this exception to the claims bar with similar results. *Stellar J. Corp. v. Smith & Loveless, Inc.*, 749 F. Supp.2d 1137 (D. Or. 2010) (affirming dismissal of unlicensed subcontractor's counterclaim against general contractor and rejecting subcontractor's argument that exception to claims bar applied). The Court noted that the exception "applies to construction defects, and was enacted to protect consumers who have contracted with unlicensed contractors and are damaged because of defective goods or services provided by the unlicensed contractor's vendors or subcontractors." 749 F. Supp.2d at 1144. The Court continued that the subsection "is intended to avoid situations in which the damages caused by construction defects exceed the amount of insurance otherwise available from those parties who have contributed to the defects but who avoided liability simply because the party with whom they contracted was not licensed," and that "[t]here is no support for the conclusion that this subsection applies where, as here, an unlicensed contractor seeks damages from another contractor." *Id.* The Court also noted that its application in that case would "swallow the rule," because under the subcontractor's interpretation "the licensing requirement would be eliminated any time a contractor brought a claim against another contractor" and that "[t]here is no support for the conclusion that the subsection was intended to have this vast reach." *Id.* at 1144-1145.

Neither the *Pincetich* nor *Stellar J* case involved the analysis of whether the exception in ORS 701.131(2)(c) would apply to allow claims by an unlicensed owner or developer against a contractor for construction defects. The plain language of the exception could be argued to support such an application, since the claim might be directed against a general or specialty contractor subject to the licensing statutes.

However, allowing a developer who was otherwise required to be licensed (because it performed "construction management" activities and/or intended to sell the property following construction) to file a construction defect action against a contractor on the job is not necessarily consistent with the purpose of the exception as discussed in the legislative history and case law, which is to protect consumers by allowing unlicensed contractors to file third-party claims in order to bring lower tier parties and their insurers into lawsuits. Owners, developers and their attorneys should monitor legislation and future case law construing this exception for guidance on this issue.

Conclusion

All property owners and developers undertaking construction, remodeling or development projects should carefully consider whether their activities fall within the categories requiring them to be licensed with the CCB. When in doubt, it is probably prudent to err on the side of caution and to obtain a license. Failure to comply could have serious negative consequences that far outweigh the burdens of applying for a license.

Keep Records: Don't Waive Claims on ODOT Projects

Dan Gragg
Jennifer Schenck
Seifer Yeats Zwierzynski & Gragg

The Oregon Department of Transportation (ODOT) has proposed a fairly onerous new administrative rule, OAR 731-005-0780. Contractors who work with ODOT need to be fully aware of this proposed rule and how it affects their record keeping practices on ODOT projects. The proposed rule requires all contractors, subcontractors, and material suppliers to maintain records relating to the project for a period of not less than: (1) three years after final payment, or (2) until the conclusion of any audit, or (3) the conclusion of proceedings relating to the project, whichever is later. A non-inclusive list of the types of records that must be maintained, including bid estimates and records identifying equipment used, is included in the proposed rule. Records may be maintained electronically, but those subject to the rule must allow ODOT to inspect or copy the records and should be prepared to provide access within a reasonable time.

As with other ODOT records, these materials have the potential to become "public records" subject to disclosure under ORS Chapter 192. In order to prevent such disclosures, if a record keeper believes that a record is exempt from disclosure due to its status as a "trade secret," it must clearly designate the records as such and cite the supporting authority. Once designated as "trade secret," ODOT will keep the records confidential unless they are required to disclose such by law or have obtained consent to disclose them from the record keeper. However, once ODOT forwards a notice of public record request to the record keeper, the record keeper must intervene to seek its own protective order against disclosure of the records.

While contractors do not waive claims by failing to comply with the proposed rule's requirements, ODOT has indicated that it intends to include language to this effect in the "special conditions" of its contracts. This as yet undisclosed condition may push similar record keeping obligations down the contract chain to subcontractors and material suppliers as well. Prime contractors will need to insure that they pass through the obligations and perhaps be prepared to protest this waiver language during the bid process.

Due to the fact that the legislature considered and ultimately denied including the waiver language in the proposed rule, ODOT's addition of this language to its contracts raises a question as to whether it has skirted the administrative rulemaking process. Lawyers whose clients work on ODOT projects should consider this issue in the event that ODOT asserts waiver based on language that is not part of the rule.

Construction Law Section
Executive Committee

Pete Viteznik, Chair:
pviteznik@kilmerlaw.com
Jason Alexander, Chair-Elect:
jason@sussmanshank.com
James Van Dyke, Past Chair:
Jim.VanDyke@portlandoregon.gov
Dan Gragg, Secretary:
gragg@seifer-yeats.com
Tara Johnson, Treasurer:
taraj@seifer-yeats.com

Members at Large:
Fritz Batson: *batson@gleaveslaw.com*
Doug Gallagher: *doug@dglawoffice.com*
Timothy Dolan:
timothymdolan@oregoncoast.com
Dan Duyck: *dduyck@whippleduyck.com*
Erika George: *Erika.george@portlandoregon.gov*
Katie Jo Johnson: *katiejoj@mcewengisvold.com*
Darien Loiselle: *dloiselle@schwabe.com*
Heather McNamee:
hmcnamee@gibsonpeabody.com
Tom Ped: *tped@williamskastner.com*
Tyler Storti: *tstorti@lawssg.com*
Jeremy Vermilyea; *jvermilyea@schwabe.com*
Curtis Welch: *cwelch@dsw-law.com*

Newsletter Editor:
Alan Mitchell: *alan@mitchell-lawoffice.com*

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