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MESSAGE FROM THE CHAIR

Pete Viteznik
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Hello, and welcome to the first Construction Law Newsletter of 2013. As the incoming Chair of the Construction Law Section of the Oregon State Bar, I want to welcome you to a great resource for all lawyers who practice in the construction arena. Please feel free to contact me at any time with any suggestions on how YOUR Construction Law Section can improve and assist you in your practice.

We have an active Section with many opportunities to learn and participate. We hope to see you (frequently) during the course of the year. More importantly, we hope to hear from you with suggestions during the course of the year.

This year our focus will be on outreach and assistance to our members. Our ongoing "Brown Bag" lunch series is designed to touch on topical issues. We will host a CLE in October covering legal issues on both the Washington and Oregon side of the river for those practitioners working in both jurisdictions. And, of course, our newsletter (under the guidance of Alan Mitchell, our Section editor) will continue to keep us abreast of the ever-changing legal environment.

With the effects of the Great Recession seemingly over (at least we hope), construction activity in our State is once again picking up. Now that the industry is waking up once again, we want to be sure that all Section members have access to the resources they need to succeed.

The ongoing legislature is in session this year, and your Section will be monitoring and counseling legislation important to the construction industry. Our efforts will be on a neutral, non-partisan basis to achieve consistence and certainty in how statutes are applied. Please regularly check in with our website for updates as the legislature proceeds through session.

Remember, your Section is a resource. We have a diverse Board, a large membership, and ambitious goals. We hope you have enjoyed our efforts in recent years, and are thankful for the past leadership of our Committee and Chair, including Jim Van Dyke and his predecessors, who have left a legacy of durability in the Construction Bar. We are excited about this year; we hope you are, too.

Thanks again for your support, and please let us know what we can do to assist you with additional resources, CLEs, and other help.

CONTRACTUAL AGREEMENTS TO ELIMINATE THE DISCOVERY RULE?

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On January 30, 2013, the Oregon Court of Appeals issued a decision confirming that AIA A201 Section 13.7 governs when both negligence and contract claims begin to accrue. Prior to the

decision in *Wood Park Terrace Apartments v. Tri Vest, LLC*, 254 Or App 690 (2013), whether or not negligence actions were subject to Section 13.7 varied, depending on the county you were in and the judge who was hearing your case.

The decision relies on the premise that parties to a construction contract can modify a statutory limitation period or even waive the right to a discovery period triggering the accrual of a claim. As of the date this article was written, Plaintiff was intending to file a Petition for Review of the Court of Appeals decision with the Oregon Supreme Court.

The facts of the case and the decision are as follows.

A. Facts

In August, 1999, construction began on an affordable housing community located in Marion County Oregon, that would come to be known as the Wood Park Terrace Apartments ("Wood Park"). The general contractor for the apartments was Tri-Vest, LLC ("Tri-Vest"). Wood Park and Tri-Vest entered into an AIA Standard Form of Agreement Between the Owner and Contractor, which incorporated the AIA A201 (1987) General Conditions. The General Conditions include Section 13.7, entitled "Commencement of Statutory Limitation Period," which provides the following language:

13.7.1 As between the Owner and Contractor:

> **.1 Before Substantial Completion.** As to acts or failures to act occurring prior the relevant date of Substantial Completion, any applicable statute of limitations shall commence to run and any alleged cause of action shall be deemed to have accrued in any and all events not later than such date of Substantial Completion.

Procedural History

Construction of the apartments began in August of 1999, and the architect for the apartments signed a certificate of substantial completion on April 3, 2000.

In 2008, the owner of the apartments discovered what it believed to be, "systemic catastrophic building envelope deficiencies," in the construction of the apartments. On February 17, 2010, the owner plaintiff filed an action for negligence, negligence per se, and nuisance against the general contractor for the project, Tri-Vest.

Defendant Tri-Vest filed a motion for summary judgment, claiming that under Section 13.7 of the construction contract, any claims related to the construction of the project began to run on April 3, 2000, the date of Substantial Completion. On March 21, 2011, the Circuit Court granted Tri-Vest's motion for summary judgment, finding that Section 13.7 modified any discovery rule for negligent construction, and that any claims arising from construction of the apartments had expired as of April 3, 2006.

The Circuit Court also found that Section 13.7 operated as an accrual provision for all claims, not just claims in tort. On January 30, 2013, the Court of Appeals affirmed the Circuit Court's decision. The Court of Appeals' written opinion addresses two key arguments : 1) Section 13.7 of the AIA A201 1987 operates as an accrual of all claims, whether in negligence or contract; and 2) that section does not operate as a waiver of claims.

The Court of Appeals noted that there was nothing in the text of Section 13.7 which would suggest a limitation of that accrual provision to contract claims only. The Court analyzed the plain language of the clause and the liberal use of the word, "any," i.e "any applicable statute of limitations," and "any alleged cause of action." *Id.* at 693. The Court also noted the absence of any language in the contract limiting the application of the clause to certain types of actions. *Id.*

The Court rejected plaintiff's argument that the court's interpretation could not reconcile with the remedy-reservation clause contained in Section 13.4.1, stating, "[o]ur interpretation gives effect to the plain language of both the remedy-reservation clause and the accrual clause, and is

supported by the long-held understanding that parties are free to contractually modify extra-contractual claims and the timeframes in which to bring them." *Id.* at 694 (citations omitted.)

Plaintiff also argued that Section 13.7 as applied to negligence claims would operate as a waiver of those claims, and that contracts could not be construed to waive remedies without a "clear and unequivocal expression," of that waiver, relying on *Estey v. MacKenzie Engineering, Inc*., 324 Or. 372 (1996). The Court of Appeals rejected that argument, acknowledging, "the practical result of applying the accrual clause is that plaintiff's negligence claims are time barred. But that result stems from plaintiff's failure to timely file its claims, not from any contractual provision that deprived plaintiff of negligent remedies altogether." *Id.* at 695.

B. Items of Interest About Wood Park Terrace

1. This case is the first Oregon Court of Appeals case recognizing that Section 13.7 of the 1987 AIA A201 General Conditions applies to claims in negligence as well as contract. Although not addressed by the Court of Appeals, the Circuit Court acknowledged this in its letter opinion on summary judgment, indicating that "multiple courts of other jurisdictions throughout the country have held the AIA accrual clause applies to claims for breach of contract and negligence."

2. The standard of review on appeal was only for "errors of law." It is interesting to note that the Circuit Court weighed the following facts at summary judgment in issuing its opinion:

   - The Plaintiff personally reviewed the Contract prior to signing, and had the assistance of an attorney.
   - The parties had the opportunity to make several changes to the Contract prior to signing, which were documented as changes or addendums. This was evidence of a "bargained for" contract.
   - "Plaintiff chose and required an AIA form contract that had been in existence and used throughout the country since 1987."
   - The accrual provision was not inconspicuous or difficult to locate.

3. At summary judgment, the parties did not dispute that the statute of limitations for Plaintiff's claims was the six year statute of limitations contained in ORS 12.080(3) for all of Plaintiff's claims. On appeal, Tri-Vest argued that under *Abraham v. T Henry Construction, Inc*., 350 Or 29 (2011), the two year statute of limitations contained in ORS 12.110 may apply as opposed to ORS 12.080(3). The Court of Appeals steered clear of the issue, mentioning it only in a footnote, and made no decision as to the applicability of either statute of limitations. *Id.* at fn. 1.

4. The AIA tends to publish new contract forms every ten years, including updated versions of the A201 General Conditions. Section 13.7 of the 1997 A201 General Conditions contains identical language to the 1987 A201 General Conditions upon which *Wood Park Terrace* was decided. However, Section 13.7 of the 2007 A201 General Conditions was completely rewritten, and promulgates as the default rule the law of the controlling jurisdiction and creates a ten year statute of ultimate repose. It provides as follows:

   13.7 TIME LIMITS ON CLAIMS

   The Owner and Contractor shall commence all claims and causes of action, whether in contract, tort, breach of warranty or otherwise, against the other arising out of or related to the Contract in accordance with the requirements of the final dispute resolution method selected in the Agreement **within the time period specified by applicable law, but in any case not more than 10 years after the date of Substantial Completion of the Work**. The Owner and Contractor waive all claims and cause of actions not commenced in accordance with this Section 13.7. (**emphasis added**)

Conclusion

The Circuit Court in granting summary judgment to Tri-Vest put a lot of weight into the bargaining power of the parties, and noted a few times in its letter opinion that these were sophisticated parties involved in an arms-length transaction. A court deciding whether an accrual provision such as the one in the 1987 and 1997 versions of the A201 will undoubtedly look at these and similar factors.

The relevance of the *Wood Park Terrace* decision in terms of the AIA contract forms has limited relevance due to the changes to the AIA forms. As discussed above, Section 13.7 was substantially modified over five years ago. Of course, *Wood Park Terrace* is a reminder that even two sophisticated parties with the assistance of an attorney can use a twelve year old AIA form contract. If anything, *Wood Park Terrace* is a good example of why parties to an AIA contract need to figure out which year the contract and general conditions were published and what protection that provides them.

Unfortunately, Section 13.7 of the 2007 AIA 201 General Conditions, with the language that claims are to accrue, "within the time period specified by applicable law," really does not provide much assistance in determining when the statute of limitations for construction claims begins to accrue for contracts entered into in Oregon, at least for the time being.

Fortunately, as recognized by the trial court in *Wood Park Terrace*, supra, the AIA forms are often edited by the parties entering into them. If using the 2007 AIA A201 General Conditions, the parties to the contract can take out the broad language and specify an accrual period, i.e. two years, in order to eliminate any uncertainty. If using the 1987 or 1997 forms, parties should realize that they are bargaining for the elimination of a potential discovery rule in any negligence action, and should modify the form accordingly if this is not their intention.

ACCORD AND SATISFACTION; EXECUTORY ACCORD; AND SUBSTITUTED CONTRACT

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The doctrine of accord and satisfaction is a common legal theory. However, there are two related legal doctrines--executory accord and substituted contract--that are less well known and less pled. The distinction among these three theories is important in litigation for purposes of proof, and also for determining whether there is a right to a jury for a defense or claim.

This article discusses the distinctions among these three theories, and also discusses ORS 73.0311, an important statute governing accord and satisfaction in relation to negotiable instruments.

1. Accord and Satisfaction

Oregon courts describe a valid accord and satisfaction as follows:

> ". . . what is given or agreed to be performed shall be offered as a satisfaction and extinction of the original demand: that the debtor shall have intended [it] as a satisfaction of such obligation, and that such intention shall be made known to the creditor in some unmistakable manner. It is equally essential that the creditor shall have accepted it with the intention that is should offer it as a satisfaction." *Gen. Constr. Co. v. Ore. Fish Comm.*, 26 Or.App. 577, 582, 554 P.2d 185 (1977) (*citing Lenchitksy v. W. J. Sandberg Co.*, 217 Or. 483, 343 P.2d 523 (1959)).

General Construction involved a dispute between the State Fish Commission and the general contractor, General Construction, arising out of a project involving construction of a fish ladder at Willamette Falls on the Willamette River between West Linn and Oregon City.

After General Construction had started construction of the fish ladder in July 1969, it discovered significant errors in the specifications and drawings provided by the Defendant Fish Commission. The errors required new surveying and engineering, as well as changes to work already done, which delayed construction significantly and at a greatly increased cost. The fish ladder was not complete in the fall of 1969, when water overtopped the dam and General Construction's work was damaged by the overflowing water.

In March and April 1970, General Construction and the State Fish Commission signed a change order which increased the contract price, and specified certain changes in the plans. The change order did not state it was General Construction's exclusive remedy for all damages arising from the inaccurate specifications, nor did it state that General Construction reserved its right to collect further damages.

The State Fish Commission contended that the change order was an accord and satisfaction by which General Construction signed away all its rights of recovery for extra costs resulting from the State Fish Commission's mistakes in design and errors in specifications. General Construction argued that the sum paid under the change order was intended only to cover costs of the specific changes described in the change order, since at the time the change order was executed, the parties had no idea what other damages would result from the delay or from damage to General Construction's work by overflow of the river during the period of delay.

The Court of Appeals rejected the State Fish Commission's argument and held that the change order (and a letter which accompanied the change order) did not make it known to General Construction "in some unmistakable manner that Change Order No. 1 was agreed or intended to be an accord and satisfaction for all damages resulting from the inaccurate specifications and consequent delay." *General Construction*, 26 Or. App. at 583.

2. Executory Accord and Substituted Contract

An executory accord is "an agreement for the future discharge of an existing claim by a substituted performance." *McDowell Welding & Pipefitting, Inc. v. U.S. Gypsum Co*., 345 Or. 272, 281, 193 P.3d 9 (2008) (*citing* Arthur Linton Corbin, *6 Corbin on Contracts* § 1268, 71, 2d ed. 1962)). The *McDowell* court stated that an executory accord is usually "a bilateral agreement; the debtor promises to pay an amount in return for the creditor's promise to release the underlying claim", and that the underlying claim is not discharged until the new agreement is performed. *McDowell*, 345 Or. at 281. Under an executory accord "the right to enforce the original claim is merely suspended and is revived by the debtor's breach of the new agreement." *Id* at 282 (*citing Savelich Logging v. Preston Mill Co.*, 265 Or. 456, 462, 509 P.2d 1129 (1973)).

A substituted contract, on the other hand, exists when the parties "agree to substitute the new agreement for the underlying obligation." *McDowell*, 345 Or. at 283. (*citing 6 Corbin on Contracts* § 1293 at 185)). The court stated that "[a] substituted contract differs from an executory accord in that the parties intend that entering into the new agreement will immediately discharge the underlying obligation." *McDowell*, 345 Or. at 283 (*citing Eagle Industries, Inc. v. Thompson*, 321 Or. 398, 408-12, 900 P.2d 475 (1995)).

In *McDowell*, the plaintiff McDowell Welding & Pipefitting, Inc. ("McDowell") sued the general contractor BE & K Construction Co. ("BE & K") and the project owner United States Gypsum Co. ("U.S. Gypsum") alleging that the defendants failed to pay for work done by McDowell for a new plant constructed for U.S. Gypsum. Defendants alleged as an affirmative defense that McDowell had agreed to release its claims against defendants in return for payment of $896,000, and counterclaimed for specific performance of that settlement agreement.

Defendant BE & K filed a motion asking the trial court to bifurcate proceedings and try its counterclaim for specific performance before

trying McDowell's claims for breach of the construction contract. BE & K also argued that because its counterclaim sought specific performance, the court, rather than a jury, should resolve the factual issues that the counterclaim raised. The trial court granted BE & K's motion. The trial court also granted BE & K's motion to strike McDowell's subsequent demand for a jury.

The trial court, sitting as trier of fact, found that McDowell had accepted defendants' offer to settle its claims in return for the defendants' promise to pay plaintiff $800,000. (Even though defendants had alleged they promised to pay $896,000, the defendants proved and the trial court found that the promise was to pay only $800,000). The trial court entered a limited judgment directing defendants to tender $800,000 to the court clerk, and directing McDowell, following defendants' tender, to execute a release of its claims against defendants. The trial court then granted defendants' motion for summary judgment dismissing McDowell's breach of contract claim arising out of the parties' construction contract.

On appeal, McDowell argued, among other things, that the trial court had erred in denying its jury demand on the question of whether it had accepted the defendants' settlement offer. The Supreme Court analyzed the issue in terms of whether McDowell had a right to a jury trial on the counterclaim for specific performance, and if there was not a right to a jury trial on that counterclaim, whether McDowell had a right to a jury trial on defendants' affirmative defense, which was also based on the settlement agreement. The Court also stated that it needed to determine, if in fact there was a right to a jury trial on the affirmative defense, whether the trial on that defense should have occurred before trial on the defendants' counterclaim for specific performance.

The Supreme Court analyzed whether defendants had pled an executory accord, an accord and satisfaction, or a substituted contract. The Court held that the defendants had not alleged an accord and satisfaction because defendants had not alleged "that they had paid plaintiff the promised sum—an allegation necessary for an accord and satisfaction." *McDowell*, 348 Or. at 283 (*citing Harding v. Bell*, 265 Or. 202, 210, 508 P.2d 216 (1973).

Further, the Court stated that defendants had not alleged a substituted contract, because defendants did not "allege that, by entering into the settlement agreement, they extinguished the underlying obligation—an allegation necessary to allege a substituted contract." *McDowell*, 348 Or. at 283-84 (*citing Abrahamso v. Brett*, 143 Or. 14, 24, 21 P.2d 229 (1933)).

The Court concluded that defendants had alleged an executory accord, because "defendants alleged that plaintiff agreed to release its claims only after defendants made the promised payment." *McDowell*, 348 Or. at 284. The Court held that since the substance of defendants' counterclaim and affirmative defense alleged an executory accord, the counterclaim and affirmative defense were equitable, and therefore the Court held that the trial court did not error in striking McDowell's jury demand. *Id.* at 286-87.

The Court also noted that, in contrast to an executory accord, the theories of accord and satisfaction and substituted contract are legal, not equitable, theories.

3. ORS 73.0311

ORS 73.0311 provides as follows:

> "The negotiation of an instrument marked 'paid in full', 'payment in full', 'full payment of a claim' or words of a similar meaning, or the negotiation of an instrument accompanied by a statement containing such words or words of similar meaning, does not establish an accord and satisfaction that binds the payee or prevents the collection of any remaining amount owed upon the underlying obligation unless the payee personally, or by an officer or employee with actual authority to settle claims, agrees in writing to accept the amount stated in the

instrument as full payment of the obligation."

The statute obviously restricts a debtor's attempts to settle unliquidated claims by unilateral conduct. Regardless, a creditor should proceed cautiously if it receives a check or other negotiable instrument for a reduced sum, with language on it or on an accompanying letter to the effect that endorsement or deposit of the check or instrument constitutes an agreement by the creditor to accept the check in full settlement of claims. In analyzing such a fact pattern, a creditor or debtor will have little guidance from Oregon case law, because there is a scarcity of Oregon case law interpreting the current version of ORS 73.0311, amended in 1997.

Conclusion

In the practice of construction contract law, where parties (and clients) may often act and enter into agreements first and seek legal counsel second, a prudent practitioner should always consider and evaluate all three of the above contract theories. The theories should be considered in any case involving a client's resolution of (or attempt to resolve) claims on a construction project, as well as in relation to other creditor/debtor disputes. The distinctions among the three theories of accord and satisfaction, executory accord, and substituted contract can significantly affect a client's procedural and substantive rights at trial.

TEN THINGS EVERY CONTRACTOR SHOULD KNOW ABOUT STAYING OUT OF LEGAL TROUBLE

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Construction contracting is a tough business. Aside from simply doing good work, the industry is highly regulated by very specific and often evolving laws. Small contractors, particularly those who contract with consumers or small businesses, are particularly at risk for disputes and litigation that threaten to delay or even eliminate the right to payment entirely. Even when the project is completed, contractors may remain at risk from construction defect claims for several years. The purpose of this article is to set forth some (but of course not all) potential problems that may lurk on any given project.

1. Beware if Carrying Only One CCB License Endorsement!

Proper licensure with the Oregon Construction Contractor's Board (CCB) is a critical issue that should be confirmed prior to entering into any contract. Contractors are required to hold a valid license and the proper endorsement when bidding "or" contracting for work and "continuously while performing" the work.

Failure to do so may create a complete defense to payment for failing to strictly comply with the licensure statutes. There are countless reported cases construing ORS 701.131 (formerly 701.065) that broadly enforce a complete defense to a contractor's otherwise valid claim to be paid for the entirety of its work. *See e.g. Remington Ranch LLC v. Hooker Creek Companies LLC*, United States Bankruptcy Court Adversary No. 10-3093-elp (2010) (The failure of the contractor to be licensed barred recovery on a $4.4 million construction lien).

License endorsement categories generally fall under "residential" and "commercial" categories, but there are also several sub-categories of each endorsement, generally related to quantity of work performed. Both types of endorsements – either residential or commercial – may work on "small commercial" projects. Given the apparent flexibility of the two basic endorsements and the requirement of having a bond for each, there is an incentive for some contractors to obtain only one endorsement to save the cost of the additional bond. But this is where contractors need to beware!

What constitutes a "residential" or "small commercial" project can be extraordinarily specific and may differ on a project-by-project basis. For example: If a convenience store owner leases a structure, the structure is not "large commercial" until it exceeds 12,000 square feet in area (or 20 feet in height as measured from the "top surface of the lowest flooring to the highest interior overhead finish"). ORS 701.005(17)(b). If the convenience store owner *owns* the structure, then the structure is a large commercial structure if it exceeds *10,000* square feet in area (or the same height restriction as above). *Id.* at (17)(a).

Some may find comfort in the definition of "small commercial" which includes projects of any size where "contract price of all construction contractor work to be performed on the structure as part of a construction project does not total more than $250,000." *Id.* at (17)(c). However, this definition may provide a false sense of security: Are change orders during the project included in the "contract price of all * * * work to be performed"? What if the owner hires multiple general contractors or acts as the general contractor? How is a subcontractor going to know the total contract price of all work?

In short, the only safe way to proceed is to pay the costs necessary to obtain <u>both</u> a residential and commercial endorsement. If a contractor is going to proceed with only one license endorsement under Oregon law, the contractor will need to do its homework to be sure that each new project is not at risk for exceeding its endorsement. Failure to do so may result in non-payment.

2. <u>Let Someone Else Have Responsibility for Design.</u>

Some contractors may unwittingly provide design services by including the designer, engineer, or architect's billings as part of the contractor's scope of services. Some contractors explicitly purport to provide "design services" as part of the work they perform.

Contractors should think carefully before assuming responsibility for design. Some reasons include:

- The contractor may not have liability insurance coverage for injury or property damages arising out of design problems.
- The homeowner may take the position that additional costs due to a poor or inadequate design should be borne by the contractor.
- If the design the contractor provides requires an architect's license (such as a commercial or multi-family building that exceeds 4,000 square feet or 20 feet in height from the top surface of lowest flooring to the highest interior overhead finish of the structure), the contractor may be considered to be providing "architectural services."
- If the contractor is not a licensed architect, the contractor may be fined and barred from asserting a lawsuit in Court under ORS 671.220. Note that a contractor that provides services consisting of the practice of architecture or engineering as part of its contract is required to disclose the name and license number of the licensed architect (or firm) or licensed engineer or land surveyor that will provide the design services. For architects, see ORS 671.030(2)(c) & (g); OAR 806-010-0078(3). For engineers and land surveyors, see ORS 672.060(12); OAR 820-010-0715.
- By including design in its contract, the contractor may be subject to a longer statute

of limitations to its customer (generally six years from the breach of contract) than the design professional is to the contractor (generally two years from date of discovery of the injury or damage). Thus, the contractor may be liable to its customer for a claim that has expired against the architect, engineer or landscape architect. Compare ORS 12.080(3) (six years for breach of contract) and ORS 12.135(3) (two years from discovery against the design professionals).

On the other hand, if the *owner* provides plans and specifications, then the owner generally impliedly warrants that the structure built according to the plans and specifications will be adequate for the owner's purposes. This concept is generally referred to as the Spearin Doctrine arising out of the case *United States v. Spearin*, 248 U.S. 132 (1918). If this doctrine applies, construction defects arising out of a faulty design or additional costs incurred to achieve the owner's objectives are more likely to be risks borne by the owner than the contractor. *See e.g. A.H. Barbour & Son, Inc. v. State Highway Comm.*, 248 Or 247 (1967) (Painting contractor was entitled to recover additional compensation where Owner specifications required rust to be removed from the Yaquina Bay bridge by sandblasting and additional work beyond sandblasting to remove the rust was required).

3. <u>Know Legal Disclosures and Requirements.</u>

There are a number of potentially applicable legal disclosures that must be made to the customer. Below are a few with potential significance to small contractors who deal with consumers. Each of these issues should be checked regularly, because many requirements (particularly state ones) seem to continually change every few years and indeed may change again soon. See e.g. SB 205 (2013 Legislative Session) (bill to authorize the CCB to change certain contract requirements presently mandated by statute).

a. CCB Statutory Form Requirements. In the case of contractors who deal with homeowners, a number of requirements apply, both as to the form of the agreement (see e.g. ORS 701.305) and various notices that must generally be given at the time of contracting. Failure to comply with these requirements may result in fines imposed by the CCB and the loss of lien rights (see e.g. ORS 87.037 & 87.093). The CCB website has a significant amount of information, including sample contract language and charts that outline when certain notices must be given. See http://www.oregon.gov/ccb/Pages/Contractor_Forms.aspx (3/6/2012).

There are several potentially overlooked notice requirements that may apply to contractors who enter into contract directly with homeowners for residential construction. One notice (required in new home construction transactions only) is the "Model List Of Accessibility Features" notice. This notice is intended to provide seniors and disabled persons with options to make their prospective home "more accessible" to a person with disabilities. See ORS 701.525-.530; OAR 812-001-0200(4). A copy of the notice is available on the CCB's website at: http://ccbed.ccb.state.or.us/WebPDF/CCB/Publications/Model%20Features%2012-04-07.pdf

A second notice is the moisture intrusion and water damage information and a home maintenance schedule that builders are required to provide to consumers as a part of a contract for new residential structure or zero-lot-line dwelling under ORS 701.335. A copy of this information and maintenance schedule can be found at: http://www.oregon.gov/ccb/Pages/Contractor_Forms.aspx#Other_Important_Forms (under the Residential Contractor Notices and Forms header).

A third important notice is the "Notice of Compliance with Homebuyer Protection Act" ("HPA"), which generally applies to "owners" who contract for the sale of a new residential home or a home with $50,000 or more in remodel costs that was completed within three months of sale. See ORS 87.007 for specific parameters and requirements of HPA. A copy of the notice and requirements for compliance with the HPA can be found on the CCB's website at:

https://ccbed.ccb.state.or.us/WebPDF/CCB/Publications/HPAform.pdf.

Note that, out of all the methods of compliance with the HPA, other than waiting 90 to 135 days after completion to close on the sale (depending on the circumstances), the most palatable method of complying with the HPA may be to provide the homebuyer with copies of lien waivers from all subcontractors and suppliers who might claim $5,000 or more. See ORS 87.007(2). The option of obtaining the homebuyer signature on a waiver of protections under the HPA is no longer available. Section 1, Chapter 77, Oregon Laws 2010 Special Session.

Failure to comply with the HPA requirements not only opens the "owner-contractor" to possible claims by injured homeowners under ORS 87.007 and Oregon's Unlawful Trade Practices Act under ORS 646.608(1)(zz), it also is a basis for the "suspension of, revocation of, refusal to issue or refusal to renew a license" by the CCB under ORS 701.106(1)(a).

b. Consumer Cancellation Rights. Many contractors are aware a homeowner has a short right to cancel any initial contract for the construction, improvement or repair of a residential structure or zero lot line dwelling. See ORS 701.310 (right to cancel by midnight the business day following the execution of the agreement unless waived or substantial work commences).

A less known requirement that residential "remodel or repair" contractors should know about, however, is the potential application of Oregon's "Home Solicitation Sales Act." This Act provides that if a seller of "goods" or "services" that are "primarily for personal, family or household use" solicits a "written agreement" "at a place other than the place of business of the seller," then the seller may be required to provide a statutory written disclosure of rights. See ORS 83.710(1)(a) (home solicitation sale definition, incorporates definition of goods and services from ORS 83.010).

The definition of "goods" generally includes most construction supplies because the definition includes goods to be "affixed" to real property "whether or not severable." "Services" explicitly includes "repairs, alterations or improvements upon or in connection with real property." Therefore, signing a home remodel contract at a coffee shop, for example, may result in application of this Act.

If the Act applies, a disclosure of the consumer's right to cancel the transaction by providing written notice within three business days must be provided directly above the signature line, among other requirements. ORS 83.730(1). A cancellation form must also be provided in duplicate (ORS 83.730(1)(c), although the homeowner needed not use the form to cancel (ORS 83.720(4)).

If the appropriate right to cancel disclosure is not provided, then the consumer may have a continuing right to rescind the contract after part or full performance. ORS 83.730. Further, the consumer may be able to keep services without paying for them, and unless the seller makes a timely written demand for the return of the goods, the consumer may be able to keep the goods without paying for them. See ORS 83.730(1) and (3).

The Act explicitly does not apply to contracts "for the sale or lease of a house or business property or the construction of a new house or business property." ORS 83.710(2)(c).

c. Warranties – State and Federal Requirements. Most Oregon contractors are aware of the requirement to "offer" a warranty for the construction or sale of a "new" residential structure or zero lot line dwelling to the owner. ORS 701.320. In the case of projects that meet the definition of "large commercial structure" (i.e. not a residential or small commercial structure), commercially endorsed general contractors must provide a two year warranty on building envelope and penetration components against defects in materials and workmanship. ORS 701.340.

Yet many contractors who do provide a warranty on materials may not be aware of additional Federal law requirements that may apply. For contractors who provide what may be considered a "consumer good" – a good that is "normally used for personal, family, or household purposes" – federal warranty law may apply.

This may apply particularly to those contractors who provide significantly more goods than services. *See e.g. Atkinson v. Elk Corp of Texas*, 48 Cal.Rptr.3d 247 (Cal. App. 2006) (roofing material supplied as part of a re-roofing contract retained their status as consumer goods in action against manufacturer); 16 CFR 701.1(d) (2012) (generally, thermal, electrical or mechanical equipment attached to realty and considered fixtures under state law may retain their status as consumer goods); 16 CFR 701.1(e-f) (2012) (materials purchased in connection with the improvement, repair, or modification of a home may be consumer goods, but materials already integrated into realty at time of contract or sold as part of a new construction or substantial improvement may not be). If so, special warranty requirements may apply. *See e.g.* http://www.business.ftc.gov/documents/bus01-businesspersons-guide-federal-warranty-law#intro (3/6/2013).

d. "Sewer Contractors." Every person offering to undertake or undertaking construction of "building sewer piping" must provide specific contract disclosures relating to insurance, bonding and permit information. ORS 701.348(1-2). "Building sewer" means that part of the system of drainage piping that conveys sewage into a septic tank, cesspool or other treatment unit that begins five feet outside the building or structure within which the sewage originates. *Id.* at (4).

4. Regularly Check Insurance Coverage with a Knowledgeable Professional.

All contractors must obtain and maintain commercial general liability insurance as a condition of obtaining a license from the CCB. Obtaining the "right" insurance is an important protection against the risks of doing business as general liability insurance generally serves two functions:

First, liability insurance may pay "covered claims," meaning claims that are based on certain types of personal injury and property damage as defined in the insurance policy. Second, and perhaps more importantly to the contractor paying the insurance premium, if the claim alleged against the contractor may be "covered" by the terms of the contractor's applicable liability insurance policy, then the insurance company is generally obligated to pay for the contractor's legal defense so long as the contractor complies with certain requirements (such as timely reporting of the claim and cooperation).

The problem is that most people (i.e. those who are not agents who sell insurance for a living) find it nearly impossible to comparison shop insurance policies and coverage options. A policy with an expensive premium may not even cover most of the risks the contractor faces because the policy language explicitly excludes those risks from what is a "covered claim."

For example, some common potential exclusions from "covered claims" include: Work performed on multi-family dwellings; Specified products, such as Exterior Insulated Finish Systems (known as EIFS) or other artificial stucco-like products; damage or injury caused by subsidence of soils (think landslides or failure of trench shoring).

Similarly, to protect valuable construction equipment or building materials stolen or damaged on the jobsite, a contractor may need additional types of insurance, such as Inland Marine insurance (for equipment) and Builder's Risk or Course of Construction Insurance (for certain types of damage or loss of the partially constructed project or unincorporated materials and supplies).

Every contractor should not simply renew its insurance when required, but rather take an active role. This includes not only asking its insurance agent what coverage is available, but also informing the agent of any significant

changes in the contractor's business, including specific types of projects, customers, new acquisitions of equipment, etc.

5. Avoid Hidden Costs of Someone Else's Insurance and Bond Requirements.

If the contractor is working under someone else's contract – often a sophisticated owner or an "upstream" contractor – the form should be carefully reviewed, particularly for insurance and bonding requirements. A bid for the work should exclude the cost of any insurance and bonding requirements, as those costs may not be fully known until the contract negotiation stage. In particular, some contracts require insurance that is prohibitively expensive or may not even be commercially available.

If a contract requires the contractor to post a bond (such as a performance and payment bond), the contractor needs to not only qualify for the bond and add the cost of the bond premium into its price, but also consider the lost opportunity of other work that may require a bond if the contractor does not have sufficient creditworthiness to qualify for multiple bonds.

6. Have a Workable Procedure for Changes.

Changes in the scope of work are to be expected. A provision that no work will be performed in the absence of written change order signed by each party may present problems if the contractor does not strictly follow its own contract.

In *Gregory v. Warren*, 51 Or App 547 (1981), the contractor Warren agreed to build a home on land he owned and then convey it to the Gregorys. The agreement contained a requirement that change orders must be in writing. The contractor inconsistently enforced the change order language, obtaining a change order for a $945 change, but not for substantial changes that were valued at $20,000 to $30,000. Despite not getting paid for the $20,000 to $30,000 change order, the judge compelled the contractor to convey title of the home to the Gregorys, stating in particular:

> *" [Y]ou [the contractor] indicated * * * that you just didn't have time to prepare changes or addendums, but yet Exhibit 7 shows you wrote out an addendum for only $945, and yet you want the Court to believe that [the] Gregorys had agreed to pay you 20- to $30,000. I can't accept that."*

While this case may be an extreme example, a contractor should formulate a workable procedure for dealing with changes that inevitably arise. One potential method may be to include a contract provision that reserves the right to refuse to do work without a signed, written change order, but otherwise provides that changes made at the owner's request shall be paid for on a time and materials basis. The hourly rates and mark up on materials or subcontractors should be set out in the agreement. The agreement should also provide a basis for time extensions based on changes, particularly where timeliness of performance will be an issue. Regular communication and documentation is a key to avoiding problems.

7. Claims for Changes Performed under Someone Else's Contract.

When working under someone else's form of agreement, the contract terms should be carefully reviewed for any notice and documentation requirements, as well as dispute resolution procedures. The contractor's failure to comply may waive a claim.

Whenever the owner or upstream contractor imposes various requirements for notice, timing and documentation of claims, a contractor should impose those terms on its own subcontractors. Otherwise, the contractor may get stuck paying a subcontractor for extra work or changes that the contractor is unable to collect from the owner or upstream contractor. Such terms can easily be incorporated by reference by what is called a "flow down clause" so long as the language is clear about what terms are incorporated by reference.

Similarly, if the work is on a publicly-owned project, the change order process should also involve obtaining confirmation that request for additional work comes from someone who has the budgetary authority of the public body and has followed the appropriate procedures to allocate additional funds to pay for the additional work. *See e.g. Wegroup PC v. State*, 131 Or App 346, 355 (1994) ("Persons who enter into public contracts are deemed to know the laws governing such contracts, and they assume the risk of nonpayment if they perform without insisting on strict compliance with those laws.").

8. Collecting Payments Owed to the Contractor.

Consideration should be given to the alternatives a contractor has to obtain payment from its customer. Some contractors who have had the unpleasant experience of using an attorney for collections subsequently insert an attorney fees clause in their agreement for future matters.

Given the potential reciprocity of these clauses, much more consideration is needed before including an attorney fee clause, such as whether the contractor is encouraging lawsuits for construction defects and the various alternatives. For example, properly preserving construction lien rights provides a basis for recovery of attorney fees. Claims under $10,000 may be recovered either in small claims court without attorneys (ORS 46.405) or by an attorney under ORS 20.082 upon satisfying certain conditions, which generally includes providing a pre-litigation demand.

9. Generally Shifting Risks From Contractor to Someone Else.

Oregon law is replete with examples showing that properly drafted contract language can help shift the risks of defective construction and accidents from the contractor to someone else (typically the owner or customer). Examples include a waiver or limitation of claims, disclaimer of warranties, or shortening of the time in which a claim may be made against the contractor.

Except for some limited statutory examples (*see e.g.* ORS 701.315 prohibiting the limitation of the right to file a Construction Contractors Board complaint, other than to require mediation and/or arbitration), many rights and remedies can be waived or minimized with properly drafted contract language. Such contract language may not be enforceable in every circumstance; however, the mere appearance of such clauses may have a "chilling effect" on potential claims or make those claims easier to resolve if lawyers get involved.

10. The Past Unresolved Conduct: A Problem that Reaches Beyond the Protections Afforded by Corporations and LLCs.

Attorneys representing any contracting business should be aware of ORS 701.102 and the CCB's implementation of ORS 701.068 before closing down the construction business or deciding to ignore a claim against the "defunct" business. The result may be very expensive for any new contracting business that shares an owner, officer or responsible managing individuals ("RMI") in common with the "defunct" business. In many circumstances, this can be true even if the owner, officer or RMI files personal bankruptcy.

The CCB has the ability to revoke, suspend or refuse to issue a license to a contracting business that owes a "construction debt" or "has had" a contractor license revoked, suspended or denied (such as in another state). ORS 701.102(2)(a). A "construction debt" includes debts arising out of a final award or order of the CCB, or a judgment award or civil penalty arising out of "construction activities" within the United States, or a failure to comply with Oregon's Worker Compensation laws. ORS 701.005(4).

What is surprising to many lawyers and contractors, perhaps because the concept partially defeats the general liability protections of a corporation or LLC, is that the "construction debt" against the "defunct" business may prevent an owner, officer or RMI of the defunct business

from obtaining a contractor's license for a new business until the "construction debt" is resolved.

In other words, an owner, officer or RMI of a defunct company may not be able to be anything other than an employee of the new contracting business (not an owner, officer or RMI) unless the "construction debt" against the defunct business is paid or otherwise resolved. ORS 701.102(2)(c).

This may be the case even if the owner, officer or RMI files and receives a bankruptcy discharge if the owner, officer or RMI was not personally liable for the construction debt. *See e.g. In re Ray*, 355 B.R. 253 (Bankr. Or. 2006) (Federal statute preempted ORS 701.102(2) where officer of defunct contracting company received a bankruptcy discharge of a debt owed by the defunct company that the officer also personally guaranteed).

Finally, if the "construction debt" arises out of a CCB order or award where a surety paid some, but not all of the order or award against the defunct contracting business, there may be additional concerns. A "new" company formed by an owner, officer or RMI in common with the defunct contractor may find the CCB taking the position that the new business will only be licensed if it obtains a bond that is up to five times the unpaid balance of the CCB order or award against the "defunct" contracting business. See ORS 701.068(4-5); OAR 812-003-0175. The CCB may seek to implement this statute even when the common person has received a bankruptcy discharge.

Conclusion. There are many other risks that exist for contractors, and these risks are continually changing as new case law is reported and statutes and regulations are re-written. Vigilance is critical.

NOTE: Prior newsletters are available (in a searchable format) at the Section's website: *www.osbarconstruction.com*.