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ORS 701.640 MAY NOT VOID FORUM- SELECTION AND CHOICE-OF-LAW

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Do not underestimate forum-selection and choice-of-law clauses when coupled with an arbitration provision; ORS 701.640 may not apply and your client may find itself arbitrating claims far from the project under unfamiliar and unfriendly law.

A forum selection clause is one that stipulates the jurisdiction in which to bring the claim. This could be the state of the project or the home state of one of the parties, typically the upstream party.

Related, a choice-of-law clause specifies which state’s law will govern the dispute. Again, this could be the state of the project or the home state of one of the parties, typically the upstream party. These clauses are very common in construction contracts and receive little attention; for construction projects in Oregon, and many other states,¹ it is against public policy to contractually

¹ See Conn. Gen. Stat. § 42-158m; Fla. Stat. Ann.

stipulate any forum other than the home state of the project or contractually apply any law other than the law of the home state of the project.

ORS 701.640 states as follows:



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1) A construction contract may not include any provision, covenant or clause that:

(a) Makes the construction contract subject to the laws of another state or that requires any litigation, arbitration or other dispute resolution proceeding arising from the construction contract to be conducted in another state.

ch 47.025; 815 Ill. Comp. Stat. Ann. 665/10; Ind. Code § 32-28-3-17; Kan. Stat. Ann. § 16-121(d); La. Rev. Stat. Ann. § 92779(B)(1); Minn. Stat. § 337.10(1); Mont. Code Ann. § 28-2-2116(1); Neb. Rev. Stat. § 45-1209; Nev. Rev. Stat. Ann. § 108.2453(2); N.M. Stat. Ann. § 57-28A-1; N.Y. Gen. Bus. Law § 757; N.C. Gen. Stat. Ann. § 22B-2; Ohio Rev. Code Ann. § 4113.62(D); Okla. Stat. Ann. tit. 15, § 15-821; Pa. Stat. Ann. tit. 73 § 514; R.I. Gen. Laws § 6-34.1-1(a); S.C. Code Ann. § 15-7-120.A; Tenn. Code Ann § 66-11-208(a); Utah Code Ann. § 13-8-3.2; Va. Code Ann. § 8.01-262.1; Wis. Stat. Ann. § 779.135(2).

Thus, the Oregon construction lawyer reviewing a subcontract for an Oregon project could shrug his or her shoulders when coming across a forum-selection or choice-of-law clause; under ORS 701.640 such a clause would be unenforceable, right? Not so fast.

Most construction contracts also contain an arbitration provision. There is mounting authority holding the Federal Arbitration Act (“FAA”) preempts otherwise applicable state home-court statutes like ORS 701.640 where the arbitration provision stipulates forum and governing law. Consequently, ORS 701.640 may not apply to void arbitration in a foreign jurisdiction under foreign law.

Section 2 of the FAA mandates arbitration provisions in contracts “shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.”² This “is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding *any state substantive or procedural policies to the contrary.*”³ While litigants can argue the contract is not subject to the FAA, given the substantial nexus a construction project has to interstate commerce, that argument is likely to fail especially where one of the parties is domiciled out of state (hence the forum-selection clause in the first place).⁴ And, there is a mounting litany of lower court decisions holding the FAA preempts a state’s construction-specific home-court statute as applied to an enforceable arbitration provision.⁵ In short, do not rely on

² 9 U.S.C. § 2.

³ *Moses H. Cone Mem'l Hosp. v. Mercury Construction Corp.*, 460 US 1, 24 (1983) (emphasis added).

⁴ See *Allied-Bruce Terminix Cos. v. Dobson*, 513 US 265, 278 (1995) (adopting a “commerce in fact” analysis to whether the subject matter of the contract involves interstate commerce).

⁵ See, e.g., *R.A. Bright Construction, Inc. v. Weis Builders, Inc.*, 930 NE2d 565 (Ill. App. Ct. 3d Dist. 2010) (holding Section 2 of the FAA

ORS 701.640 to void a forum-selection or choice-of-law clause in a construction contract subject to arbitration.

The importance of these types of clauses as a dispute resolution lever should not be underestimated. Putting aside the perceived “home field advantage,” a forum-selection clause can require a party to litigate far from its place of business and far from the location of the project while simultaneously allowing the other party to litigate close to home. If the stipulated location is a great distance from the project it may be difficult (and certainly more expensive) to marshal witnesses and evidence to the distant forum. Further, the travelling party will need to hire unfamiliar local counsel, but the party litigating in its “home field” will be able to use its own familiar counsel. While *forum non conveniens* grounds may persuade the arbitrator to move the arbitration to the project’s home state, do not rely on ORS 701.640 to do so.

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preempts state law that restricts venue for arbitration to the project's home state) (citing *OPE Int'l LP v. Chet Morrison Contractors*, 258 F3d 443 (5th Cir. Tex. 2001) (holding same with regard to similar Louisiana statute), *KKW Enterprises, Inc. v. Gloria Jean's Gourmet Coffees Franchising Corp.*, 184 F.3d 42 (1st Cir.1999) (holding same with regard to similar Rhode Island statute involving franchise agreements); *Bradley v. Harris Research, Inc.*, 275 F3d 884 (9th Cir.2001) (same)); *M.A. Mortenson/Meyne Co. v. Edward E. Gillen Co.*, 2003 WL 23024511, * 4 (D. Minn. 2003)(acknowledging preemption: "state laws, which attempt to 'rewrite the parties' agreements and compel arbitration of their dispute in a forum which is not one of those enumerated in an arbitration agreement's forum-selection clause,' are presumably preempted by the FAA) (citing cases); *Gem Mechanical Services, Inc. v. DV II, LLC*, 2012 WL 4094476 (D.R.I. 2012) (holding FAA preempts statute voiding contract clause requiring arbitration in another state).

WHAT IS THE “OCCURRENCE” IN A CGL POLICY

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caused by defective work? Is it the accident of unintended property damage?

The significance of this inquiry cannot be overstated. Not only is the “occurrence” necessary to trigger the insuring agreement, but CGL policy limits customarily apply per each “occurrence.” Moreover, deductibles and self-insured retentions often apply per each “occurrence.” Endorsements sometimes attempt to limit coverage to a single policy period by addressing continuing and progressive property damage “arising from the same ‘occurrence.’” Excess insurers sometimes argue multiple occurrences to attempt exhaustion of the primary policy’s aggregate limit before the excess policy is triggered. In these scenarios and more, how the “occurrence” is articulated can be key.

The standard CGL policy defines the term “occurrence” as “an accident, including continuous or repeated exposure to substantially the same general harmful conditions.” If you think this definition is as clear as mud, you are not alone. Oregon courts find this definition inherently ambiguous, as well. “There are probably not many words which have caused

The standard Commercial General Liability (“CGL”) policy covers, among other things, damages because of property damage caused by an “occurrence.” So, what then is the “occurrence?” Is it the defective work? Is it the building’s exposure to conditions

courts as much trouble as ‘accident’ and ‘accidental.’” *Botts v. Hartford Acc. & Indem. Co.*, 284 Or 95 (1978). “The problem arises from an erroneous impression that there is one all-encompassing definition of ‘accident’ or ‘accidental’ * * *.” *Id.* at 102; accord *Chale v. Allstate Life Ins. Co.*, 353 F3d 742, 746 (9th Cir 2003) (“Notably, the Oregon Supreme Court has acknowledged the futility of such an undertaking,” *i.e.*, trying to formulate such a “universally accepted definition”); *St. Paul Fire & Marine Ins. Co., Inc. v. McCormick & Baxter Creosoting Co., Inc.* v. *McCormick & Baxter Creosoting Co.*, 324 Or 184, 204 (1996) (finding the dictionary definition “broad enough to cover the proposed definitions of both sides”). Ambiguous policy language is uniformly construed in favor of coverage for the insured under *Hoffman Constr. Co. v. Fred S. James & Co.*, 313 Or 464, 469-72 (1992).

In appropriate cases, Oregon courts have focused on the unintended *result*, finding that the “occurrence” is the accidental injury or damage. *See, e.g., N. Clackamas School Dist. No. 12 v. Oregon School Brds. Assoc. Prop. & Cas. Trust*, 164 Or App 339, 345 (1999) (“[W]e and the Supreme Court have recently reaffirmed that, in the insurance context, the meaning and determination of ‘accident’ focuses not on conduct, but on result.”).

Alternatively, in the context of ongoing exposures causing damage over a period of time, courts applying Oregon law have held that the *exposure* is the “occurrence.” *See California Ins. Co. v. Stimson Lumber Co.*, No. Civ. 01-514-HA, 2005 WL 627624, at *7 (D Or March 17, 2005) (holding that the repeated exposure to building materials constituted one “occurrence”); *see also Interstate Fire & Cas. Co. v. Archdiocese of Portland in Oregon*, 35 F3d 1325, 1329-30 (9th Cir 1994) (holding that the ongoing exposure to the subject priest constituted the “occurrence”).

Outside of the statutory auto insurance context, Oregon courts have not focused on the cause of

the injury or damage, but what that tells us is that focusing on the cause does not favor the insured in most cases. If it did, insureds would be well-positioned under *Hoffman* to prevail on that interpretation, as well.

Ultimately, the inherent ambiguity of the “occurrence” definition makes it susceptible to varying applications, depending on the facts of a particular case and which result favors coverage for the insured.

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OREGON LIEN LAW – TRAPS FOR THE UNWARY

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Every construction practitioner is (or should) at least be generally aware of the technical, statutory quagmire that is Oregon construction lien law, ORS Chapter 87.001, *et. seq.* Known to most are the requirements and deadlines for lien notices, the recording of a lien, and the foreclosing of a lien that must be followed in order to preserve a claimant’s right to perfect and enforce a construction lien. However, mired in the bowels of the Oregon lien law statutes are several less obvious traps for the unwary practitioner.



Bill Fig

The first such trap may be sprung early on in the life of a project, well before counsel is involved, and it has serious consequences to material suppliers. Generally speaking, on new construction, if a material supplier sends out a proper and timely pre-lien notice to the appropriate

parties, including any mortgagee, the material supplier’s lien will have priority over the mortgagee’s existing encumbrance as to the improvement and the “land that may be required for the convenient use and occupation of the improvement constructed on the site.” ORS 87.015(1). This is commonly referred to as “super priority.”

However, for the savvy mortgagee, there is another card to play - ORS 87.025(4). This statute provides:

A mortgagee who has received notice of delivery of materials or supplies in accordance with the provisions of subsection (3) of this section, may demand a list of those materials or supplies including a statement of the amount due by reason of delivery thereof. The list of materials or supplies shall be delivered to the mortgagee within 15 days, not including Saturdays, Sundays and other holidays as defined in ORS 187.010, of receipt of demand, as evidenced by a receipt or a receipt of delivery of a registered or certified letter containing the demand. Failure to furnish the list or the amount due by the person giving notice of delivery of the materials or supplies *shall constitute a waiver of the preference provided in subsections (1) and (2) of this section.* (Emphasis added).

With construction liens, the importance of priority over existing encumbrances cannot be overstated. A lien that has super priority, *i.e.* priority over a mortgagee’s (*i.e.* banks/lenders) Deed of Trust, provides serious leverage to the lien claimant, which generally results in the mortgagee paying the lien claimant. In most cases, the mortgagee, after performing some early due diligence, will

pay off a superior lien to avoid the lien claimant foreclosing its lien (and being awarded its attorney fees for doing so) and extinguishing the mortgagee's inferior interest. A mortgagee's early payment to a claimant with a superior lien claim is simply good business because it minimizes the mortgagee's loss and preserves its encumbrance. A lien claimant's failure to comply with ORS 87.025(4) results in a loss of the lien's super priority and, consequently, the lien is inferior to the mortgagee's pre-existing interest. As a result, the mortgagee's secured interest in the property is no longer threatened by the lien; the lien claimant loses most, if not all, of its leverage vis a vis the mortgagee; and the mortgagee generally will not satisfy the lien. Thus, it is important for counsel who represent parties that supply materials to a construction project to ensure their clients are aware of, and comply with, ORS 87.025(4). Likewise, counsel to mortgagees should advise their clients of the potential benefit of making such a request.

A second trap lies in the language of ORS 87.057. Subsection (2) of that statute provides:

Where a notice of intent to foreclose a lien has been given as provided by subsection (1) of this section, the sender of the notice upon demand of the owner shall furnish to the owner *within five days* after the demand a list of the materials and supplies with the charge therefor, or a statement of a contractual basis for the owner's obligation, for which a claim will be made in the suit to foreclose. (Emphasis added).

The kicker is in ORS 87.057(3), which requires a "plaintiff or cross-complainant seeking to foreclose a lien in a suit to foreclose shall plead and prove compliance with subsections (1) and (2) of this section. *No costs, disbursements or attorney fees otherwise allowable as provided by*

ORS 87.060 shall be allowed to any party failing to comply with the provisions of this section." (Emphasis added). While this statute does not affect the priority of a lien, it does affect a very important right of a construction lien claimant – the right to recover attorney fees incurred in foreclosing the lien. After priority, the threat of attorney fees is the lien claimant's second biggest leverage point in getting its lien paid. This is especially true regarding a lien for a smaller amount where the owner/mortgagee knows it is not cost effective for the claimant to foreclose the lien absent the ability to recovery attorney fees. At the point a notice of intent to foreclose is sent, a claimant may be so frustrated with the project that it ignores or "round files" correspondence from other parties. However, it is important to counsel a lien claimant that it needs to continue to carefully review any project-related correspondence and timely comply with an ORS 87.057 request.

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AVOIDING COVERAGE CONFUSION IN DESIGN PROFESSIONAL CONTRACT TERMS

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to perform work, but may be less familiar with hiring architects and engineers to provide professional services. These clients often base their contracts with design firms off of their latest

Often the design firm's professional liability insurance policy is its greatest, maybe sole, asset to pay to clients with valid claims. In turn, a lot of clients, from private landowners through public entities,

are familiar with hiring construction contractors

construction contract. When they do so, however, they use terms we see all the time that can give the designer's insurance company some arguments about distancing themselves from coverage. This is not in anyone's best interest.

While there are many different types of contract clauses, one central concept is that the professional liability policy applies to the *professional service* – the work of the discipline itself. This means that the design professional cannot name other project participants who are not practicing the discipline of architecture, or engineering, or whatever it may be, as “additional insureds” on their professional liability policies. Coming from the construction side, clients are used to being named “additional insureds,” and keeping a chain of “additional insured” endorsements going down through the contracting ranks. While design professionals can still name clients and others as “additional insureds” on their own CGL and other policies, contract language which purports to give access to the professional liability policy other than through practice of the covered discipline creates confusion.

One example provision purports to give the property owner unilateral control over any defense and resolution of third-party claims brought against both the property owner and design professional jointly. This creates confusion for a few different reasons. First, it creates confusion regarding the professional liability insurer's control over the defense and resolution of an insured claim. Second, it creates confusion regarding whether the property owner is trying to insert itself into the policy directly, giving the insurance company a platform to argue the design professional has contractually agreed to something that has altered the insurer's obligations, and therefore, muddying the waters of defense and coverage for what otherwise could have been a straightforward claim.

Another example provision purports to make the prime design professional responsible for the acts

of its subconsultants “as if the professional services had been performed by the prime itself.” This created concerns for both the prime's and the subconsultant's insurance security. As to the prime, it raised the question whether it amounted to a contractual agreement extending the prime's liability beyond its standard of care. As to the subconsultant, it raised a question whether there was other primary insurance coverage through the prime that moved the subconsultant's insurance coverage into the back seat, potentially leaving the subconsultant in a gap with both insurers making hay of the overly ambitious provision.

This brings up another central concept: that the design professional policies to insure damages for deviations from the “standard of care.” As the rules governing architects describes it, “In practicing architecture, an Architect shall act with reasonable care and competence, and shall apply the technical knowledge and skill which is applied by architects of good standing, practicing in the same locality.” OAR 806-020-0030(1).

It is an old red flag for contract negotiators to see “warranties” for design professional services, like you would see in the construction context. But we continue to see property owners make efforts to land everywhere else around this target in efforts to bolster the design professional's obligations under a contract. These include a “warranty” that the design services will be provided within the standard of care; a “warranty” that if the project is constructed in accord with the design documents it will perform as intended; a “warranty” that the design will comply with all laws (however broad that is); a “warranty” that the design professional has read and understands the performance requirements of the contract and will design to meet these requirements, etc.

The property owner's intent is no mystery. “Warranty” is a strong word to pump up the design professional's obligations so there are more promises to point to if there are problems later. Inadvertently, however, property owners are also

providing more promises *for the design professional's insurance company* to point to, valid or not, to create uncertainty about insurance coverage for a claim which might otherwise have been a simple fit into the design professionals' insurance.

A lot of times in the negotiation of these types of provisions, counsel may assume a zero-sum posture, that the design professional is pushing back on these broader provisions in order to reduce its liability. Often, however, that is not the case. Sophisticated counsel can coordinate to make sure the design professional's greatest asset, its professional liability policy, can do its job and help clients in need, without undue confusion.

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