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SUIT-LIMITATION CLAUSES HELD AMBIGUOUS WHEN INSURANCE CARRIERS DEVIATED FROM THE STATUTORY LANGUAGE

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Stacey

The U.S. District Court for the District of Oregon issued three significant decisions related to an insured's ability to bring a first-party suit against a property insurance carrier. The decisions have equipped insureds with additional arguments to extend the time to bring suit and will be of special interest to any construction lawyer who deals with cases involving hidden property damage.

The holdings interpret a contract clause commonly referred to as a "suit-limitation clause" which, in the context of an insurance policy, contractually limits the time-period when an insured can bring suit against the insurance carrier. Oregon courts have routinely enforced and interpreted these suit-limitation clauses in favor of the insurance carriers. The recent decisions by the Oregon federal court address hidden property damage and hold that the language of certain suit-limitation clauses were ambiguous when they deviated from the statutory language of ORS 742.240.

I. Statutory Suit-Limitation Clause for Fire Policies

To understand the significance of these federal decisions, a brief overview of the statutory provisions related to a suit-limitation clause is

warranted. In Oregon, fire insurance policies, like other types of insurance, are regulated by statute. *See* ORS 731.004, *et seq.* (the "Insurance Code"). The Insurance Code contains a section that specifically addresses fire insurance, and it provides that a fire insurance policy must have certain mandatory provisions.[1] *See* ORS 742.200, *et seq*. One of those mandatory clauses is provided in ORS 742.240[2], which provides:

> No suit or action on this policy for the recovery of any claim shall be sustainable in any court of law or equity unless all the requirements of this policy shall have been complied with, and unless commenced within 24 months next *after inception of the loss*.

(Emphasis added.)

Although some cases have referred to this suit-limitation clause as "statute of limitations," the Oregon Supreme Court clarified that ORS 742.240 is not a statute of limitations but, rather, a provision that "requires a particular contractual arrangement between the parties to insurance policies." *Ben Rybke Co. v. Royal Globe Ins. Co*., 293 Or 513, 518 (1982). This means that ORS 742.240 prevents an insurance carrier from imposing a shorter limitation period, but does not provide a maximum time in which a suit may be filed. *Id.* Of course, the reality is that almost all first-property insurance policies contain a suit-limitation clause that acts to reduce Oregon's six-year statute of limitations for a breach-of-contract action to only two years. *See* ORS 12.080 (contract actions). Because of this shortened time period, it is crucial for the insured to understand when the clock begins to run.

A. Interpretation of the Phrase "Inception of the Loss."

ORS 742.240 provides that an insured must bring suit against its fire insurance carrier within 24 months after "inception of the loss." However, does the "inception of loss" mean the date the loss occurred or accrual of the insurance carrier's liability?

In 1962, the Oregon Supreme Court held that the term "inception of the loss" meant the "beginning" of the casualty or event insured against. *Bell v. Quaker City Fire & Marine Ins. Co., Philadelphia*, 230 Or 615, 625 (1962). In *Bell*, a fire damaged an insured's property which resulted in a suit being filed against the insurance carrier. *Id.* at 617. The question before the court was whether the suit was timely. The fire policy contained a suit-limitation clause that mirrored ORS 744.100 (a former version ORS 742.240) that required commencement of a suit within "12 months after the inception of the loss." *Id.* The court reviewed whether "inception of the loss" meant the occurrence of the fire, or whether it was when the loss was ascertained and payable by the insurance carrier. Central to the decision was the history of the phrase, which was changed in 1945 from "after the fire shall have occurred" to "inception of the loss." *Id.* at 618 (citing to in *Margulies v. Quaker City Fire & Marine Ins. Co*., 276 App Div 695, 97 NYS2d 100 (1950). Based on the reasoning that this change was similar to a New York statute, and the plain meaning of "inception," the court reasoned that "inception" meant the beginning of the "occurrence of the casualty or event insured against" or, in this case, the date of the fire. *Id.*

[1] Most courts now refer to "fire insurance" and "property insurance" interchangeably. *See, e.g., Herman v. Valley Ins. Co.*, 145 Or App 124, 126 (1996) (applying provisions to a burglary). The Insurance Code defines "property insurance" but does not define "fire insurance." *See* ORS 731.182 (defining "property insurance"). Although beyond the scope of this article, based on the legislative history, an insured could make the argument that Chapter ORS 742 should be narrowly interpreted to only homeowner "fire insurance," as opposed to broadly construed to cover all types of property insurance.

[2] ORS 742.240 was originally numbered ORS 743.660, and included a limitation period of one year.

B. Inception of Loss and the Discovery Rule.

The *Bell* court dealt with a readily apparent event—a fire. It did not address when the time period would begin to run in the event of hidden damage or late discovery. In other words, does ORS 742.240 incorporate a "discovery rule" that extends the time to bring suit?

Unfortunately, for insureds, thirty years later, the Oregon Supreme Court held that Oregon law does not apply a "discovery rule" to this statutorily required insurance provision. *Moore v. Mut. of Enumclaw Ins. Co*., 317 Or 235, 250 (1993). In *Moore*, the insured rented a house to tenants from July 1989 to October 1990. *Id.* at 238. On October 15, 1990, the tenant confessed to the police to using the house for cooking methamphetamine. *Id.* at 239. Plaintiff submitted a claim to its carrier for property damage a week later, and the insurance carrier issued payment to the insured in December 1990. The insured objected to the amount of payment and sued the insurance carrier in February 2020, four months after the discovery of the damage. *Id.* After reviewing *Bell*, the court held that the clause "inception of the loss" was not ambiguous, and there was no exception for the discovery of the loss. Thus, the insured's suit was untimely as it was not brought within 12 months[3] of when the "cooking" occurred.

Based on this strict interpretation, insureds were left with little recourse in the event of hidden or latent property damage.

II. New Line of Oregon Federal Cases

A new line of Oregon federal cases have provided insureds with some relief from this strict interpretation. Although these cases do not reject the ruling in *Bell* and *Moore,* they do interpret policies that include a suit-limitation clause without the "inception of the loss" language.

As stated above, both policies in question in the *Bell* and *Moore* decisions contained a suit-limitation clause that mirrored the language of ORS 742.240, and included the "inception of the loss" language. Many insurance policies do not contain this language because the insurance carrier uses ISO[4] form policies, or has drafted its own suit-limitation provision.

The following line of Oregon federal cases address suit-limitation clauses that do not include the "inception of the loss" language, and highlight the extreme importance in reviewing the policy for the exact language.

A. *Housing Northwest Incorporated v. American Insurance Company*, 3:19-CV-00253-SB, 2019 WL 7040922 (D Or Dec 20, 2019).

In *Housing Northwest Incorporated v. American Insurance Company*, 3:19 CV 00253 SB, 2019 WL 7040922 (D Or Dec 20, 2019), Magistrate Judge Beckerman held that a suit-limitation clause was ambiguous, and construed it against the insurance carrier. In this case, the insured provided college housing in Portland, Oregon. In 2017, the insured retained the services of a building envelope expert who reported that the insured's property was sustaining "hidden property damage from water intrusion," and that such damage likely happened from 1997 until it was discovered in 2017. *Id.* at *1. The insured tendered the claim to its insurance carriers, and

[3] ORS 742.240 was amended in 1991 to increase this limitation period from one year to two years. Oregon Laws 1991, chapter 437, § 1.

[4] "ISO" refers to the Insurance Services Office, which was created in 1971. Since 1971, ISO has served as an advisory organization to the insurance industry and, in that role, has published many standard insurance forms. Many of these forms are considered the industry standard, and do not include the "inception of the loss" language. *See*, *e.g.,* ISO forms: HO 00 05 10 00 (homeowner); CP 00 90 07 88 (commercial property); and FP 00 10 09 94 (farm policy).

both carriers denied, citing the suit-limitation clause contained in the policies. *Id.* The suit-limitation clause provided that "[t]he action be brought within 2 years after the date on which *the direct physical loss or damage occurred*." *Id.* (Emphasis added).

The insured argued that the suit was timely because it was filed within two years of the date of the discovery of the physical loss or damage. The insurance carriers, relying on *Moore* and ORS 742.240, argued that no discovery rule applied. The court noted that the suit-limitation clause at issue did not include the "inception of the loss" language, which, instead, had been replaced with "direct physical loss or damage occurred." The court held that the term "occurred" was ambiguous, and it construed the term against the insurance carrier.

Not only did the court construe the provision in favor of the insured and hold the suit was timely, it also warned insurance carriers as follows:

> First, any insurance company selling property insurance in Oregon should be aware that progressive water damage is a common occurrence, and should be motivated to draft clear policy language to govern coverage of such damage. Second, insurance companies have been litigating this same policy language in Oregon for over one hundred years, and Defendants were on notice regarding the ambiguity of the term 'occurred' in this context."

Id. at *4.

B. *Great American Alliance Insurance Co. v. SIR Columbia Knoll Associates Limited Partnership*, No. 3:18-CV-00908-HZ, 2020 WL 5351035 (D Or Sept 4, 2020).

In September 2020, Chief Judge Hernandez examined the same suit-limitation language as in *Housing Northwest* in the context of long-term hidden water damage of some buildings. *Great American Alliance Insurance Co. v. SIR Columbia Knoll Associates Limited Partnership*, No. 3:18 CV 00908 HZ, 2020 WL 5351035 (D Or Sept 4, 2020).

In this case, the court dealt with the exact same suit-limitation language as in *Housing Northwest*—that legal action must be "brought within 2 years after the date on which *the direct physical loss or damage occurred*." *Id.* at *12 (emphasis added). In *Great American*, the insured argued that its suit was timely, as it had been brought within two years of the date of the discovery of the damage, while the insurance carriers argued that no discovery rule applied. The court adopted the reasoning in *Housing Northwest*, and held that the discovery rule applied, because the term "occurred" could also mean "to present itself," "to appear," or "to exist." Further, ORS 742.240 was not applicable because the policy's suit-limitation clause deviated from the statutory language of ORS 742.240.

C. *Silver Ridge Homeowners' Ass'n, Inc. v. State Farm Fire & Cas. Co.*, No. 3:19-CV-01218-YY, 2020 WL 5893317 (D Or Oct 5, 2020).

Lastly, on October 5, 2020, Magistrate You expanded on the rulings of both *Housing Northwest* and *Greater American. Silver Ridge Homeowners' Ass'n, Inc. v. State Farm Fire & Cas. Co.*, No. 3:19-CV-01218-YY, 2020 WL 5893317, *4 (D Or Oct 5, 2020).

In *Silver Ridge,* plaintiff owns a townhome development in Portland, Oregon. The defendant, State Farm Fire and Casualty Company, insured

the townhomes from 1993 to 2009. *Id.* at *1. In February 2018, plaintiff retained a building consultant who discovered systemic property damage. *Id.* The expert opined that the hidden damage commenced in 1993 and continued each year, until it was discovered in 2018. *Id.* Plaintiff tendered the claim for property damage to State Farm, State Farm denied, and plaintiff filed suit. State Farm brought a summary judgment motion asking the court to dismiss plaintiff's claims as barred by the policy's suit-limitation provision. Like *Housing Northwest* and *Greater American,* the suit-limitation clause did not follow the statutory language of ORS 742.240 but, rather, stated that the action must be "brought within two years after the accidental direct physical loss occurred."

For the same reasons as set forth in *Housing Northwest* and *Greater American*, the court held that the suit-limitation clause was ambiguous and construed it against State Farm.

However, of significance, is that the court also addressed whether Oregon law requires the court to incorporate the language of ORS 742.240 if the policy was not drafted to include the statute's exact language. Thus, State Farm argued that it still be construed consistently with ORS 742.240 and not allow a discovery rule, even though its suit-limitation clause failed to include the "inception of the loss" language. The court disagreed, and reiterated that ORS 742.240 is a contractual limitation, not a maximum time in which to file a lawsuit. *Id.* (Citing to *Ben Rybke***,** 293 Or at 518). Therefore, an insurance carrier can deviate from the statutory language of ORS 74.240, and provide a broader time limit.

The takeaway from these three recent decisions is that the exact language of the suit-limitation clause is crucial, and it is likely to be interpreted broadly if it deviates from the statutory language.

III. Final Comments

For many of us construction lawyers, insurance coverage for hidden property is a common issue. With the new line of Oregon federal cases, it is extremely important to review the exact language of the suit-limitation clause, keeping in mind that most property insurance policies use standard form language that do not include "the inception of the loss" language. Although, insurance carriers may heed the warning of the courts, and change their forms in the near future, these new decisions provide some ammunition moving forward. Thus, if the suit-limitation clause deviates from the statutory language of ORS 742.240, such language may be considered ambiguous and favorable to the insured.

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Beware of the Owner's Statutory Right to Cancel Certain Residential Repair and Remodel Contracts

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Residential construction contractors typically deal with consumers as their clients. As a result, residential contractors may be subject to the myriad of laws enacted to protect consumers. Some of the consumer protection laws are included in the contractor related statutes (in Chapter 701 – regarding contractors; and in Chapter 87 – regarding construction liens). Other consumer protection laws are found

Laurie

elsewhere. A recent trial court decision has brought focus on the intersection between residential repair and remodel contractors and the Oregon Home Solicitation Sales Act (ORS 83.710, *et seq*) ("HSSA").

The HSSA applies to goods or services that are purchased primarily for personal, family, or household use. It specifically includes "repairs, alterations or improvements upon or in connection with real property." ORS 83.010(12)(hereinafter "residential work"). Thus, work performed by residential repair and remodeling contractors is within the general purview of this act. The HSSA imposes certain requirements for "home solicitation sales" of such residential repair and remodel work. The law confirms that a contract for construction of a new house is not a home solicitation sale. ORS 83.710(2)(c).

The HSSA provides that a contract for residential repair or remodel work is a home solicitation sale if: (1) the seller (i.e., the contractor) solicits the sale, even if invited by the buyer (i.e., owner); and (2) the construction contract is signed at a place other than the contractor's permanent place of business. ORS 83.710(1)(a). The statute confirms that the owner's home or a neutral location does not constitute the contractor's place of business. It is not uncommon for a residential contractor to meet with its client at the owner's house or at a local coffee shop or restaurant to sign contract documents. Thus, it is likely that many residential repair or remodel contracts are considered "home solicitation sales" and, therefore, subject to the HSSA's provisions regulating these contracts.

While there are some exceptions to the HSSA's requirements that are not relevant to this discussion, the HSSA requires that home solicitation sales include a contract in writing signed by the client owner, and requires that the contractor provide the owner with a fully executed copy of the contract when the owner signs it. Under ORS 83.730, the HSSA also requires certain other details to be included in the construction contract. Significantly, one of the requirements is that the contract include a notice of the "buyer's" (owner's) right to cancel the contract within three business days after the date the owner signs the contract. The statute also provides two specific forms of notice which must be included in the contract. ORS 83.730(1)(b) and 83.730(2).

If the notice is not provided when required, the owner client may have the unfettered right to terminate the construction contract at any time, notwithstanding any inconsistent termination provision in the contract. If that happens, the owner can avoid paying the contractor anything under the contract, even after work has been performed. ORS 83.750(3). The statute even requires the contractor to return, within 10 days from the owner's cancellation, any payments that the contractor received from the owner under the contract. ORS 83.740(1).

Given the potential downside of not providing the HSSA notice of right to cancel, residential repair and remodel contractors may want to err on the side of caution and include the notice to cut off the contractor's HSSA exposure, even if it is not certain that the contract will be subject to the HSSA. While that might result in giving the notice sometimes when not required, eliminating the risk on a larger scale may be worth it. Besides, if an owner decides to cancel the contract within three business days of signing (whether it has a statutory right or not), that is likely a red flag that performing the work for this owner would have been perilous anyway.

Contractors may be able to mitigate the effects of the potential cancellation by waiting until after the three-business day cancellation period ends before starting work or purchasing materials, assuming the contract allows for such delay.

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Provision in Washington's Construction Lien Law provides Important Protections to Lien Claimants against Coercive Acts of Others

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Most project developers and general contractors respect the right of a potential lien claimant to record a construction lien in order to protect their right to payment. Periodically, however, there are those who seek to put undue pressure on a potential lien claimant to not exercise their lien rights. For example, a developer may threaten to stop doing business with a contractor to try to prevent the contractor from recording a construction lien, or a contractor may threaten to terminate an ongoing business relationship with a subcontractor or supplier to try and prevent their recording of a construction lien.

Curt

In 1992, as part of the Washington legislature's amendments to many provisions of the Washington construction lien law, the legislature enacted a statute designed to deter persons from engaging in the above conduct and other similar coercive conduct. That statute, RCW 60.04.035, provides as follows:

> The legislature finds that acts of coercion or attempted coercion, including threats to withhold future contracts, made by a contractor or developer to discourage a contractor, subcontractor, or material or equipment supplier from giving an owner the notice of right to claim a lien required by RCW 60.04.031, or from filing a claim of lien under this chapter are matters vitally affecting the public interest for the purpose of applying the consumer protection act, chapter 19.86 RCW. These acts of coercion are not reasonable in relation to the development and preservation of business. These acts of coercion shall constitute an unfair or deceptive act or practice in trade or commerce for the purpose of applying the consumer protection act, chapter 19.86 RCW.

This statute appears to be unique to Washington. Although other states have consumer protection acts that impose liability for coercive conduct, there does not appear to be another state statute such as RCW 60.04.035 that relates specifically to coercive conduct in connection with construction liens.

The legislative history relating to the enactment of RCW 60.04.035 states that it was designed to protect from "intimidation and coercion". Final Bill Report, E.S.B. 6441, at 2, 52nd Leg., Reg. Sess. (Wash. 1992). The house bill report states that "[a] consumer protection violation is added to make acts of coercion against contractors and material suppliers unfair practices when the coercion is designed to discourage the filing of liens". House Bill Report, E.S.B. 6441, at 1, 52nd Leg., Reg. Sess. (Wash. 1992).

There is no indication in the available legislative history whether the impetus for proposing the statute was a case or cases in which there had been coercive conduct in relation to construction liens. Regardless, legislators obviously saw the danger of such conduct and acted to provide a remedy.

I. Interpretation of RCW 60.04.035

RCW 60.04.035 does not define the term "coercion" but that term is generally defined as "[c]ompulsion of a free agent by physical, moral, or economic force." *Black's Law Dictionary* (10th ed. 2014).

The statute lists an example of an act of coercion—the threat to withhold future contracts. The statute's language makes it clear that is just one example.

The one example set forth in the statute does help to shed light on other acts that courts would likely find to be coercive. For example, the act of a developer in threatening to withhold payments owed to a general contractor as retribution for recording a construction lien would most likely be held to be a violation of the statute.

RCW 60.04.035 prohibits attempted coercion as well as completed coercion. Thus, for example, if a contractor threatens a subcontractor in order to dissuade them from recording a construction lien, and the subcontractor records the lien despite the threat, the contractor may nevertheless be held liable under the statute for attempted coercion. The subcontractor would still need to prove damages however.

Also noteworthy is the fact that the statute not only prohibits coercion intended to prevent the recording of a construction lien, but also prohibits coercion intended to pressure the potential lien claimant into not providing a notice of right to claim a lien. As those familiar with the Washington lien law are aware, if a potential lien claimant is required under RCW 60.04.031 to provide a notice of right to claim a lien, but does not, they lose their lien rights. Thus, coercion that prevents the giving of a notice of right to claim a lien has the same effect as coercion that prevents the actual recording of a construction lien, and therefore gives rise to liability on the part of the offender.

There is so far no guidance from the courts regarding interpretation of RCW 60.04.035. As of this writing, there is not a reported case interpreting this statute.

II. Remedies for Violation of RCW 60.04.035

The Washington Consumer Protection Act, codified in RCW 19.86 ("Consumer Protection Act" or "Act") is an effective remedy because of significant financial effect on those who commit violations of its provisions.

Under the Consumer Protection Act, not only may the Washington Attorney General file suit to enforce the Act, but private parties are entitled to file suit under the Act. Remedies available to a private party are, in addition to the amount of their damages to compensate for their loss, treble damages up to an additional $25,000, and attorney fees the party has incurred in enforcing remedies under the Act. Further, a private party may sue to enjoin or restrain the offender from committing further violations of the Act.

Despite its name as the "Consumer Protection Act", the protections of the Act apply not only to individuals, but also to "corporations, trusts, unincorporated associations, and partnerships." RCW 19.86.010 (1).

Damages can be substantial for the violation of the Consumer Protection Act. For example, if a contractor coerced a subcontractor into not recording a lien that would have secured $100,000 of labor and materials, and the subcontractor could not collect payment because it did not record a lien, the subcontractor's damages against the contractor may be proven to be $100,000, plus treble damages of $25,000 (the maximum amount of treble damages), plus the subcontractor's reasonable attorney fees.

Other damages may be awarded depending on the circumstances. For example, should a developer follow through on a threat of withholding the awarding of a future contract to an otherwise qualified contractor, the contractor's damages, if proven, may include the lost profits from the contract that would have been awarded to the contractor on the other project.

The language of RCW 60.04.035 paves the way for a party to prove a violation of the Consumer Protection Act. Two of the elements for a violation of the Consumer Protection Act are an unfair or deceptive act, and that the act must occur in trade or commerce. The last sentence of RCW 60.04.035 addresses both of these elements, stating that acts of coercion under the statute constitute “an unfair or deceptive act or practice in trade or commerce for the purpose of applying the consumer protection act.”

A third element, and often a primary issue in proving claims under the Consumer Protection Act, is whether the conduct at issue is a matter that has an impact on the public interest. RCW 60.04.035 addresses this element, by expressly stating that a violation of RCW 60.04.035 is a “matter vitally affecting the public interest for the purpose of applying the consumer protection act, 19.86 RCW”.

Thus, once a violation of RCW 60.04.035 is proven, just two of the required five elements under the Consumer Protection Act are left to be proven—that the claimant suffered damage, and that the damage was caused by the violation.

A defense that is sometimes raised in response to a claim under the Consumer Protection Act is that the act or practice was reasonable in relation to the preservation and development of business. It is unlikely that a court would ever rule that an act of coercion is reasonable, but regardless, RCW 60.04.035 resolves any doubt on this issue—the statute expressly states that “[t]hese acts of coercion are not reasonable in relation to the development and preservation of business.”

III. Conclusion

Lien rights are valuable rights and the exercise of those rights must be free from coercion.

RCW 60.04.035 helps to compensate a potential lien claimant for the loss of lien rights due to coercion, but it is important to note that the remedies under RCW 60.04.035 are not a substitute for a lien. A potential lien claimant should never give up lien rights in response to coercive conduct of another.

Once lien rights are lost either because the potential lien claimant failed to provide a notice of right to lien if required to give that notice, or failed to record a lien within the 90-day period under RCW 60.04.091, those lien rights cannot be recovered. A lien claimant would not be able to recover lien rights by arguing to the court that they would have sent a required notice of right to lien or timely recorded their lien but for the coercive conduct of another.

Accordingly, if the potential lien claimant is faced with coercive conduct from a potentially liable party such as an owner or general contractor, the lien claimant should maintain their lien rights, and also strongly consider filing an action or claim against the offending party under RCW 60.04.035.

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OWNER’S / GC’S OPTIONS WHEN A SUBCONTRACTOR OR SUPPLIER RECORDS A LIEN

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When a lien is recorded against the real property upon which an improvement is being constructed, it usually results in an unhappy lender and property owner and, likely, a stern call from the property owner to the general contractor working on the subject project. The lender is displeased, of course, because the recorded lien puts its security interest in the collateral, *i.e.* the real property, at risk. This is especially true in Oregon where construction liens can have “super priority” over a previously recorded lender’s deed of trust. The recording of a construction lien against the owner’s property likely constitutes a technical

default of the terms of the owner's loan documents with the lender. The unhappy lender will usually demand that the owner address the lien or risk having its loan called. Likewise, the recording of a lien by a subcontractor or material supplier likely constitutes a breach by the general contractor of the terms of its contract with the owner. The owner, likely in response to pressure from its lender, demands that the general contractor remove the lien from the property. This chain of events is exactly why an aggrieved claimant records a lien.

Bill

Unfortunately, a claimant may record a lien of questionable validity in the hope the aforementioned friction between the owner, lender, and general contractor will result in a quick payment to the claimant. Understandably, an owner and/or general contractor (hereinafter "Respondent") do not want to pay off a bogus lien simply because they are being pressured to do so. So, what is a Respondent to do? The Respondent should (or at least can) do three things.

First, if no notice of intent to foreclose the lien has been received, under ORS 87.027, the Respondent can send a written demand to the lien claimant for a list of materials or equipment or description of labor or services supplied or a statement of the contractual basis for supplying the materials, equipment, services or labor, including the percentage of the contract completed, and the charge therefor to the date of the demand. If a notice of intent to foreclose has been received, under ORS 87.057(2), the Respondent can send a request to the claimant for a list of the materials and supplies with the charge therefor, or a statement of a contractual basis for the owner's obligation. If the claimant does not respond within the time lines set forth under each respective statute, 15 days (not including Saturdays, Sundays and other holidays) and 5 days respectively, the claimant is not entitled to recover attorney fees incurred in foreclosing its lien. The loss of the recovery of attorney fees is a powerful blow to a claimant's lien claim, especially if the amount of the lien claim is small.

The second action the Respondent can take is to send a written demand to the claimant under ORS 87.076(4) that it release the lien and stating that, if the lien is not released, the Respondent may recover the actual costs incurred in complying with ORS 87.076, ORS 87.078 and ORS 87.081 (the steps to bond around a lien) or the sum of $500, whichever is greater. Moreover, if the lien is not released within 10 days after such demand is delivered to the lien claimant and the lien claimant does not bring a suit to foreclose the lien within the time provided in ORS 87.055, the lien claimant is liable for the same damages. ORS 87.076(4). This can be a bit of counterpressure for the Respondent to apply to a claimant who files a questionable lien (that it does not intend to foreclose) in an attempt to leverage a quick settlement payment from Respondent.

Lastly, a Respondent may "bond around" a lien. This process, covered by ORS 87.076-87.081, removes the lien from the property and replaces the property with a bond or a cash deposit with the county treasurer in a sum equal to 150% of the lien amount. *See* also ORS 87.083(1) (release of property). This protects a lender's security and allows the property to be sold or refinanced. When a lien gets bonded around, the lien claimant knows the matter is not going to go away quickly. However, on the flip side, the lien claimant also knows it will be pursuing a designated pool of money rather than foreclosing and selling a property of unknown value.

Bonding around a lien consists of <u>three</u> steps – the recording of the bond/tender of payment, notice to the claimant of the bond recording/payment, and the recording of an affidavit that proper notice was given to the claimant. The failure to timely

comply with the second step of this process renders the bond/payment ineffective. ORS 87.078(2). There appears to be no case law regarding the impact of failing to properly record the affidavit. Under ORS 87.086, the claimant may petition the court challenging the adequacy of the bond for a reason other than the amount.

Now to reward those of you who hung in until the bitter end. As said above, under ORS 87.076(1), the required bond/cash deposit amount to bond around a lien is 150% of the lien claim amount. The 150% covers 100% of the lien claim amount with the additional 50% available to pay for attorney fees incurred in foreclosing the lien. ORS 87.060(5). So, on a small lien claim of say $12,000, the bond/cash deposit amount would be $18,000. That means a maximum of only $6,000 for attorney fees. If the Respondent has no other potential fee liability to the lien claimant, bonding around a lien can be a powerful disincentive for the claimant to foreclose its lien claim. It also negates the tail (the fee claim) wagging the dog (the lien amount) in settlement discussions. Conversely, the math works in the claimant's favor as the amount of the lien claim increases and, as a result, the amount available for attorney fees increases. This somewhat limits the owner's benefit of bonding around a lien. However, absent bonding around a lien, the claimant's attorney fee claim is uncapped (as is the owner's exposure thereto) and the fee claim will likely be paid in full so long as there are sufficient funds available from the foreclosure sale of the subject real property.

In addition, under ORS 87.076(3), "[a] person may file a bond or deposit money under subsection (1) or (2) of this section <u>at any time after the claim of lien is filed</u> under ORS 87.035." (Emphasis added). This statute can also have a devastating effect on lien claims, especially small ones. By way of example – opposing counsel has been aggressively litigating the above $12,000 lien claim with the expectation of recovering all of his/her fees, which counsel informs you are double the amount of the lien, from the impending judicial foreclosure. Just before the settlement conference, you have your client bond around the lien. Under ORS 87.076(1), counsel's fee claim should now be limited to $6,000 and his/her incentive to try the foreclosure claim has likely evaporated.

While the recording of lien claim with questionable validity is frustrating to an owner, lender, and/or general contractor, these parties are not without recourse. A savvy owner, lender or general contractor should consider all of the aforementioned proactive steps to respond to such a lien. Taking these steps could potentially limit the claimant's recovery and encourage an early and modest resolution of the claim.

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Potential First Amendment Protections for Disgruntled Bidders

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State and local governments must follow public bidding and procurement laws, including letting projects out for competitive bids, unless an exception applies.[5] Competitive bidding enables the contracting agency to identify and award the contract to the "lowest responsible bidder."[6] Normally, the contracting agency awards the contract to the lowest bidder, but there may be instances in which the contracting agency wishes to award the project to the second lowest bidder, particularly where the contracting agency views the lowest bidder as not "responsible." However, a contracting agency's belief that the lowest bidder as not "responsible" could be seen as retaliatory, exposing the agency to a First Amendment claim.

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[5] ORS 279C.300; ORS 279C.335(1).
[6] ORS 279C.375(1).

A "responsible" bidder is one that has "completed previous contracts of a similar nature with a satisfactory record of performance."[7]

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[A] satisfactory record of performance means that to the extent that the costs associated with and time available to perform a previous contract remained within the bidder's control, the bidder stayed within the time and budget allotted for the procurement and otherwise performed the contract in a satisfactory manner.[8]

If the contracting agency finds the bidder "is not responsible," the contracting agency must "document the bidder's record of performance."[9] This ensures the contracting agency's decision is not arbitrary, capricious, or based on unlawful grounds, but instead based on a record of past performance showing the bidder failed to stay on time and on budget when it was in the bidder's control to do so. Ideally, the agency makes its determination at the prequalification stage, allowing the potential bidder to appeal the agency's determination before it incurs the time and expense of preparing a bid.[10]

Overlaying the agency's determination, however, is the constitutional prohibition on retaliation for exercising First Amendment rights. Generally speaking, a contracting agency cannot retaliate against a contractor for engaging in protected speech activity. Thus, an agency cannot make its decision to award a contract based on the bidder's prior protected speech activity, which could include a prior lawsuit arising out of delay or payment claims.

In 1990, the United State Supreme Court held that a government entity's refusal to hire an employee for engaging in protected activity supports a claim for First Amendment retaliation.[11] Then, in 1996, the United States Supreme Court extended its First Amendment retaliation cause of action to contractors and regular providers of services.[12] In reaching its decision, the Supreme Court did "not address the possibility of suits by bidders or applicants for new government contracts"[13]

Picking up this queue, the Fifth Circuit recognized that a low bidder might have a cause of action for First Amendment retaliation where the contracting agency refuses to award the contract because the agency viewed the bidder as "lawsuit happy."[14] Since First Amendment rights have been afforded to individuals applying for government employment, bidders applying for "employment" with the government under a bidding arrangement should have no less protection.[15]

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[7] ORS 279C.375(3)(b)(H).
[8] *Id.*
[9] *Id.*
[10] ORS 279C.430.

[11] *Rutan v. Republican Party of Illinois,* 497 U.S. 62, 74 (1990).
[12] *Board of County Com'rs, Wabaunsee County, Kan. v. Umbehr*, 518 U.S. 668 (1996); *O'Hare Truck Service, Inc. v. City of Northlake*, 518 U.S. 712 (1996).
[13] 518 U.S. at 670.
[14] *Oscar Renda Contracting, Inc. v. City of Lubbock, Tex.,* 463 F.3d 378 (5th Cir. 2006) (holding that the First Amendment protects an independent contractor whose bid has been rejected by a city in retaliation for the contractor's exercise of freedom of speech, even if the contractor had no pre-existing commercial relationship with that city), *cert. denied* 127 S. Ct. 2033 (2007).
[15] *Id. See also Lucas v. Monroe Cty.,* 203 F.3d 964, 972–75 (6th Cir.2000) (extending *Umbehr* to tow operators on call with Sheriff's Department); *Del Valle Grp. v. Puerto Rico Ports Auth.,* 756 F Supp 2d 169, 181 (DPR 2010) (observing *Oscar Renda Contracting* as the "logical extension of previous Supreme Court rulings"); *The Yadin Co., Inc. v. City of Peoria,* CV-06-1317-PHX-PGR, 2007 WL 63611, at *4 (D Ariz Jan 8, 2007) (noting absence of 9th Circuit authority and following *Oscar Renda Contracting, supra.*);

For bidders to state a First Amendment retaliation claim, the bidder must allege (1) it suffered an adverse contract/employment decision; (2) its speech-activity involved a matter of public concern; (3) its interest in commenting on the matter of public concern outweighs the agency's interest in promoting efficiency; and (4) its speech-activity must have motivated the owner's adverse action.[16] Of course, even if a bidder can allege the elements, it may be difficult to prove the elements.[17]

In summary, while contracting agencies may consider a bidder's history of performance in determining whether the bidder is "responsible," it cannot retaliate against that bidder for engaging in prior protected speech activity.

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Heritage Constructors, Inc. v. City of Greenwood, Ark., CIV. 06-2183, 2008 WL 190457, at *3 (WD Ark Jan 18, 2008), *aff'd*, 545 F3d 599 (8th Cir 2008) (finding "an independent contractor bidding on a new contract, like an individual employment applicant, is protected by the First Amendment if its bid is rejected in retaliation for the exercise of protected activity" but holding the contractor's initiation of private arbitration seeking additional compensation on a prior project did not involve a matter of public concern).

[16] *Oscar Renda Contracting,* 463 F.3d at 382.

[17] *See Oscar Renda Contracting, Inc. v. City of Lubbock, Tex.*, 577 F.3d 264 (5th Cir. 2009) (affirming dismissal on summary judgment where bidder was unable to prove its prior lawsuit was the cause of the agency's refusal to award it a contract based on its low bid).

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