



# COMMON SENSE CONTRACTING

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## Challenging Past Performance Evaluations

**621** Currently, the federal government agencies use the “best value” selection process when making an award on a competitive basis. In that context, a

contractor’s past performance record can be a critical factor in the selection process. Consequently, any contractor performing work on a federal government project needs to appreciate the past performance evaluation process and develop a plan to avoid receiving a disappointing evaluation.

Notwithstanding a contractor’s best efforts, it may be necessary for a contractor to consider challenging an evaluation that is unjustified.

Two cases recently decided by the Court of Federal Claims (the “COFC”) and the Armed Services Board of Contract Appeals (the “ASBCA” or the “Board”) specifically addressed the COFC’s and the Board’s ability to review unjust or inaccurate past performance evaluations issued by the federal government. In *Todd Construction, L.P. v. United States*, 85 Fed. Cl. 34 (Dec. 9, 2008) and *Sundt Construction, Inc.*, ASBCA No. 56293, 09-1 BCA ¶ 34,084, both the COFC and the Board ruled that unfavorable past performance evaluations are capable of being challenged by contractors through a Contract Disputes Act (“CDA”) claim.

In the recent past, a contractor that received an unfavorable past performance evaluation from the federal government had little recourse beyond petitioning the agency to change the evaluation. When an agency refused to change the past performance evaluation, a contractor’s only means of appeal was to challenge the evaluation at

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Timothy W. (Tim) Johnson, former Vice-President at Coca-Cola Enterprises, has rejoined the firm as “Counsel” and will focus on labor, employment, and related issues for firm clients. A graduate of Texas Law School, Tim was originally an associate and partner here, and has been a labor and employment lawyer for over thirty years.

At Coke, he was the corporate officer and senior manager over labor and employee relations for their 72,000 employees and 500 facilities in the US and beyond. In that capacity, he devised the strategies, approaches, and measurements to insure that employment-related business risks were anticipated and well managed. He also oversaw all labor negotiations, union organizing issues, employee grievances, complaints, and unfair labor practice claims, including wage-hour, contract benefits, and safety issues.

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the COFC or at the Government Accountability Office (“GAO”) through a bid protest challenging a subsequent procurement that the contractor was competing for. However, the bid protest review of past performance evaluations was quite limited and oftentimes failed to provide contractors an adequate remedy from an unjust or inaccurate evaluation.

*Todd* and *Sundt* reflect departures from past precedent and permit a contractor to directly challenge an unfavorable past performance evaluation through a CDA claim in certain circumstances. Both of these cases signal a beneficial change in philosophy that will make it easier for contractors to challenge unfavorable past performance evaluations at either the COFC or the Board in the future.

#### Direct Challenge to a Rating

In the *Todd* case, the contractor (Todd Construction) provided roof repair services for the U.S. Army Corps of Engineers (the “Corps”). The Corps issued Todd Construction an unsatisfactory performance evaluation rating at the conclusion of the contract. Todd Construction promptly appealed the unsatisfactory rating to the contracting officer (“CO”) on the grounds that the government (1) violated applicable performance review procedures set forth in Corps regulations and (2) arbitrarily issued the unsatisfactory rating which was not supported by the facts of the contractor’s performance. The CO denied the appeal, and Todd Construction appealed the

CO’s denial to the COFC of Federal Claims through a CDA claim seeking judicial review of the unsatisfactory performance evaluation.

The government moved to dismiss Todd Construction’s claim alleging that the COFC did not have jurisdiction over a CDA claim challenging an unfavorable performance evaluation because such a challenge did not “arise from or relate to” the underlying contract, and therefore did not constitute a “claim” as defined by the CDA. The COFC rejected the government’s argument and found that a contractor’s challenge to an unfavorable performance evaluation did indeed constitute a viable claim under the CDA and that the COFC had jurisdiction over such a claim. In finding that jurisdiction existed over Todd Construction’s claim, the COFC relied on the plain language of the Tucker Act, 28 U.S.C. § 1491, the COFC’s general jurisdiction statute.

The Tucker Act states that the COFC has jurisdiction over “any claim by or against, or dispute with, a contractor arising under Section 10(a)(1) of the Contract Disputes Act of 1978, including . . . nonmonetary disputes on which a decision of the contracting officer has been issued. . . . The COFC latched onto this broad language in the Tucker Act and determined that Todd Construction’s challenge to its unfavorable performance evaluation constituted a “nonmonetary dispute” that the CO had issued a decision on. The court explained that it had jurisdiction over performance evaluation challenges and other nonmonetary claims under the CDA where:

- (1) a written demand or claim is submitted by a contractor to the CO;
- (2) the claim is made as a matter of right by the contractor;
- (3) the claim requests relief arising under or relating to the contract; and
- (4) the CO issued a decision denying the claim.

The COFC found that Todd Construction satisfied these four requirements. Specifically, the court found that Todd Construction’s claim was made as a “matter of right” because contractors are “entitled to an accurate and fair performance evaluation prepared in accordance with the [agency] regulations. . . . The court also found that Todd Construction’s performance evaluation arose under or related to the underlying contract between Todd Construction and the government because, “[a]s a matter of logic, a performance evaluation relates to the contractor’s performance under the contract in the same way that any evaluation relates to the thing evaluated.”

However, the *Todd* decision does not provide all the answers that contractors need to navigate this complex area of government contracts law. The COFC purposely failed to determine whether Todd Construction’s claims were meritorious and what type of relief the contractor would be entitled to if its claims were deemed to be meritorious. The court was reluctant to rule on the form of relief that Todd Construction might be entitled to because the state of the law in this area is unclear. In an effort to fully develop this issue, the court requested additional

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briefing from Todd Construction and the government on the following issues:

- Whether it is within the jurisdiction of the COFC to declare the past performance evaluation to be unlawful and to set aside or correct the evaluation;
- Whether the exercise of such authority by the COFC is appropriate in the case;
- Whether the COFC possesses the authority to remand the case to the agency if it were to declare the performance evaluation rating to be unlawful; and
- Whether the COFC possesses the injunctive authority to order the government to remove the performance evaluation from the CCASS database.

In sum, *Todd* is a favorable ruling for contractors in that it allows a direct challenge of an unjust or inaccurate past performance evaluation through a CDA action at the COFC. The *Todd* decision does not bring an end to the story as the COFC has yet to determine what relief can and should be granted where it finds that the government issued an unjust or inaccurate performance evaluation.

#### Enforcement of Agreed Revision to a Rating

Similar to the *Todd* case, the *Sundt* appeal involved a contractor that received an unfavorable past performance evaluation at the conclusion of its work performance. Sundt Construction received a marginal past performance evaluation from the U.S. Air Force even though the contractor claimed that it had an oral agreement with the Air Force which guaranteed it a satisfactory past performance evaluation if it withdrew \$300,000 worth of claims for equitable adjustments to the contract and completed its punch list responsibilities in a designated period of time. The Air Force denied that any such agreement had been reached between the parties and assigned Sundt Construction a marginal past performance evaluation when it appeared that the contractor was not proceeding quickly enough in closing out the contract.

Sundt Construction appealed the past performance evaluation to the CO claiming that it was entitled to a satisfactory rating under the terms of the oral agreement reached between the contractor and the Air Force. The CO rejected the claim and Sundt Construction appealed to the ASBCA under the CDA seeking a satisfactory past performance evaluation. The government moved to dismiss Sundt Construction's claim on the ground that the Board has consistently ruled that it lacked jurisdiction to decide appeals from unsatisfactory past performance evaluations where contract terms are not at issue.

The Board rejected the government's motion to dismiss and found that it had jurisdiction to evaluate Sundt Construction's claim for a satisfactory past performance evaluation. Although the Board chose to exercise jurisdiction over Sundt Construction's claim, it did so for reasons other than those addressed by the COFC in *Todd*. The Board explained that it had jurisdiction under the CDA "to determine the rights and obligations of the parties under disputed terms of a contract, which includes contract modifications and settlement agreements."

The Board found that because the administrative record reflected that an oral agreement between the parties did exist which guaranteed Sundt Construction a satisfactory past performance evaluation, the contractor's challenge to the marginal past performance evaluation constituted a challenge to its rights and obligations under the terms of the oral agreement between the parties. In other words, the Board found that it had jurisdiction over Sundt Construction's claims not because the claims involved a challenge to its past performance evaluation, but because the claims involved a challenge to the terms of the modified contract between the parties.

The ASBCA did not go as far in *Sundt* as the COFC of Federal Claims did in *Todd*. *Sundt* appears to limit jurisdiction at the Board to past performance evaluation challenges that involve a contractor's rights and obligations under the terms of the contract or any modifications to that contract. Where contract terms are not at issue in a past performance evaluation claim, it appears that the Board would decline to exercise jurisdiction over such a claim as it has done many times in the past. See e.g. *TLT Construction Corp.*, ASBCA No. 53769, 02-2 BCA ¶ 31,969; *CardioMetrix*, ASBCA No. 50897, 97-2 BCA ¶ 29,319. On the other hand, the COFC of Federal Claims has made it clear that it will continue to exercise jurisdiction over challenges to past performance evaluations as long as a contractor satisfies the general requirements of a CDA claim. However, neither the COFC nor the Board have provided any significant guidance to date regarding the type of relief that a contractor can expect if it is successful in challenging an unjust or inaccurate past performance evaluation.

#### Comment

While the potential for asserting a challenge to an unjust past performance evaluation at the COFC or one of the boards provides some measure of relief for a contractor, using the disputes process as a remedy should be viewed as the last option. Rather, contractors should make the achievement of an outstanding evaluation one of its priorities from the date of contract award. In that context, consider the following:

- If there is a pre-construction partnering meeting, advise all participants that the contractor intends to strive to achieve an outstanding rating.
- Make that achievement one of the contractor's stated goals.
- Attempt to engage the government's representative in a discussion of the various categories in order to gain insight regarding the practical application of the concepts evaluated in the report.
- Periodically address the past performance evaluation categories at project meetings with the government's representatives. Ask "How Are We Doing?".
- If there are positive comments or criticisms, undertake to address these and improve on them. Remember, the key is to avoid being surprised at the end of the project. If you can draw from others, information on their

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expectations or standards, it is more unlikely that new standards or expectations will be applied at the end of the project. If there are new or different standards applied, it should be easier to challenge an unjust evaluation if these practical steps have been followed throughout the project.

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## Final Payment Provisions

### 622 Introduction

Construction subcontracts frequently contain payment provisions that seek to allocate the risk of non-payment by the owner. Despite those provisions, disputes can, and frequently do, arise when an owner does not make payment to the contractor. Although those disputes cannot be avoided entirely, they can be minimized by clearly stated unambiguous payment provisions. Such carefully drafted provisions give the parties a roadmap to which to apply the facts of the case thus encouraging mutual resolution of issues or at least reducing the scope of disputes. Ambiguous language has the opposite effect, inviting disputes not only as to application of the facts to the contract, but also as to the meaning of the contract itself. In *Lobo Painting, Inc. v. Lamb Construction Company*, 231 S.W.2d 256 (Mo. App. 2007), the Missouri Court of Appeals held that resolution of conflicting testimony of parties by trial court was necessary in order to determine intent of ambiguous final payment provision.

### Background

Lamb Construction Co. (“Lamb”), a general contractor, entered into a subcontract with Lobo Painting, Inc. (“Lobo”) to paint a building, which Lamb was constructing. Lamb withheld final payment of retainage under the subcontract and Lobo filed suit. Lamb, in reliance upon the final payment provision in the subcontract, asserted that it was not obligated to make final payment to Lobo because the owner was withholding final payment to it. The final payment provision at issue provided as follows:

Final payment, constituting the entire unpaid balance of the Subcontract Sum, shall be made by the Contractor to the Subcontractor when the Subcontractor’s Work is fully performed in accordance with the requirements of the Subcontract Documents, the Architect has issued a certificate for payment covering the Subcontractor’s completed Work and the Contractor has received payment from the Owner. If, for any cause which is not the fault of the Subcontractor, a certificate for payment is not issued or the Contractor does not receive timely payment or does not pay the Subcontractor within three working days after receipt of payment from the Owner, final payment to the Subcontractor shall be made upon demand.

The trial court found in favor of Lamb and, based upon this provision, dismissed Lobo’s claim. Lobo then appealed, arguing that the final payment provision was ambiguous and, therefore, was not a condition precedent to the contractor’s obligation to make payment to it.

### Court’s Analysis

The Missouri Court of Appeals began its analysis by recounting the rules of contract interpretation, stating that its function was to ascertain the parties’ intent. Where the language in a contract is unambiguous, a court will not look beyond the plain meaning of the contract to determine that intent. Where there is an ambiguity in the contract, on the other hand, the court may refer to matters beyond the document itself, including testimony, in order to determine the parties’ intent. The court stated that an ambiguity exists where the terms of a contract are “susceptible of more than one meaning so that reasonable persons may fairly and honestly differ in their construction of its terms.”

The appellate court held that the final payment provision at issue in this case was ambiguous because its second sentence could reasonably be interpreted to have different meanings. The court held that the clause “for any cause which is not the fault of the Subcontractor” could be read either to apply only to the immediately following condition, “a certificate for payment is not issued,” or to apply also to the other two conditions, “Contractor does not receive timely payment or does not pay the Subcontractor within three working days after receipt of payment from the Owner,” as well. Under the former reading, the court would only need to determine whether Lobo was at fault for a certificate of payment not being issued. If a certificate for payment was issued and either of the other conditions occurred, final payment would be due upon demand, regardless of which party was to blame. Under the latter reading of the clause, on the other hand, the court would also be required to determine whether Lobo was at fault for either the owner’s nonpayment to Lamb or Lamb’s delay in paying Lobo and payment would not be due on demand if it was. Therefore, the court held that it could review extrinsic evidence in order to determine the parties’ intent.

The court reviewed the testimony given at trial by the parties regarding the operation of the final payment clause. The testimony was in conflict and the appellate court stated that the ambiguity in the final payment provision could not be resolved without resolving that conflicting testimony. The trial court had found the final payment provision to be unambiguous and had not examined the conflict in the testimony regarding the meaning of that provision. Thus, the appellate court remanded the case to the trial court to determine the parties’ intent.

### Comment

This case illustrates the importance of careful drafting of contracts. It is possible that the intent of the provision at issue in this case is that the modifier regarding fault on the part of the subcontractor applied to all three conditions. Any other reading would seem inconsistent with the first sentence of the provision providing, among other

things, that final payment “shall be made by the Contractor to the Subcontractor when . . . the Architect has issued a certificate for payment covering the Subcontractor’s completed work and the Contractor has received payment from the Owner.” However, because of the way the sentence was structured, the appellate court, reading the second sentence alone, outside of any context provided by the first, was able to describe an ambiguity in its phrasing. This ambiguity, once found, allowed testimony to be heard regarding the parties’ intended meaning of the provision, thus increasing the expense of dispute resolution and removing the certainty of the result. Carefully drafted contract language that clearly stated the parties’ agreement could have avoided both of these problems.

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## Risk Shifting Clauses: Is a Trend Emerging?

**623** In Article 601 in our Fall 2008 newsletter, we discussed recent court decisions in Georgia, North Carolina, and Arizona pertaining to the enforceability of contract clauses attempting to limit one party’s liability in light of state anti-indemnity statutes. Since then, two more similar decisions have been issued. These recent decisions, as well as those previously discussed, are informative because they explain key distinctions in these contractual “risk shifting” provisions.

The courts’ analyses and explanations should aid the construction professional in understanding how states may differ in their interpretation of these contractual risk shifting clauses, and should help guide in the drafting of “risk shifting” provisions, such as limitation of liability and indemnification clauses. These decisions further show that some courts appear willing to strike a balance between the contracting parties’ rights to allocate risks amongst themselves and public policy seeking to avoid too much allocation of risk to one party, perhaps indicating a trend that bears watching.

### Arizona’s Analysis

In *1800 Ocotillo, LLC v. WLB Group, Inc.*, 196 P.3d 222 (Ariz. 2008) (“Ocotillo”), the Arizona Supreme Court upheld both the trial court and the court of appeals’ finding that a contractual limitation of liability provision did not violate Arizona’s stated public policy against broad form indemnification.

In *Ocotillo*, a property owner contracted with a surveyor to perform a boundary survey in anticipation of building a residential development. A boundary dispute arose and the owner claimed damages against the surveyor for construction delays and increased design and survey costs resulting from the negligently prepared survey. The written contract between the owner and the surveyor contained a contractual limitation of liability clause in which the parties agreed that the surveyor’s liability related

to services rendered to the owner “and to all persons having contractual relationships with them, resulting from any negligent acts, errors and/or omissions” of the surveyor would be limited to the total fees paid by the owner to the surveyor. The owner’s damages exceeded the fees paid to the surveyor.

The applicable Arizona anti-indemnity statute provided:

A covenant, clause or understanding in, collateral to or affecting a construction contract or architect-engineer professional service contract that purports to indemnify, to hold harmless or to defend the promisee from or against liability for loss or damage resulting from the sole negligence of the promisee or the promisee’s agents, employees or indemnitee is against the public policy of this state and is void.

The *Ocotillo* court reasoned that the contractual limitation of liability provision did not run afoul of this statutory provision because the anti-indemnity statute, on its face, only extends to indemnification provisions that attempt to shift liability for one’s sole negligence. The court reasoned that the contract clause at issue only limited (or shifted) liability for the design professional’s contract liability and, therefore, was not at odds with the statutory prohibition.

The *Ocotillo* court also distinguished its ruling from a seemingly contrary ruling penned by the Georgia Supreme Court in *Lanier at McEver, L.P. v. Planners & Engineers Collaborative, Inc.*, 663 S.E. 2d 240 (Ga. 2008) (“Lanier”). In *Lanier* (previously discussed in our Fall, 2008 newsletter), the Georgia Supreme Court held that a contractual limitation of liability clause somewhat similar to the one in *Ocotillo*, violated Georgia’s comparable anti-indemnity statute. The *Ocotillo* court distinguished its ruling from the *Lanier* ruling by contrasting the two contract provisions. The *Lanier* contract clause included a similar liability cap tied to amounts paid to the design professional, but it also stated that this liability cap included claims brought by third parties—that is, persons who were not parties to the underlying contract. The contract clause at issue in *Ocotillo* only capped liability for “contract” claims.

### New York’s Analysis

Similarly, in *Brooks v. Judlau Contracting*, 898 N.E. 2d 549 (N.Y. 2008) (“Brooks”), the Court of Appeals of New York was asked to determine whether a contractual indemnification provision between a general contractor and subcontractor violated New York’s anti-indemnity statute. *Brooks* takes up a slightly different, but all too familiar battle—the conflict between a general indemnification clause in a general contractor/subcontractor arrangement and an anti-indemnity statute. In *Brooks*, an ironworker employed by a subcontractor, was injured on a highway construction project, having fallen after grabbing onto a perimeter safety cable that came loose. The injured ironworker sued the general contractor, Judlau Contracting, claiming that it had improperly installed the safety cable. The general contractor then sued the subcontractor/employer, under the

subcontract's general indemnification clause. The trial court dismissed the general contractor's complaint against the subcontractor on grounds that the contractual indemnification clause violated New York's anti-indemnity statute, and this decision was later affirmed by another New York appellate court.

This contract's general indemnity provision required the subcontractor to, "*to the fullest extent permitted by law*, hold the [general contractor] harmless from all liability, costs, damages, attorneys' fees, and expenses from any claims or causes of action of whatever nature arising from the Subcontractor's work ...." (Emphasis added). New York's anti-indemnity statute, which is much broader than Arizona's, states in pertinent part:

A covenant, promise, agreement or understanding in, or in connection with ... a contract or agreement relative to the construction, alteration, repair or maintenance of a building ... purporting to indemnify or hold harmless the promisee against liability for damage arising out of bodily injury to persons or damage to property contributed to, caused by or resulting from the negligence of the promisee, his agents or employees, or indemnitee, whether such negligence be in whole or in part, is against public policy and is void and unenforceable.

In overturning the lower courts' rulings, New York's highest appellate court found that the contractual indemnification provision did not violate the anti-indemnity statute. The court reasoned that, while the general contractor could not seek indemnification from the subcontractor for its own negligent acts without violating public policy, the general contractor could still seek indemnification for the subcontractor's negligent acts. Based upon a detailed analysis of the subcontract language, "To the fullest extent permitted by law," the *Brooks*' decision limited the scope of the indemnification clause such that the contractor could seek indemnification from the subcontractor's negligent acts.

#### Comment

The reader should take away two key points from these cases about the enforceability of construction contracts indemnity clauses. First, *Brooks* decision shows that enforceability of a construction indemnity clause depends on whether governing state law has an anti-indemnity law. As parties in the construction industry may have contracts in several states, it might be impossible to use a single, enforceable anti-indemnity clause, because laws vary from state to state.

Second, the language of the governing state law may be decisive. The importance of statutory language is compounded by the fact that different states regulate indemnity clauses differently. Many states, such as Georgia (*See* O.C.G.A. § 13-8-2), prohibit contract indemnity clauses that allow a party to be indemnified for its own negligence or misconduct. Other states, such as North Carolina (*See* N.C. Gen. Stat. 22B-1), prohibit indemnity clauses as a general matter, but allow each party to accept liability for its own negligence. Finally, several states have enacted statutes that reflect individual policies and considerations

deemed uniquely important in those states. Florida, for example, prohibits indemnity contract clauses generally, but creates its own set of exceptions allowing enforcement of indemnity agreements. (*See* Fla. Stat. Ann. § 725.06(2).) The same or similar results might be reached in all of these states, but the contract language used may have to be different from state to state. Thus, the enforceability of an indemnity clause depends on specific language in the statute (if any) of the state whose law governs.

The *Brooks* case suggests that some of the obstacles to enforcement of an indemnity clause may be overcome by an indemnity clause that applies "to the fullest extent of, but no farther than, the indemnity allowed by state law". In the end, however, to insure a valid indemnity clause for use in a particular state may require knowledge of both the law of the state that will apply and the language of the clause that is employed in the contract. It is essential for any contractor or subcontractor to know and understand that the law varies from state to state on the extent to which contractual risk shifting provisions may be deemed enforceable. Therefore, the prudent contractor or professional must understand the laws of the state in which it will be contracting for, and performing, work when developing, or attempting to enforce, such contractual provisions.

Second, and more generally, a trend appears to be emerging in the courts. Broad contractual limitation clauses attempting to avoid liability for claims coming from "non-contracting" parties (*i.e.*, third parties), and broad indemnification clauses attempting to require the indemnitor to assume liability for the indemnitee's negligent acts, appear to be disfavored. As such, they will probably not be enforced when challenged. With this understanding, the prudent construction professional would be wise to review and, possibly, revise his contractual risk shifting clauses to account for these restrictions and, hopefully, avoid being faced with unenforceable contract provisions.

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## Construction Professionals' Personal Liability

**624** Construction professionals should be familiar with the application of liability on behalf of a corporation or firm that fails to provide services within industry standards. In contrast, construction professionals may not be familiar with the fact that they can be held *personally* liable when they fail to exercise a reasonable degree of care, skill, and ability as ordinarily employed by

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others within the profession. This article examines a recent Georgia decision that held a project manager *personally* liable for negligent acts taken in the course and scope of his employment in overseeing office renovations.

In *Schofield Interior Contractors, Inc. v. Standard Building Company, Inc.*, 668 S.E. 2d 316 (Ga. Ct. App. 2008) Schofield sued a project management firm and that firm's employee individually. Schofield maintained that the employee owed a duty to ensure that construction was performed in accordance with industry standards, which he breached, and that this duty was independent of any contractual duty. The trial court dismissed the claim against the employee without explanation, which Schofield appealed. Upon appeal, the defendants argued that plaintiffs could not maintain a negligence action against the employee individually for two reasons: (1) the allegations against the employee arose only out of his obligation as an employee of the project management firm to supervise the work and (2) the allegations therefore, asserted only the failure of a contractual obligation.

The Georgia Court of Appeals rejected the defendant's arguments. That court noted that a negligent construction claim, as asserted by Schofield, arises not from a breach of contract, but from a breach of a duty implied by law to perform the work in accordance with industry standards. Therefore, the claim against the project manager arose in tort and thus, existed independently of any claim for breach of contract.

Although the court found that individual liability was based on principles of tort, the court noted that, as a general rule, there is implied in every contract for work or services, a duty to perform it skillfully, carefully, diligently, and in workmanlike manner. Accordingly, the court held that the law imposes upon building contractors (and others performing skilled services) the obligation to exercise a reasonable degree of care, skill, and ability. This "standard of care" is measured against the degree of care exercised by others of the same profession under similar conditions and circumstances.

In the end, the court relied upon a contractual standard of care to impose an independent duty on construction professionals supervising the work. Specifically, the court held that the project manager was obligated to exercise a standard of care in the supervision of the work. Consequently, Schofield stated a claim for relief against the project manager when it alleged that the project manager "demonstrated a lack of knowledge of the construction trade and performed his duties and responsibilities at the job site in a negligent manner" and listed several specific acts of negligence.

After determining that Schofield had stated a viable claim for negligent supervision, the court focused on whether the project manager could be held personally liable for actions taken in the course and scope of his employment. The court observed that "a servant, as a wrongdoer, is liable individually for a tort committed within the scope of his master's business." As applied to the project manager, the project manager thus had a duty

to perform the supervision of the construction work skillfully, carefully, diligently, and in a workmanlike manner. Schofield could therefore, sue the project manager personally as well as the project management firm for the project manager's breach of this duty and failure to supervise the work properly.

#### Comment

Georgia is not alone in attributing personal liability for negligence upon construction professionals. Other jurisdictions have found corporate officers liable for negligent supervision and misfeasance. In the face of personal liability (both civil and criminal), the need to exercise reasonable care and conform to industry standards extends beyond a construction professional's contractual obligations. Employees of construction management firms who undertake contractual obligations or even supervise performance of the contractual obligations must exercise reasonable care and ensure they conform with industry standards. Otherwise, they may be personally liable.

Likewise, civil liability may be the least of a construction professional's worries. As examined in our newsletter, New York City prosecutors obtained criminal indictments against several contractor personnel arising out of two separate construction-site safety incidents. See "Criminal Prosecutions for Site-Safety Violations," Article 614, *Common Sense Contracting* (Spring 2009). Thus, a prudent construction professional must always exercise reasonable care, and should be warned that his failure to do so may not only lead to individual civil liability, but also criminal liability.

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## The Project Labor Agreement Is Back!

**625** The Project Labor Agreement is back. A project labor agreement is a pre-hire agreement with a labor organization establishing the terms and conditions of employment for a specific construction project. On February 6, 2009, President Obama signed Executive Order 13502 — "Use of Project Labor Agreements for Federal Construction Projects." The order encourages, but does not require, the use of project labor agreements on "large-scale construction projects" — defined as projects where the total cost to the federal government is \$25 million or more.

By way of background, in 1997, President Clinton issued a memorandum to executive agencies authorizing the use of project labor agreements on federal construction projects valued at \$5 million or more. Congress, controlled at that time by Republicans, countered by introducing legislation to ban federally mandated project labor agreements. In 2001, President Bush resolved the debate for the duration of his administration by issuing an executive order prohibiting federal agencies from requiring bidders on construction projects to adhere to contracts

with one or more unions.

The Federal Acquisition Regulation Councils have not yet issued regulations implementing the newest executive order. However, the construction industry should expect the use of project labor agreements on federal construction projects in the latter months of 2009. Private and local government projects may also be impacted by the new federal policy encouraging project labor agreements. Generally, such project agreements are neither totally prohibited nor absolutely permitted for state projects governed by competitive bidding requirements. Often however, a finding has to be made to justify use of a project labor agreement (i.e. cost savings, prevent labor unrest, resolve trade disputes, importance of timely completion and need to avoid strikes, lock-outs, etc.).

Many states have right to work laws. Project labor agreements in right to work states cannot discriminate against non-union contractors and cannot require employees to join a union as a condition of employment. Nonetheless, project labor agreements are valid, if properly designed, for projects in right to work states. Traditional non-union contractors may be required to sign project labor agreements as a condition to performing work.

For the non-union contractors, signing a project labor agreement means unions will be representing your employees and the terms and conditions of work will be determined by the agreement (or a referenced and incorporated collective bargaining agreement). Most project labor agreements require the use of union hiring halls for the source of all project employees. Finally, project labor agreements may require even non-union contractors to make contributions to the union benefit and pension funds for each employee.

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## Be Very Clear When Incorporating by Reference

**626** When incorporating by reference extrinsic materials into a contract, parties should clearly and explicitly identify the materials they want incorporated. Vague references simply are not good enough. Courts will not stretch contractual interpretations to find the materials incorporated by reference into a contract if the parties' intent is not clear. *Northrop Grumman Information Technology, Inc. v. U.S.*, 535 F.3d 1339 (Fed. Cir. 2008).

### Factual Background

Logicon, Inc., (now, Northrop Grumman Information Technology, Inc. ("Northrop")) acted as a middleman between a software developer and the U.S. Army. The software developer, Starburst Software, created a software program designed to minimize the bandwidth required to

send data over a network to multiple recipients. Starburst made a marketing call to an Army employee to pitch the software. The Army employee thought the software would increase efficiency in communications between different Army computer systems, and agreed to license the software. Starburst did not have an existing contract with the Army, and the Army employee was not a contracting officer authorized to bind the government. The parties did not sign a contract, but rather decided to use a pre-existing contract between Northrop and the Air Force to effect the lease.

Under the plan, Starburst would sell the software to Northrop, and then Northrop would lease the software to the Air Force. The Army would receive the software, and then pay the Air Force for the lease payments. Because the Army employee could not enter into the contract, Northrop drafted a "Letter of Essential Need" to be signed by the Army employee. Northrop purportedly wanted the signed letter to prove the transaction would be worthwhile. The letter stated that the software was "essential to the operation of," and "integral to," certain Army computer systems. The Army signed the letter, and the Air Force issued the delivery order.

The delivery order provided for a base period of one month, then two successive one-year renewal terms, and a final purchase option for an additional fee. The delivery order incorporated certain leasing terms and conditions, which contained the following language:

*It is hereby mutually understood and agreed that as an inducement for Contractor entering into this Agreement, the Government has provided required information relative to the essential use of the software which includes, but is not limited to, a description of the currently identified applications to be supported and planned life-cycle operations for the leased software.*

The agreement also contained a clause setting forth conditions whereby the government would be relieved of its lease obligations. The Army paid through the first year, but quickly discovered the software did not work effectively with its computer systems. About the same time, Starburst announced it was being acquired by another software company and that there would be no more updates to the software. The Army decided not to renew the software license. Northrop sued the government for breach of contract, seeking the amount of money it would have received had the Army exercised the second renewal option and purchased the software at the end of the lease.

### The Breach of Contract Claim

The basis of Northrop's breach of contract claim was that the government breached a warranty that the software was essential, when, in fact, the Army acquired the software on a test basis. Northrop argued the letter stating the software was "essential to the operation of," and "integral to," the Army computer systems provided the warranty that was breached, and that that letter was incorporated by reference into the agreement through the above-referenced

language (“the Government has provided required information relative to the essential use of the software...”).

The Federal Circuit affirmed a finding by the Court of Federal Claims that the letter was not incorporated by reference. Recognizing a lack of authority regarding incorporation by reference in the government contracts context, the Federal Circuit turned to patent cases and other circuits in determining what standards, or guiding principles, should be used in determining whether a contract incorporates by reference extrinsic material. The court noted that no “magic words” were necessary to incorporate extrinsic material by reference. But parties could easily avoid litigating this issue by adopting widely-used and judicially-approved language, such as “is hereby incorporated by reference” or “is hereby incorporated as though fully set forth herein,” and followed by information sufficient and specific enough to clearly identify the document to be incorporated.

The court found that Northrop’s argument failed on two fronts. First, the court found that the agreement language that “the Government has provided required information relative to the essential use of the software” did not clearly and explicitly refer to the letter. Second, even if the language did refer to the letter, the language did not incorporate the letter. Simply stating that the Government had provided information did not incorporate that information into the agreement.

### Conclusion

If parties genuinely desire to incorporate by reference into an agreement certain extrinsic material, they should state those desires as explicitly and clearly as possible. Testing the judicial boundaries of what contract language will be sufficient to incorporate extrinsic material by reference is an expensive proposition. The Court surveyed opinions from different circuits where language was, and was not, sufficient to incorporate extrinsic material by reference. While there are no “magic words” necessary, why test the boundaries? The easiest and most effective way to incorporate by reference is to use widely-used phrases, like “is hereby incorporated by reference” or “is hereby incorporated as though fully set forth herein.” Finally, if there is extrinsic material to be incorporated by reference, then reference that material explicitly. Do not rely on all-encompassing or broad phrases in the hopes that the material will be incorporated by reference.

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## One Project - Multiple Claim Deadlines

**627** A reality of many construction projects of significant size is that there will be multiple claims that must be resolved, either amicably or by resort to the applicable disputes process. Contractors and subcon-

tractors need to be cognizant of potential statute of limitations issues when dealing with any claim. It is not unusual for a statute of limitations period to be triggered by the “completion of the work”, or the “acceptance of the project.” As evidenced by the Florida appellate court’s decision in *BDI Constr. Co. v. Hartford Fire Ins. Co.*, 995 So. 2d 576 (Fla. 3d 2008), a concept such as “acceptance of the project” can have different meanings on the same project. A contractor must appreciate this potential difference in its relationship with the owner as well as with its subcontractors or vendors and any sureties.

### *BDI v. Hartford* - Factual Background

In July 1998, BDI Construction Company (“BDI”) was engaged as a subcontractor on a public school project in Dade County, Florida. BDI entered into a sub-subcontract with E & F Contractors, Inc. (“E & F”) for the performance of the stucco and drywall work. E & F provided a performance bond from Hartford Fire Insurance Company (“Hartford”) for the project naming BDI as an obligee on the bond.

Asserting that it had completed its work under its contract with BDI in August 2000, E & F requested a release of retainage from BDI on September 15, 2000. BDI paid 100% of the retainage to E & F on February 15, 2001. The court decision is not clear as to whether the School Board ever accepted the project as the School Board had asserted that the project was not constructed in accordance with the contract documents.

On March 30, 2006, BDI filed a third-party complaint against E & F and Hartford based upon allegations that E & F had failed to properly perform its work. In response, Hartford filed a motion for summary judgment alleging that Florida’s five-year statute of limitations began to run on September 15, 2000, when the final payment was due E & F. Hartford alleged that it was never notified of any default by E & F prior to the litigation and that final payment was considered fulfillment of E & F’s duties under the subcontract. In response, BDI argued that the statute of limitations accrued when the entire project was completed and accepted by the School Board rather than the date E & F completed its work or received final payment.

The trial court granted summary judgment in favor of Hartford on the grounds that the contract referenced by the bond was not the contract for the entire project, but only the sub-subcontract for the completion of E & F’s portion of the project. Therefore the statute of limitations on an action arising out of the E & F contract with BDI had expired.

### Multiple Deadlines for Claims

On appeal, the only issue was when the applicable statute of limitations began to run because the parties agreed that the applicable statute of limitations was five years, as set forth in Section 95.11(2)(b), Florida Statutes. Relying upon the decision in *Federal Ins. Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119, 1121 (Fla. 1998), BDI argued that the statute of limitations had commenced running because the School Board had yet to

accept the project and that it never formally accepted E & F's work as complete. In the *Federal Ins.* decision, the Florida Supreme Court held that an action based on Section 95.11(2)(b), as it applies to an action on a performance bond, "accrues on the date of acceptance of the project as having been completed according to the term and conditions set out in the construction contract."

In the *BDI* decision, the appellate court noted that if BDI thought E & F's work was defective, there was nothing to prevent it from filing suit after February 15, 2001, when it made final payment to E & F. In the court's opinion, BDI presented no support for its assertion that it had not accepted E & F's work when it made the final payment to BDI.

The court in *BDI* also distinguished *Federal Ins.* because that case involved a dispute regarding alleged defective work between the owner and the surety for the general contractor. The court held that in context of a subcontract, when a contractor accepts the work of the subcontractor and pays in full for that work, the action accrued when the subcontractor finished its work. The *BDI* decision interpreted the language in *Federal Ins.* to the extent that the cause of action "accrues on the date of acceptance of the project as having been completed according to the term and conditions set out in the construction contract" to mean that the "project" is the subcontracted work, and the "construction contract" in this case was the sub-subcontract between BDI and E & F.. Thus, the court noted that when BDI accepted E & F's work as having been completed, without reservations, the statute of limitations commenced to run. Based on this analysis, the court held that the action of the performance bond became time barred on February 15, 2006 (five years after final payment was made to E & F).

### Practical Implications of *BDI* Decision

BDI ultimately missed the statute of limitations by 45 days and as a result lost all claims against the performance bond surety. There are several important lessons for Florida contractors in this decision.

- Every construction project is actually multiple projects for purposes of tracking the statute of limitations on claims among the various parties.
- Contractors, as well as subcontractors, will need to separately identify the date of "acceptance" of the work of each lower tier firm (subcontractor or vendor) and track the applicable statute of limitations.
- Final payment to a lower tier firm without documentation that the work has not been "accepted" may be deemed sufficient to trigger the start of a statute of limitations period.
- If a firm elects to make final payment or release retainage to a lower tier entity, that firm should consider whether there is clear documentation that the work or project has not been accepted by it.
- If the lower tier contract (purchase order) is bonded,

determine if the surety has been on notice of a potential claim in accordance with the bond and whether the contractor's rights have been adequately reserved.

- Finally, consider whether a tolling agreement on the running of the statute of limitations is enforceable and can be negotiated as an alternative to commencing litigation or arbitration.

This decision reinforces the importance for every contractor to have knowledgeable personnel on staff handling claims which are cognizant of statute of limitations issues. The tracking of claims becomes even more important once the physical construction on a project is completed.

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## Avoid Losing a Bid Protest Before It Begins

### 628 Introduction

Today's harsh economic climate and federal Recovery Act legislation allocating substantial funds for public projects are causing more and more contractors to turn to federal government contracts as potential revenue sources. Thus, contractors are increasingly exposed to the highly-regulated area of public procurement. In this area, the bid protest is an important tool that allows contractors to challenge agency conduct during the procurement process. Bid protests help ensure agencies adhere to applicable law in letting public contracts, which promotes competition and increases the likelihood that public funds are economically spent on the most responsive and responsible bidder. Given the importance of the bid protest, the purpose of this article is to remind contractors of two important general rules that, if not followed, will likely result in summary dismissal of what may be otherwise meritorious protests. First: no bid, no protest. Second: challenges to defective specifications are waived if not timely made before the bid submission deadline.

### No Bid, No Protest

In *Rex Service Corp. v. United States*, 448 F.3d 1305 (Fed. Cir. 2006), the United States Court of Appeals for the Federal Circuit reiterated the important principle that only *interested parties* have standing to maintain a bid protest. There, the court construed standing under 28 U.S.C. § 1491(b)(1), which provides that the United States Court of Federal Claims ("COFC") has jurisdiction to decide an action by an "interested party" objecting to (i) a federal agency's solicitation for bids or proposals; (ii) a proposed award or award of a contract; or (iii) any alleged violation of statute or regulation in connection with a procurement or a proposed procurement. The court identified a two-prong definition for determining who is an "interested party": (i) an actual or (ii) prospective bidder who possesses the requisite direct economic interest. Applying this

definition to a protesting contractor who failed to submit a bid, the court affirmed the Court of Federal Claims' dismissal for lack of jurisdiction. The protester could not satisfy the first prong of the definition: the facts established the protester "could have bid, but chose not to." Nor could the protester satisfy the second prong of the definition, which requires the protester to prove it had "a substantial chance of receiving the contract." The court noted that even if the substantive basis for the protest (deviation from the process specified in the solicitation) was valid, the protester's failure to bid eliminated any chance of securing the contract. This failure translated into a lack of the direct economic interest necessary for standing. Thus, the general rule: no bid, no protest.

### Challenges to Defective Specifications are Waived If Not Timely Made

In *Blue & Gold Fleet, L.P. v. United States*, 492 F.3d 1308 (Fed. Cir. 2007), the Federal Circuit adopted a "waiver rule" requiring that challenges to patently defective specifications under 28 U.S.C. § 1491(b) be made before the close of the bid submission process. If a challenge is not timely made, the waiver rule, true to its name, requires the court to hold the challenge waived. The court identified the following rationale for the rule:

In the absence of a waiver rule, a contractor with knowledge of a solicitation defect could choose to stay silent when submitting its first proposal. If its first proposal loses to another bidder, the contractor could then come forward with the defect to restart the bidding process, perhaps with increased knowledge of its competitors. A waiver rule thus prevents contractors from taking advantage of the government and other bidders, and avoids costly after-the-fact litigation.

*Id.* at 1314. Applying the waiver rule to the facts, the court held the protester's challenge that the specifications failed to require that proposals comply with a certain federal act constituted a challenge to the terms of the solicitation. The court ruled this challenge untimely and, therefore, waived because it was not made prior to the submission deadline. Thus, the general rule: challenges to defective specifications are waived if not timely made before the bid submission deadline.

### Possible Exceptions

With most general rules come exceptions. An exception to the "no bid, no protest" rule may exist where the agency has taken some action that effectively denies the protester the opportunity to compete or makes submission of a bid futile. For example, in *RhinoCorps Ltd. Co. v. United States*, 2009 WL 1362843 (Fed. Cl. May 15, 2009), the Court of Federal Claims distinguished *Rex Service Corp.* and determined the protester was an interested party even though it had not submitted a proposal. Unlike the protester in *Rex Service Corp.* who could have submitted a bid, the small business protester in *RhinoCorps* alleged that the government improperly pre-judged it incapable of satisfying the solicitation requirements, making a proposal futile. Additionally, although the protester in *RhinoCorps* did

not submit a proposal, it did protest the government's decision not to solicit a small business for the procurement at issue. This protest was pending when the solicitation was issued.

The Court of Federal Claims has also recently held the waiver rule "should be applied only in appropriate cases." *Labatt Food Service, Inc. v. United States*, 84 Fed. Cl. 50, 64 (Fed. Cl. 2008). In *Labatt Food Service*, the court refused to apply the waiver rule to a protester's challenge regarding the use of e-mail during the solicitation process. The facts established the agency permitted the use of e-mail throughout the solicitation process even though e-mail use was contrary to the solicitation specifications, and then, at the close of the solicitation process, refused to consider proposal revisions the protester transmitted to the agency by e-mail.

### Be Sensitive to Deadlines

Bid protests involving federal contracts may be protested in three different forums. Protests may be filed with the agency conducting the procurement ("agency protests"), with the Government Accountability Office ("GAO protests"), as well as the COFC. Each forum has advantages and disadvantages.

This article addressed two basic principles involving protests to the COFC. In addition, there are specific procedures and time frames governing both agency protests in FAR Subpart 33.1 and GAO protests in 4 C.F.R. Part 21. These need to be carefully evaluated and followed. Failure to adhere to the various deadlines may result in the summary dismissal of the protest without consideration of its merits. Since it may be possible to file protests on the same matter with the agency and the GAO and also file a court action at the COFC, the decision on the appropriate steps to protect a contractor's rights needs to be carefully considered and reviewed throughout the pendency of a protest.

Finally, protests involving programs administered by the U.S. Small Business Administration ("SBA") are subject to specific procedures and deadlines based upon the SBA program. Protests related to a firm's representation as a small business concern are governed by 13 CFR 121.1004. Protests related to a firm's disadvantaged business status are governed by 13 CFR 124, Subpart B. Protests involving a firm's status as a service-disabled veteran-owned small business are governed by 13 CFR 125.24 through 125.28.

Observation of the general rules discussed above will help ensure contractors do not lose bid protests before they begin. However, as almost every case is factually unique, contractors should retain legal counsel to examine the likelihood of success of any potential protest, even where one of these general rules has been violated and to help evaluate the protest options or forums available to a contractor.

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## Upcoming Seminars

**The Masters Institute in Construction Contracting**, Federal Publications, July 21, 2009, Hilton Head, South Carolina. *James F. Butler.*

**Federal Government Contracts, What's Different?** Independent Electrical Contractors Association of Atlanta, July 23, 2009, Atlanta, Georgia. *Thomas J. Kelleher, Joseph C. Staak.*

**FCILB Seminar**, Georgia Branch of the AGC, August 6-7, 2009, Atlanta, Georgia. *SCH Attorneys.*

**FCILB Seminar**, Alabama ABC, August 13-14, 2009, Birmingham, Alabama. *SCH Attorneys.*

**SCH Update Conference**, CAGC, September 16-17, 2009, Charlotte, North Carolina. *Robert J. Greene, Matthew E. Cox, H. Lee Falls, Mark S. Wierman, Thomas J. Kelleher, Philip L. Fortune, Philip E. Beck, Robert C. Chambers.*

**Legal Issues and Contract Clauses**, AGC's Construction Project Manager Course, October 8, 2009, Indianapolis, Indiana. *Philip E. Beck.*

**Construction Delay, Acceleration and Inefficiency Claims**, Federal Publications, October 20-21, 2009, Washington, D.C. *Steven L. Reed, Reginald M. Jones.*

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*This newsletter is intended to be a source of general information on new or current topics on construction law, government contracts and commercial law. It is not intended to render legal advice on specific problems. In assessing specific problems, advice and counsel should be sought from experienced professionals.*



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